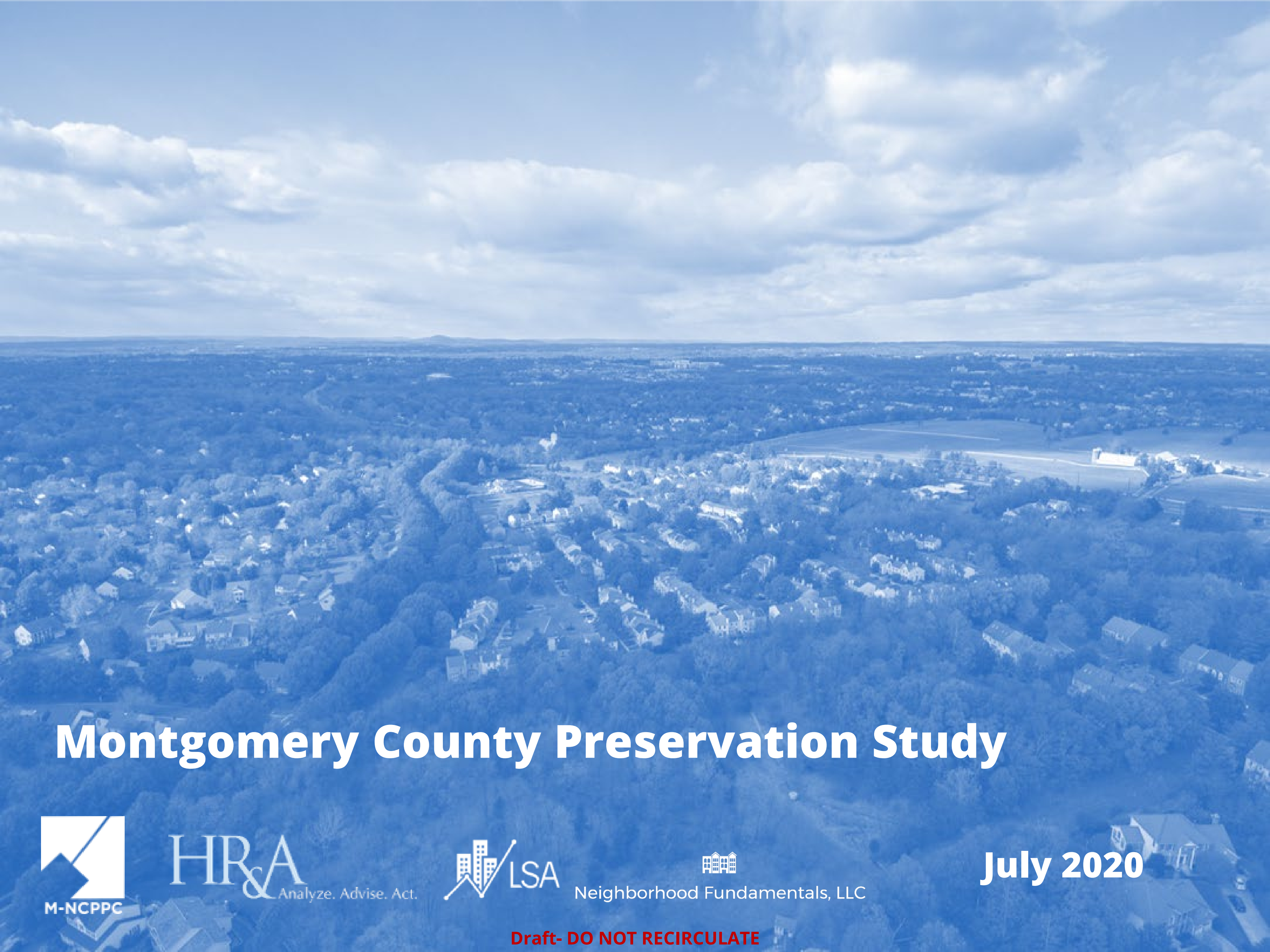

Montgomery County Preservation Study

M-NCPPC

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LSA

Neighborhood Fundamentals, LLC

July 2020

Draft- DO NOT RECIRCULATE

Contents

Executive Summary

Executive Summary

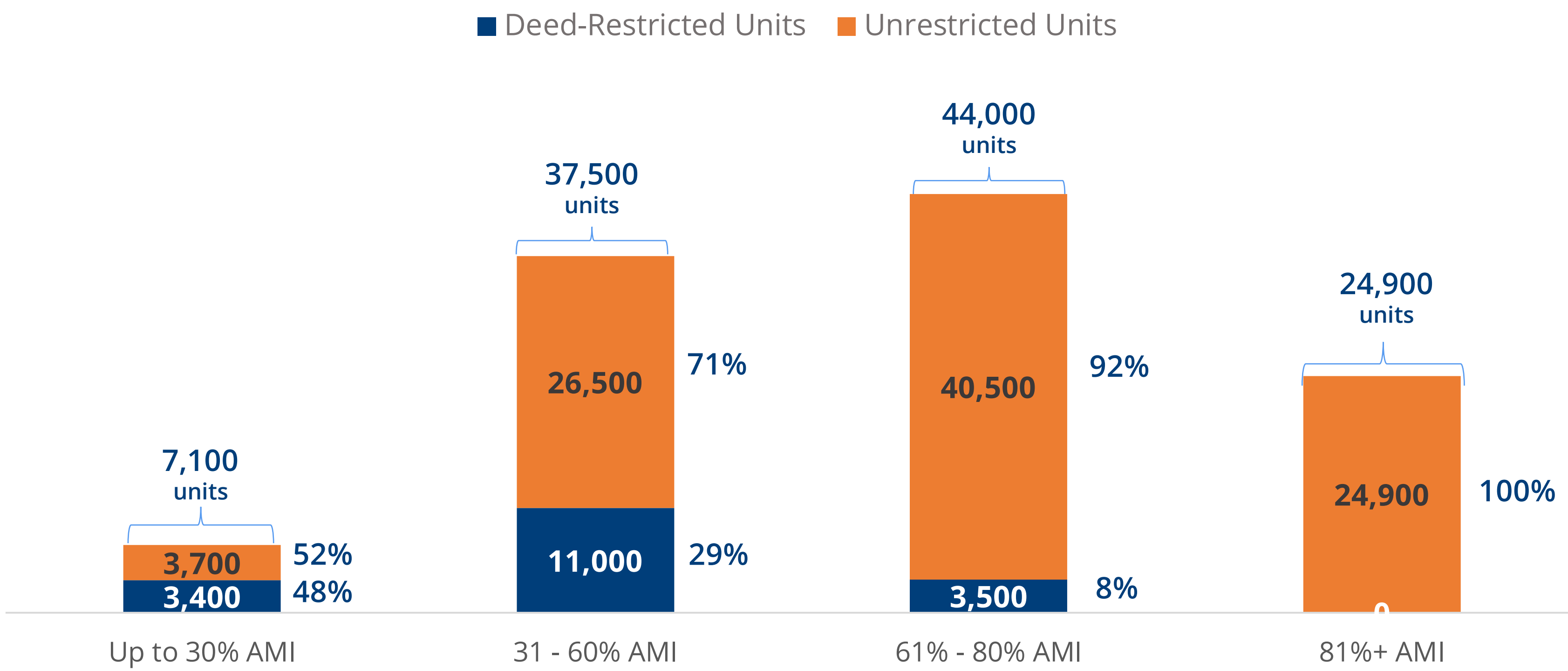
Preserving the existing inventory of affordable housing is an essential part of a comprehensive approach to address the housing affordability crisis in Montgomery County and retain affordably priced housing options for all residents.

This report provides a guiding framework for policy makers, stakeholders, and residents to understand Montgomery County's preservation challenges, current initiatives, and the strategies available to address them. Preservation is defined as any action that extends the deed-restricted status of an affordable rental housing unit or converts an unrestricted naturally occurring affordable housing (NOAH) unit to deed-restricted to ensure affordability remains in place. This study is organized around six questions:

Housing Landscape	• What are the characteristics of the County's deed-restricted and unrestricted housing stock? • How has the County's housing stock changed over time, and how will it look in the future?
Deed-restricted and Naturally-Occurring Affordable Housing	• How will the County's deed-restricted housing stock change over time? • What are the risk criteria for units losing affordability?
Preservation Framework	• Which existing and potential funding sources, policies, tools and programs are Montgomery County using currently? • How can the County support the preservation of affordable housing, to meet its housing goals?

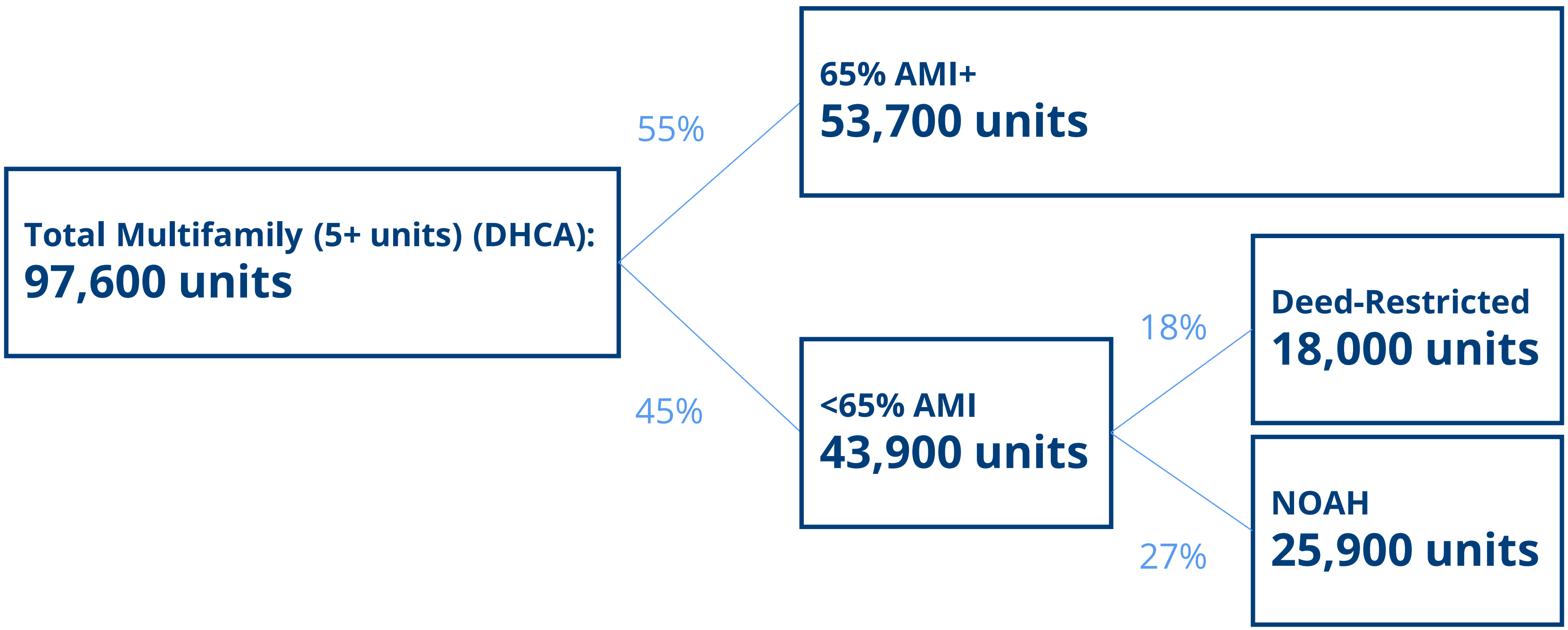
The plurality of the County's rental multifamily housing stock is affordable to households earning between 60% - 80% of AMI currently. Deed-restricted units make up 32% of units below 60% of AMI.

Multifamily Units by Affordability Level



Source: ACS 2018 1-year

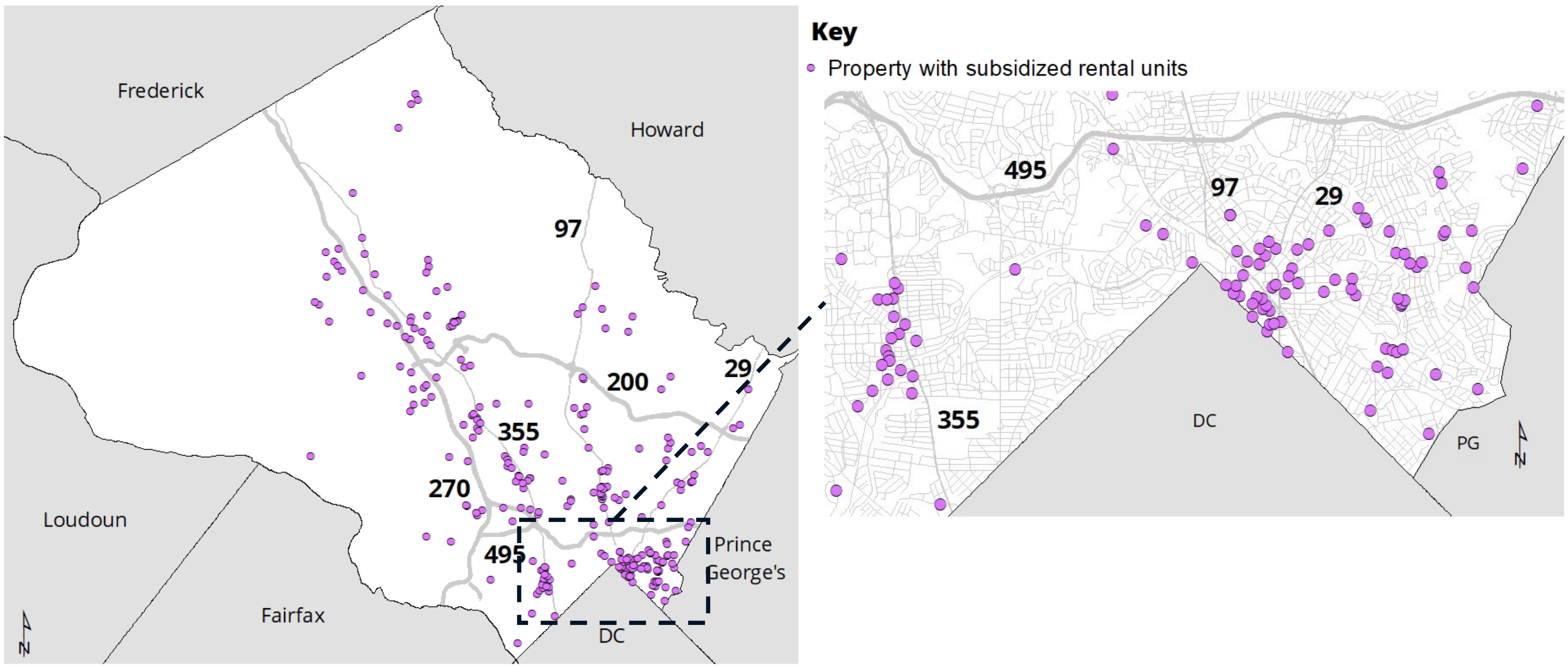
About 80% of the County's multifamily housing stock is unrestricted, or subject to market forces. 25,900 of these market-rate units rent for less than 65% of AMI and are classified as naturally occurring affordable housing (NOAH), comprising 27% of the total multifamily housing stock.



Sources: DHCA, ACS 2018 1-year

There are approximately 18,000 units in the County's deed-restricted rental housing inventory. While the units are spread out in many areas of the County, most of the units are in the more densely populated areas where multifamily housing is more prevalent.

Deed-Restricted Inventory (5+ units), 2020



Source: DHCA, NHPD, HUD

Executive Summary | Deed-Restricted Inventory Risk Criteria

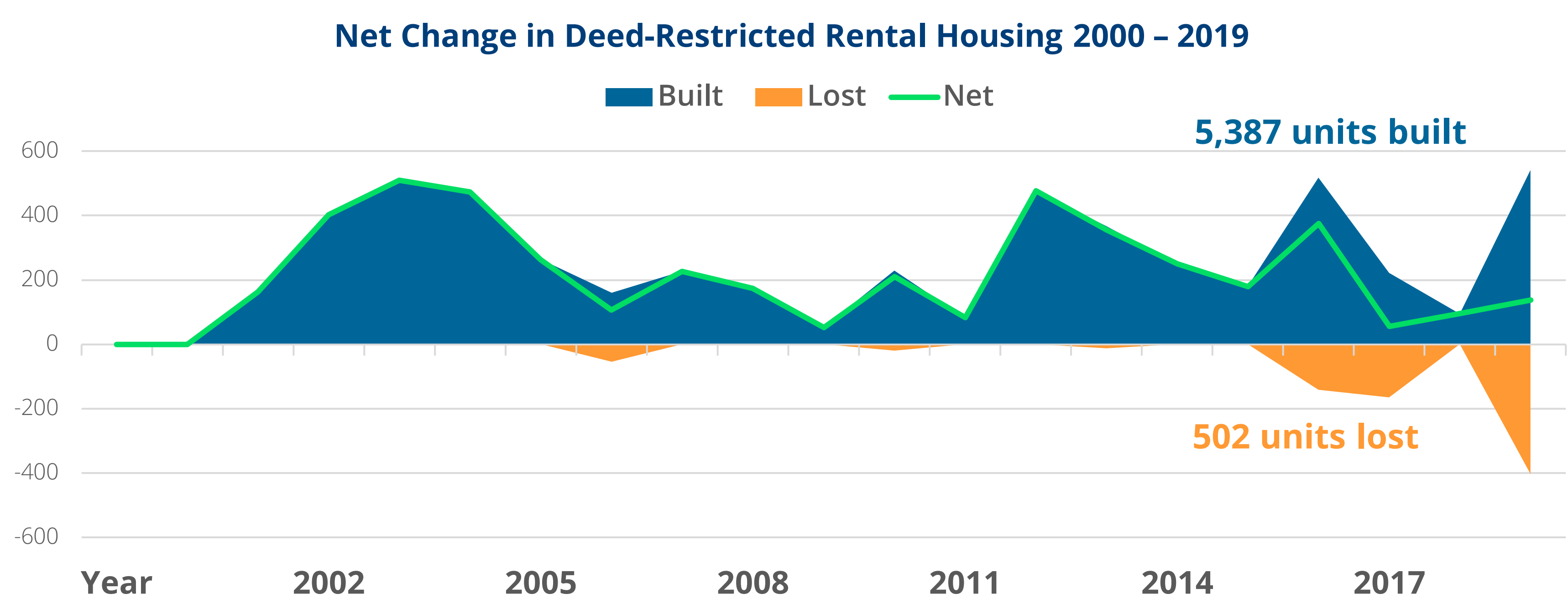
A set of risk criteria was applied to the deed-restricted rental housing inventory in Montgomery County to assess the level of affordability-loss risk across deed-restricted properties, and to identify high-risk deed-restricted properties.

Risk Criteria	Description
Upcoming subsidy expirations	Subsidy expirations set to occur in the 2020s and 2030s. Property owners with near-term expirations are more likely to explore options ahead of the expiration date, which could include new ownership, rehabilitation, renovation, and redevelopment, all of which could impact affordability.
Ownership type	For-profit ownership or non-profit ownership. Properties owned by for-profit entities are more likely to be lost from the deed-restricted rental stock once the subsidy compliance period ends. Properties that are owned by non-profit and mission-based entities are more likely to work with the County to find solutions to extend the affordability period to align with the goals, mission, and vision of their organizations.
Age of buildings	The age of a building can play a significant role in the decision-making process of apartment owners. Many of the decisions can directly impact affordability. Typically, if a building is 30 years or older, renovations, rehabilitation, and redevelopment become more common scenarios. Major investments into a property are more likely to trigger a rent increase and could therefore impact the affordability.
Proximity to transit	Properties near transit infrastructure are more likely to command higher market rents when subsidy expirations expire, and in some cases are more likely to be facing redevelopment pressures.
Rent trends in neighborhood	Deed-restricted rental properties located in neighborhoods with rising rent trends are more likely to lose affordability when the subsidy compliance period expires.
Income trends in community	Rising income levels in communities around deed-restricted rental properties could have an impact on market-rents, and therefore increase the possibility of rent increases when the subsidy compliance period expires.

Executive Summary | Deed-Restricted Inventory Loss and Gain

Overall, the County has been gaining deed-restricted rental housing stock at a faster rate than it is being lost. Since 2000, approximately 502 deed-restricted rental housing units have been lost from the inventory.

In 2000, the County began to implement preservation strategies for the deed-restricted rental housing stock that was at risk of being lost. A series of tools and policies have been used (often in tandem) over the years to effectively preserve deed-restricted rental housing in the County.



Source: *DHCA, NHPD, HUD, MD Dept. of Assessments and Taxation, Montgomery County Property Tax Records*

Executive Summary | Properties Most At-Risk

Based on the risk assessment, there are about 1,400 deed-restricted units that are the most at risk of losing affordability when their respective subsidy compliance periods expire over the next 2 decades. Notably, all these higher-risk units are affordable below 60% AMI, many of which are at or below 30% AMI.

2020s/2030s Subsidy Expirations, Higher-Risk Properties

									Census Tract Trends (2012 to 2017)	
Property Name	Subsidy Expiration	Subsidized Units	<30%	40% - 60%	60% - 80%	Rail Transit < 1 mile	Ownership Type	Building Age (Years)	Median Rent	Median HH Income
Heritage House	2021	100	100	0	0	Yes	For-Profit	39	13%	7%
Silver Spring House	2022	46	0	46	0	Yes	For-Profit	57	9%	1%
Lenox Park	2022	82	0	82	0	Yes	For-Profit	29	7%	1%
Sligo House Apartments	2024	50	0	50	0	Yes	For-Profit	61	9%	1%
Croydon Manor	2027	96	0	96	0	Yes	For-Profit	71	7%	11%
Fields At Bethesda	2029	369	0	369	0	Yes	For-Profit	67	9%	-3%
Franklin Apartments	2030	185	185	0	0	Yes	For-Profit	65	16%	26%
Fields Of Gaithersburg	2031	168	0	168	0	No	For-Profit	46	20%	15%
Barrington Apartments	2037	310	125	185	0	Yes	For-Profit	68	24%	-4%

Source: DHCA, NHPD, HUD, MD Dept. of Assessments and Taxation, Montgomery County Property Tax Records, Census Bureau 5-Year ACS

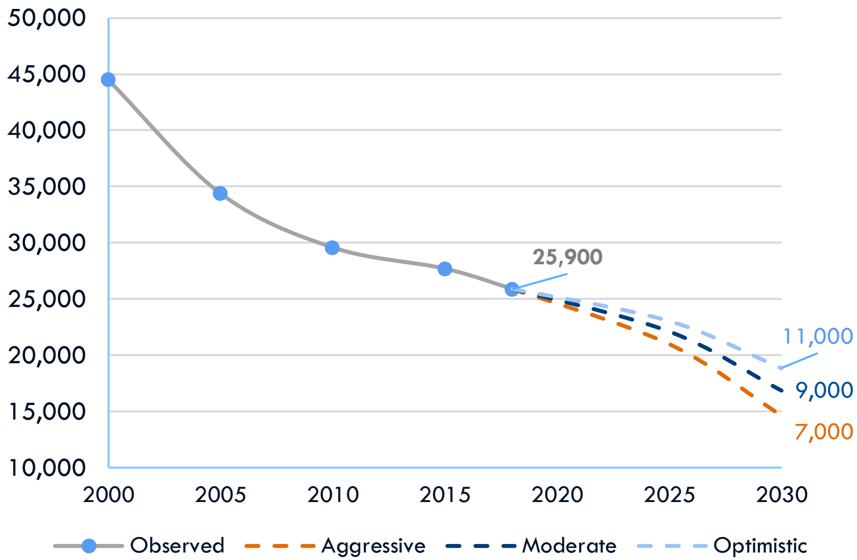
Based on our findings, proximity to transit, building size, income trends, and building age are the greatest risk indicators for NOAH units to lose affordability.

Risk Factor	
Building Age	While we did not find a linear relationship, we found that older units built between the 1960s and 1970s have the greatest risk for redevelopment or increase in prices as the neighborhood around them shifts.
Building Size	Smaller buildings are more likely to be affordable, but are losing affordability rapidly as 5 – 9 unit buildings are sold to larger investors. Larger properties that are affordable are most likely to be deed-restricted.
Proximity to Transit	Proximity to transit and new infrastructure is the strongest indicator for increase in assessment land values and rents, although jurisdictional zoning and transit access (not just proximity) remain key confounding variables.
Renovation	Although a large capital investment suggests an increase in future revenue, the data remains unclear on the quantitative effect on rents in Montgomery County. More longitudinal data may be required to assess long-term impacts.
Property Transfers	Property transfers and sales are a lagging indicator of NOAH risk—as investors see increasing rents, more transfer activity occurs.
Income Trends	While the analysis considered multiple demographic trends, changes in tract-level income shows the greatest risk of NOAH loss.
Owner Type	Consistent with findings around building size, larger property owners (with 10+) units tend to own properties at risk of loss.

Sources: DHCA, ACS 2018 1-year

Based on these criteria, we forecast a loss of NOAH between 7,000 – 11,000 units by 2030.

Properties classified as NOAH 2000 – 2030 (forecast)



Using the weighted averages of the independent analyses, we forecast a loss of 7,000 – 11,000 NOAH units by 2030. These losses are estimated to be in the following typologies, categorized by decade built and size of building.

Common NOAH Typologies by Category

Typology	Total Units <65% AMI	Median Rent 2018	Annual rent Growth (2010 - 2018)
1970s - 1980s 10 - 19 unit	5,080	$1,583	0.78%
1960s - 1970s 50+ unit	4,046	$1,571	0.56%
1990s - 2000s 10 - 19 unit	2,342	$1,671	0.18%
1960s - 1980s 5- 9 unit	3,817	$1,698	0.66%
1950s - 1960s 10 - 19 unit	2,493	$1,513	1.14%
2000s 50+ unit	917	$2,122	0.34%
1980s - 1990s 50+ unit	1,662	$1,800	0.17%
Total	**20,357**		

Sources: DHCA, ACS 2018 1-year

Preservation Framework| Unit Loss

There are four key ways in which a housing unit can be lost from the affordable stock. Each has different implications for how we approach preservation.

Physical Deterioration	As a NOAH or deed-restricted affordable property ages, there is insufficient investment in the property to maintain habitability, and the property is eventually removed from the building stock. This can result from insufficient cash flow from operations, poor management and/or intentional neglect.
Erosion of affordability via rent increase	If rents in NOAH properties increase faster than tenant incomes, eventually some rental units will no longer be considered "affordable," despite no other changes to the property, building, or business model.
Value-add Investment	In response to market demand from middle- and high-income rental properties, NOAH or expiring deed-restricted properties may undergo light-to-moderate rehabilitation to improve the property to be repositioned in the rental market or convert to for-sale condominiums. This process may be initiated by a transfer in ownership.
Redevelopment	In areas where the market can support redevelopment, an owner may completely redevelop a NOAH or expiring deed-restricted property, which can include a full rehabilitation, demolition and new construction, or a combination of both approaches. Such properties are generally targeted at the top of the market to offset the major investment in the property.

There are two primary conditions required to preserve a property:

1. Achieve a sustainable financial position.	The property must generate a net operating income (NOI) to sustain operations and repairs. If a property cannot sustain itself through NOI, it is at risk of being lost through lack of upkeep or be sold through a distressed sale.
2. Protected from exposure to market pressure.	There are a two key ways to ensure that properties are not exposed to existing market pressures: • A legal restriction, policy or loan agreement that regulates the increase of rent on the property; or • Transferring ownership to non-profit motivated owners (mission-oriented nonprofits, tenant ownership.)

There are three primary intervention points to preserve buildings: change in **ownership**, **recapitalization**, and **redevelopment**.
When a property is bought or sold, facilitating transfer to mission-driven ownership can restrict rent increases. The property must generate a net operating income (NOI) to sustain operations and repairs. If a property cannot sustain itself through NOI, it is at risk of being lost through lack of upkeep or be sold through a distressed sale.

Preservation Framework| Policy Categories

There are five key policy categories in which different permutations of preservation approaches can be combined to develop a sustainable preservation framework for Montgomery County.

Strategy and outreach	Analyzing preservation needs, opportunities, approaches, and interventions in the local context; and coordinating and executing efforts (often across agencies) to achieve identified goals and targets.
Land use and planning	Leveraging the rules governing or guiding development within a jurisdiction (including zoning codes and area plans) to incentivize or require preservation of affordability.
Tenants' Rights	Leveraging the rules that govern how various stakeholders (owners, property managers, developers) participate in the market to preserve affordability and protect tenants.
Capital Financing	Providing the financial resources necessary to undertake preservation interventions.
Operating Subsidy and Cost Reduction	Operating subsidy/cost reduction: Offering incentives and resources that make it financially feasible for landlords/owners to offer reduced rents to lower-income tenants.

The most appropriate preservation approach and intervention is likely to depend on multiple factors, including but not limited to: the type of unit (NOAH, expiring deed-restricted); risk of loss; most likely loss type(s); property characteristics (scale, building typology, location, redevelopment potential); and priorities for resource allocation. **All these tools will be required for an effective preservation framework.**

Preservation Framework| Recommendations

There are five key policy categories in which different permutations of preservation approaches can be combined to develop a sustainable preservation framework for Montgomery County.

Category	Key Recommendations
Strategy and outreach	• Triage opportunities to preserve affordability, focusing on near-term opportunistic approaches such as COVID-19-related policies to bridge towards future comprehensive preservation efforts.
Land use and planning	• Allow or incentivize directly preserving existing NOAH as an alternative to MPDU compliance. • Consider a transfer of development rights program that builds off the County's agricultural TDR program to preserve priority existing affordability and continue to designate affordable housing as a public benefit.
Tenants' Rights	• Consider expanding rent stabilization after the Covid-19 crisis following the 90-day rent relief bill. Rent stabilization needs to be designed carefully to ensure a healthy pipeline of new development along with preservation of residents at risk (especially in areas along the Purple Line expansion).
Capital financing	• Explore opportunities to expand the Housing Initiative Fund to meet the needs of the preservation pipeline. • Adjust HIF administration guidelines to align with new LIHTC income averaging regulations. • Review allocation decisions to ensure that funding criteria promotes preservation, especially at lower income levels.
Operating subsidy/cost reduction	• Expand utilization of rental agreements through the County's PILOT provision. • Evaluate the previous County reduced rent program for elderly tenants and explore development of a new preservation property tax credit.

Montgomery County's Housing Landscape

Housing Landscape | Introduction

The Housing Landscape section provides summary data on Montgomery County's housing inventory, with a focus on multifamily rental housing units.

- **Housing Snapshot**: A brief overview of the population, households, and housing units in Montgomery County
- **Housing Affordability**: Discussion of recent affordability trends in Montgomery County and the household income groups used in this report.
- **Multifamily Rental Housing**: A detailed analysis of the rents and geographic distribution of the multifamily units.

Source: ACS 2018 1-year

Montgomery County has a population of 1.1 million residents with 391,000 housing units. Of these, 240,000 units (65%) are owner-occupied and 129,000 units (35%) are renter-occupied.

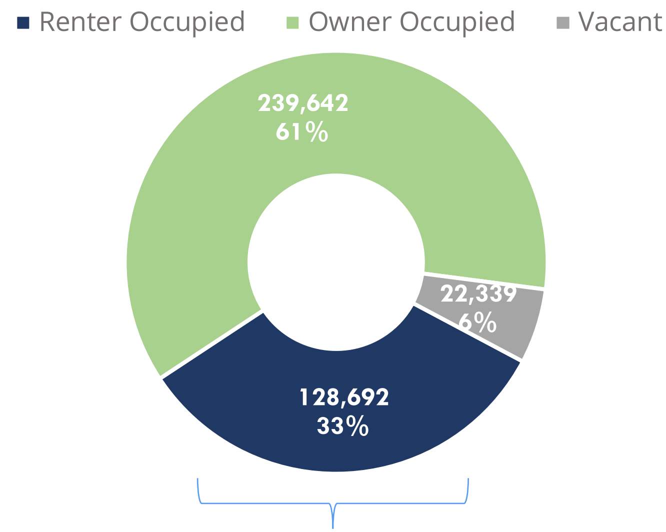
The share of households who rent in Montgomery County has increased by one percentage point since 2010, from 34% to 35%, and is three percentage points below the DC region as a whole.

Following development trends, most rental households in Montgomery County live in multifamily buildings and are increasingly living in larger multifamily buildings. Approximately 96,400 rental units (75%) are in buildings with five or more units, while 1,270 (1%) are in smaller two-to-four-unit multifamily buildings. The remaining 27,285 renter households (23%) are in single-family homes (both attached and detached). This report will primarily focus on multifamily properties with five or more units, as this is a threshold that has been identified by most preservation policies as the minimum number of units required to make a preservation investment economically feasible.

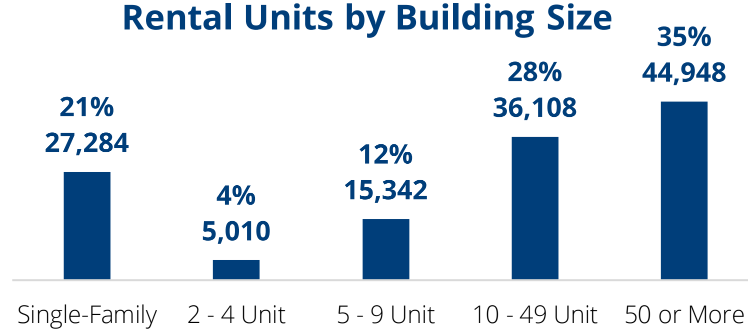
Since 2010, the number of renter households living in buildings with five or more units increased by 12%. In comparison, the number of households living in two-to-four unit multifamily buildings increased by 14%, and the number of households living in single-family units decreased by 11%.

Source: ACS 2018 1-year

Montgomery County Housing Units



Rental Units by Building Size

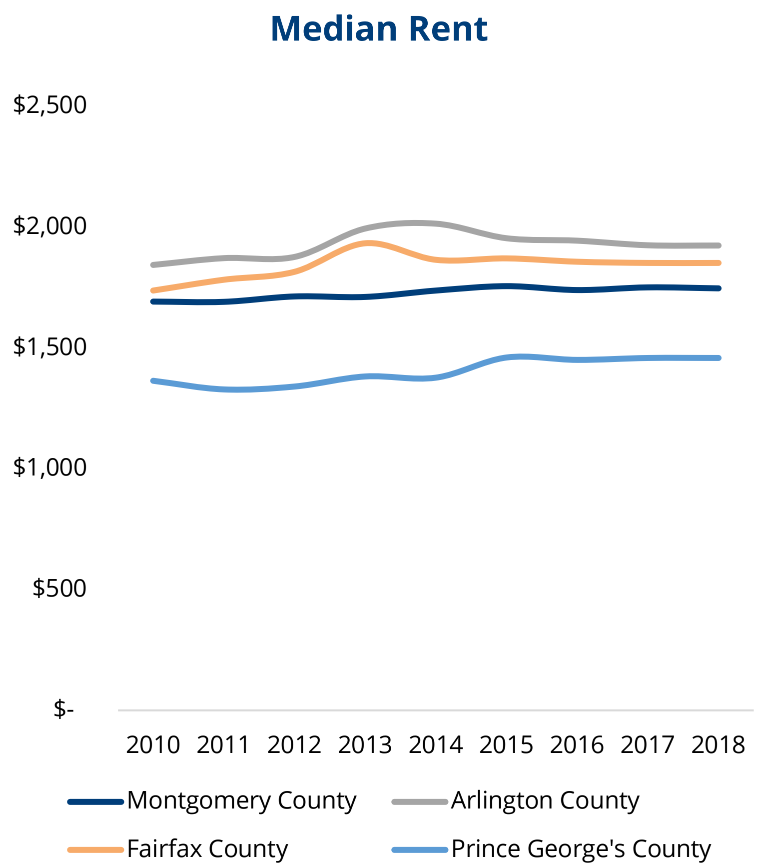


The preservation study focuses on rental multifamily housing.

Median rents in Montgomery County have increased 3% between 2010 and 2018, and median renter incomes have increased by 9% in the same period.

Housing affordability is the product of two factors: **household income** and **housing costs**. Housing is considered affordable if total housing costs are below 30% of total household pre-tax income. In most U.S counties, housing costs have grown faster than household incomes over the last decade, leading to a growing affordability challenge for low- and middle-income households.

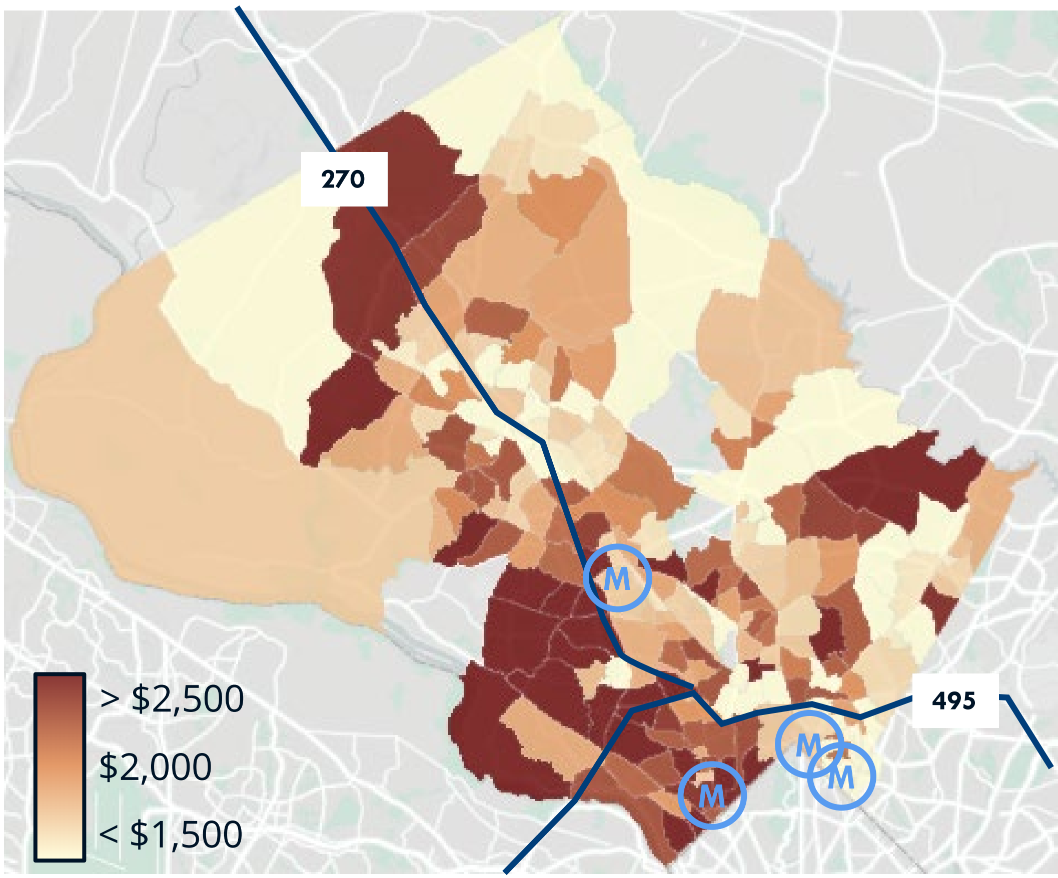
In the same time period, median home values have increased by 15%, from $406K to $468K. This has caused many households with moderate incomes who may have previously purchased homes to remain in the rental market. As more of these households enter the rental market, either due to a lack of homeownership options or changing preferences, households with lower incomes compete for the same rental units. This further reduces vacancy rates, drives up rents, and increases the housing cost burden on those at the lower end of the income spectrum.



Source: ACS 2018 1-year

Median rents vary significantly by locality in Montgomery County, with a difference of $2,500 per month between the highest median rents ($3,500 in Bethesda/Chevy Chase) and the lowest ($1,000 in Aspen Hill, Olney, and Takoma Park).

Median Rent by Census Tract



On average, the median rents in western portions of the county (cities like Bethesda, Rockville, and Potomac) are about $425 (or 23%) higher than those in the east.

Between 2010 and 2018, this disparity has increased. The median rent increased most dramatically in Potomac, Bethesda/Chevy Chase, and Kensington/Wheaton. Areas near WMATA Metrorail Stations and along I-495 (including Silver Spring, Takoma Park, Bethesda/Chevy Chase, and Kensington/Wheaton) lost the greatest number of affordably priced rental units (units <$1,250). Areas in the northern part of the County saw an increase in rents, but less so.

Source: ACS 2018 5-year

To understand the housing inventory in the context of affordability for households at different income levels, this report organizes renter households into 3 groups based on income and household size, based on Montgomery County's existing deed-restricted housing programs.

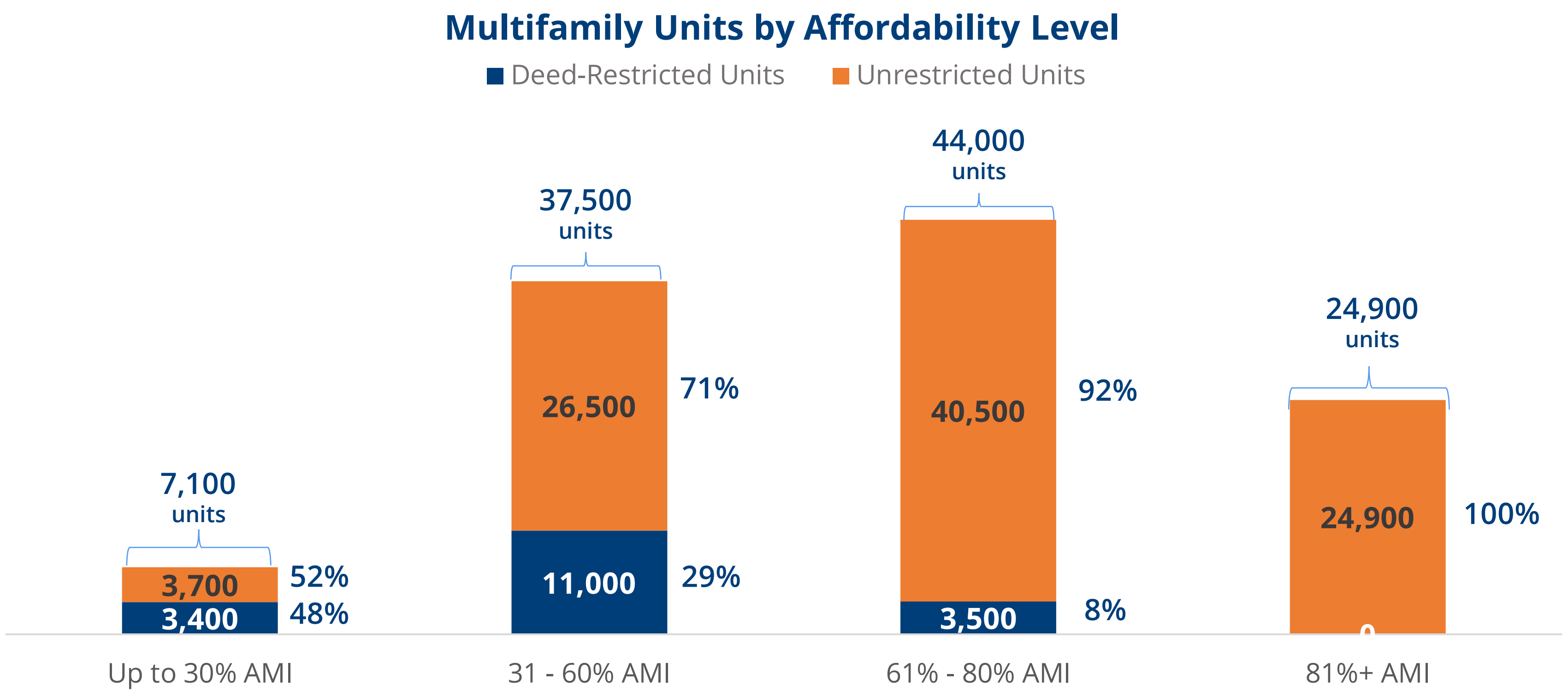
Income Group	0 – 30% AMI	31 – 50% AMI	51 – 65% AMI	66 – 80% AMI	81 – 120% AMI	121%+
Total Households	30,888	18,787	14,778	8,437	29,106	26,696
Share Cost Burdened	82%	90%	62%	33%	17%	4%
Share Severely Cost Burdened	74%	35%	5%	4%	2%	0%

38% of renter households in Montgomery County earn below 50% of AMI. The remaining 62% renter households are split between incomes between 65% - 80% of AMI (8,437 households, 7%), and above 80% of AMI (55,802 households, 43%).

The private market does not effectively provide rental housing options that are affordable to renters in the lower income bands, as 78% of households earning below 65% of AMI are housing cost-burdened--paying more than 30% of their household. In addition, 60% of households earning below 50% AMI are **severely housing cost-burdened—**paying more than 50% of their gross household income on housing costs. After paying for housing, many of these households do not have enough resources to adequately cover necessary expenses like transportation, food and healthcare.

Source: ACS 2018 1-year

The plurality of the County's rental multifamily housing stock is affordable to households earning between 60% - 80% of AMI currently. Deed-restricted units make up 32% of units below 60% of AMI.



Source: ACS 2018 1-year

Housing Landscape | Rental Housing Gap

At incomes below 50 percent of AMI, a significant mismatch exists between the supply of affordable rental housing available and the number of households that need it. Almost all households earning below 30 percent of AMI face a lack of affordable supply.

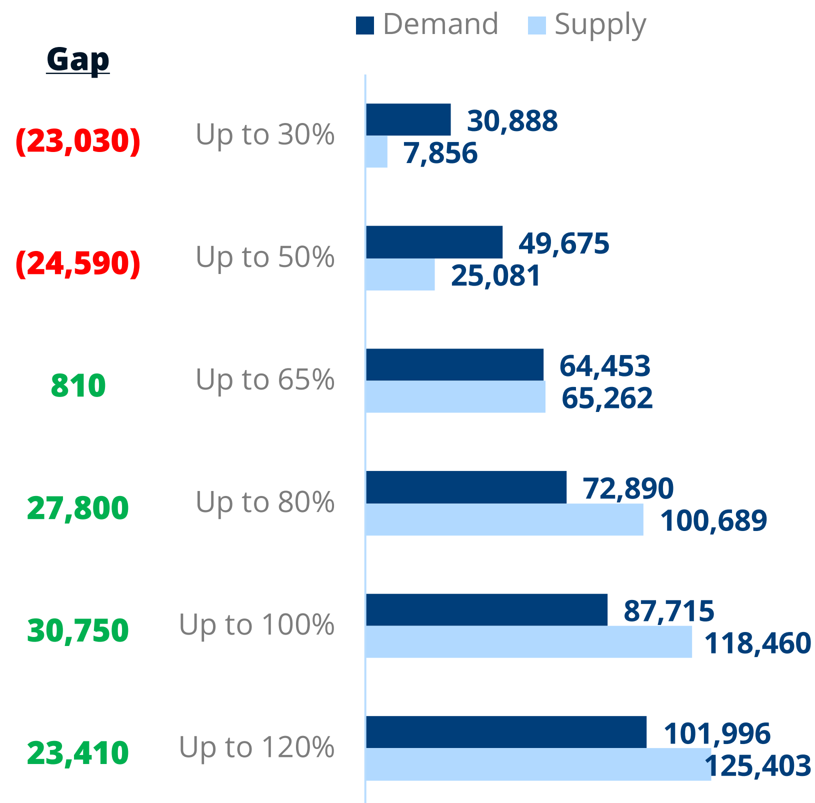
The current affordable housing availability gap measures the difference between what Montgomery County residents can afford to pay in rent (need, or demand) and the housing options affordable to them at that price point (availability, or supply). These gaps are summed cumulatively for each income threshold, as each household can afford any unit below their income threshold.

At incomes below 50 percent of AMI (VLI), a significant mismatch exists between the supply of affordable rental housing available and the number of households that need homes at that price level. In Montgomery County, 49,675 households earn less than 50 percent of AMI, but only 25,081 units are affordable to these households, resulting in a rental housing affordability gap of 24,590 units.

More acutely, almost every renter earning less than 30 percent of AMI (extremely low-income) faces a lack of affordable housing. Only 7,856 units are affordable to extremely low-income renters, with a total demand of 30,888 households, leading to a gap of 23,030 units.

Source: ACS 2018 1-year

Housing Supply and Demand by AMI Band (Cumulative), 2018



Deed-Restricted Affordable Housing Inventory

Deed-Restricted Inventory | Key Takeaways

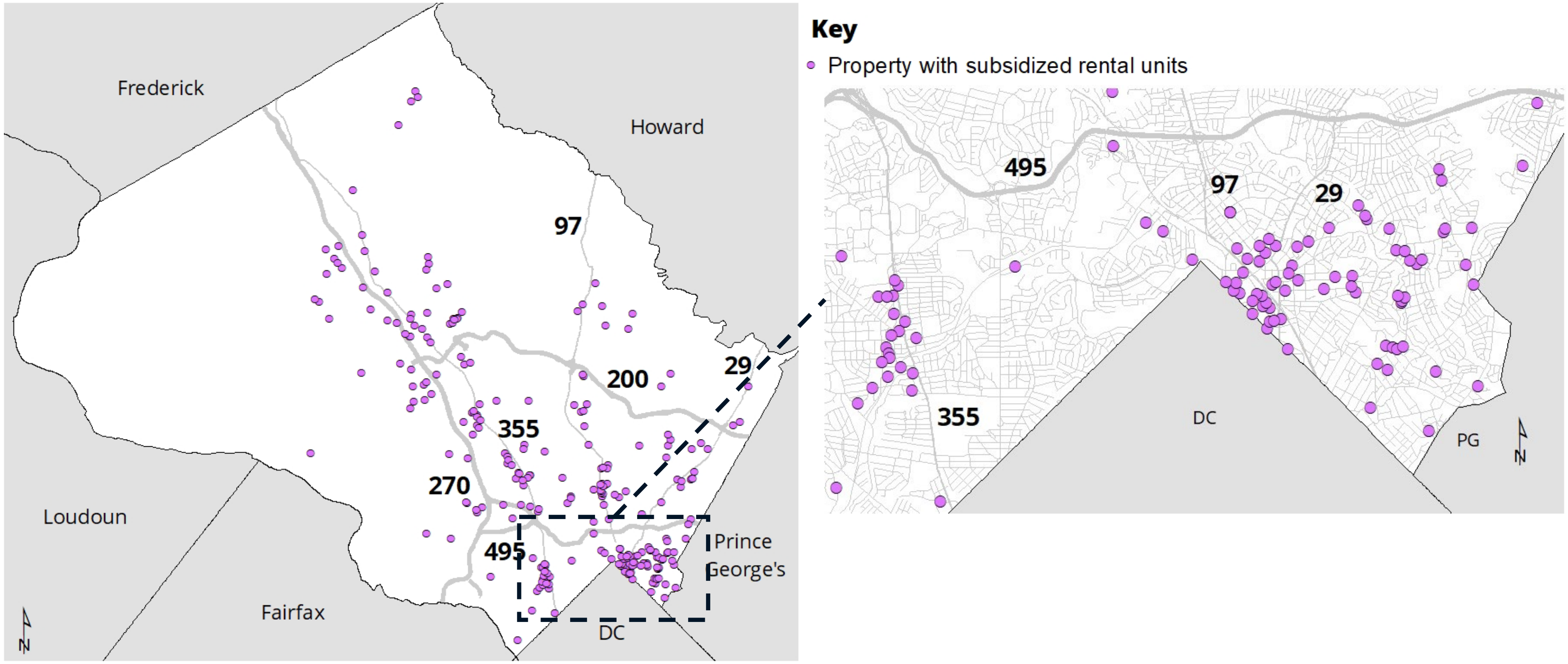
Subsidized deed-restricted housing units have documents recorded on the property that set binding rent restrictions. These restrictions are often based on federal, state, or county programs that subsidize the development and operation of units. Depending on the type of affordability program and subsidy, rental housing regulations on units often have a set time period for affordability. This section of the preservation study examines the characteristics of the deed-restricted rental housing stock in Montgomery County, and evaluates historical and future patterns of unit loss, production, and preservation. A risk assessment is then applied to the inventory to identify which units in the County's deed-restricted housing stock have a higher risk of losing affordability when the subsidy compliance periods expire.

Key Takeaways

- **Subsidized deed-restricted rental housing accounts for 1 out of 5 multifamily units in the County.** There are approximately 18,000 deed-restricted multifamily rental housing units in Montgomery County, representing just under 20% of the County's total multifamily rental stock.
- **Preservation of these units is actively pursued.** The County has been using a variety of preservation strategies to mitigate the loss of deed-restricted rental housing. Since 2000, these efforts have preserved approximately 1,770 units from being lost.
- **Production has increased in recent years.** Since 2000, 5,387 deed-restricted rental units have been added to the inventory, nearly double the amount added in the 20 years prior. The pipeline is projected to add another 6,409 in the coming 2 decades, most of which are MPDUs.
- **Upcoming expirations put many deeply affordable units at risk**. Between 2020 and 2040, the compliance period for over 7,000 deed-restricted units will expire. More than 90% of these units are affordable below 60% AMI.
- **There are about 1,400 units that have a higher risk of being lost**. More than half of these higher-risk units are located in and around the Silver Spring CBD, close to Metrorail and the Purple Line. All of these higher-risk units are affordable below 60% AMI and are critical to the County's deed-restricted housing stock.

There are approximately **18,000 units in the County's deed-restricted rental housing inventory**. While the units are spread out in many areas of the County, most of the units are located in the more densely populated areas where multifamily housing is more prevalent. About a third of the deed-restricted rental inventory is located inside of the Beltway (32%). Most of these inside-the-Beltway units are in Silver Spring (3,518) and Takoma Park (886). More than a third of the deed-restricted inventory (38%) is located along the I-270 and Route 355 corridors, primarily in Gaithersburg (3,077) and Rockville (2,616).

Deed-Restricted Inventory (5+ units), 2020

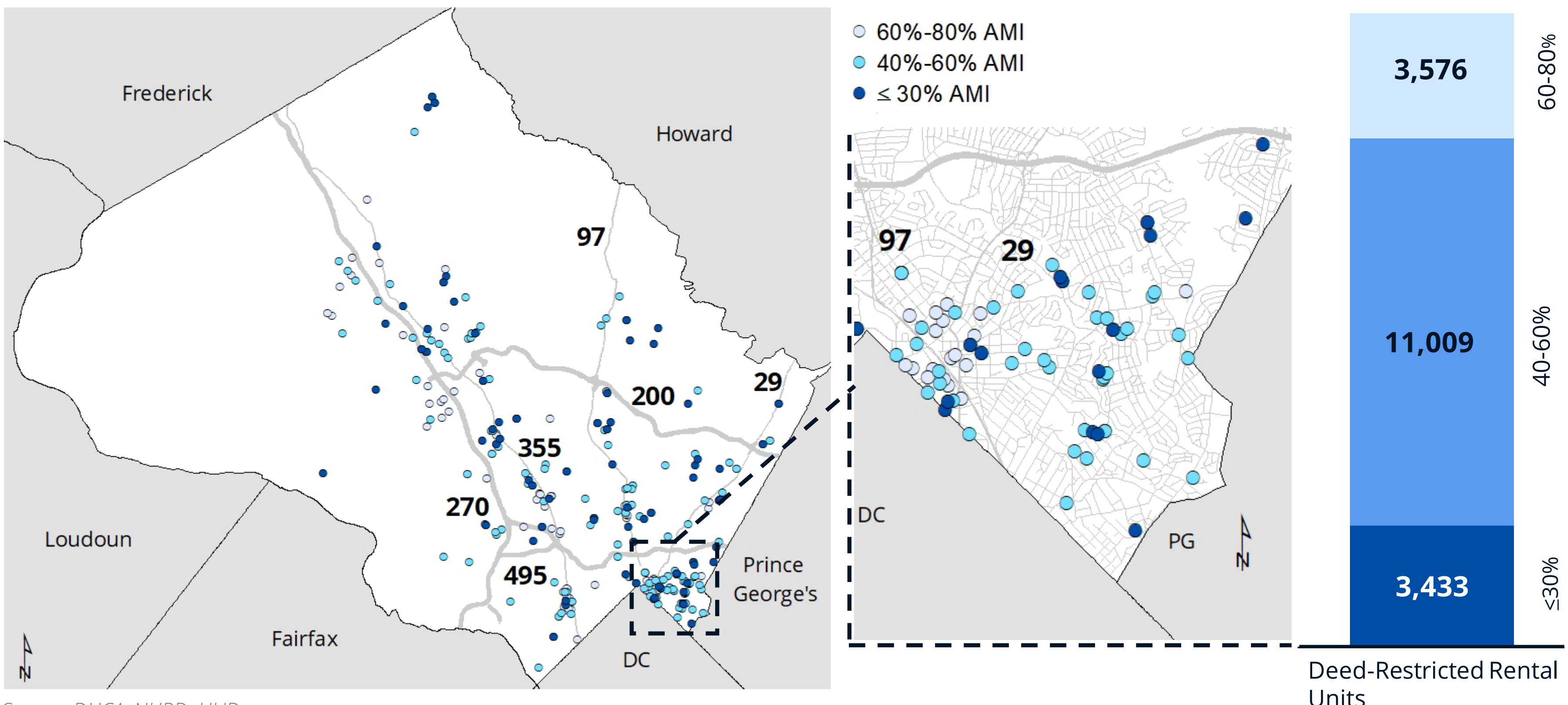


Source: DHCA, NHPD, HUD

Deed-Restricted Inventory | Affordability Ranges

Most of the deed-restricted rental housing stock in the County is affordable in the 40% to 60% AMI range; about 6 out of every 10 deed-restricted units falls in this range (61%). There are approximately 3,433 deed-restricted units that are affordable at and below 30% AMI. Most of these deeply affordable units were built in the 1970s and 1980s and are located in Silver Spring, Rockville, and Gaithersburg. Only 7% of the deeply affordable units in the inventory have been built since 2000. About 20% of the deed-restricted inventory in the County is in the 60% to 80% AMI range, many of these units are MPDUs. Most of the units in the 60% to 80% AMI range have been built since 2000 (75%).

Deed-Restricted Rental Inventory, Affordability Ranges



Source: DHCA, NHPD, HUD

Deed-Restricted Inventory | Age of Inventory

The deed-restricted rental inventory in the County is relatively old overall, but there has been an influx of units in recent years. Of the approximately 18,000 total units in the inventory, more than 10,000 were built more than 30 years ago. More than a third of the total inventory (35%) were built in the 1960s and 1970s, making them 40 to 50 years old. As the inventory continues to age, maintenance and repair will become increasingly critical for the older units to remain a viable part of the deed-restricted housing stock. While most of the units were built between 1960 and 1980, there has been an increase in units in the past couple decades. Since 2000, approximately 5,387 deed-restricted rental units have been built, which is about 30% of the County's total inventory.

Montgomery Arms Apts

1941

Silver Spring House

1963

Fields of Gaithersburg

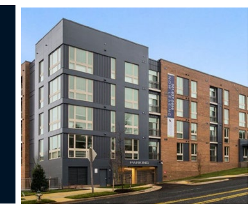
1974

Timberlawn Crescent

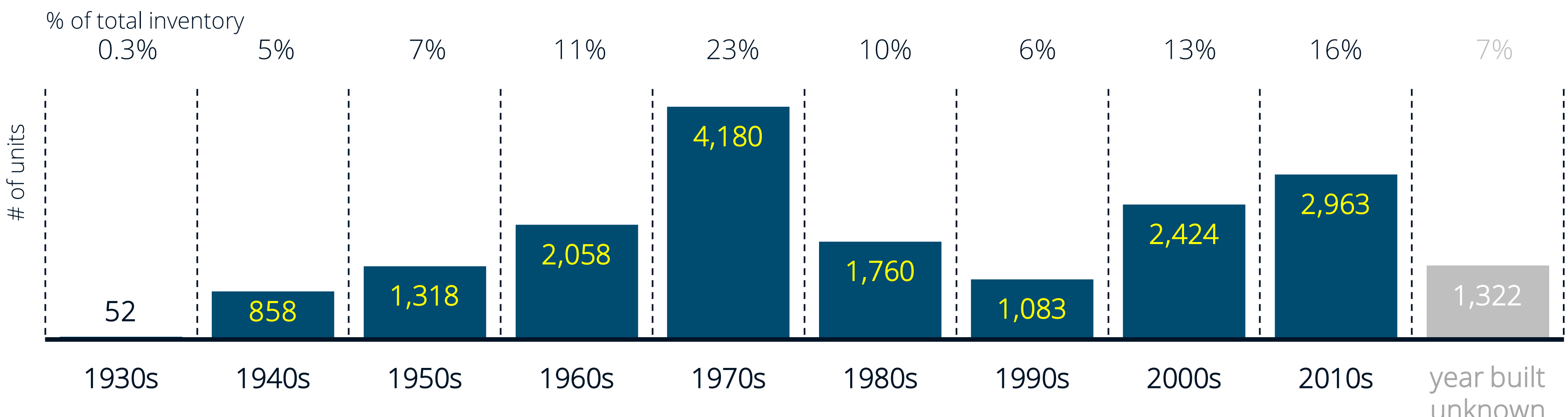
1989

Momentum at Shady Grove

2019



Deed-Restricted Rental Inventory, by Decade Built

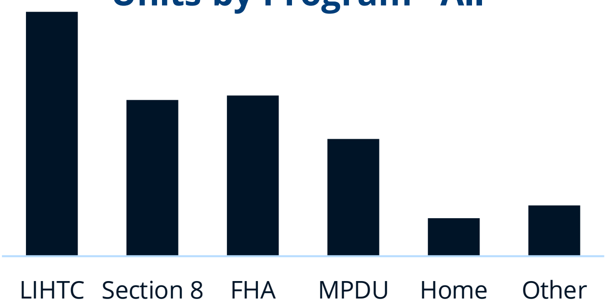


Source: DHCA, NHPD, HUD, MD Dept. of Assessments and Taxation, Montgomery County Property Tax Records

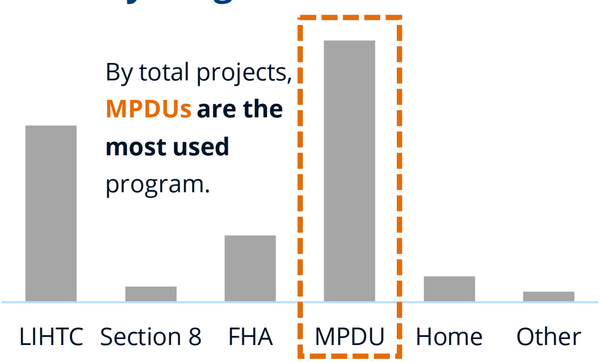
Deed-Restricted Inventory | Subsidy Programs

A wide range of federal state and local programs control the affordability and time period of the deed-restricted rental housing stock in the County. In terms of unit yield, the federal low-income housing tax credit program (LIHTC) has produced the largest number of deed-restricted rental units. While the LIHTC program has been leveraged extensively, the County's MPDU program is the most commonly used program. About a third (33%) of all properties that contain deed-restricted rental units have MPDUs. In many cases, multiple subsidy programs are used on the same site. For example, 32% of all properties with deed-restricted rental units use more than one program. These funding stacks play a critical role in the financial viability of this housing stock. About 24 properties in the inventory are using between 3 and 4 subsidy programs from a variety of sources.

Units by Program - All



Units by Program – Built Since 2000



Source: DHCA, NHPD, HUD, FHA

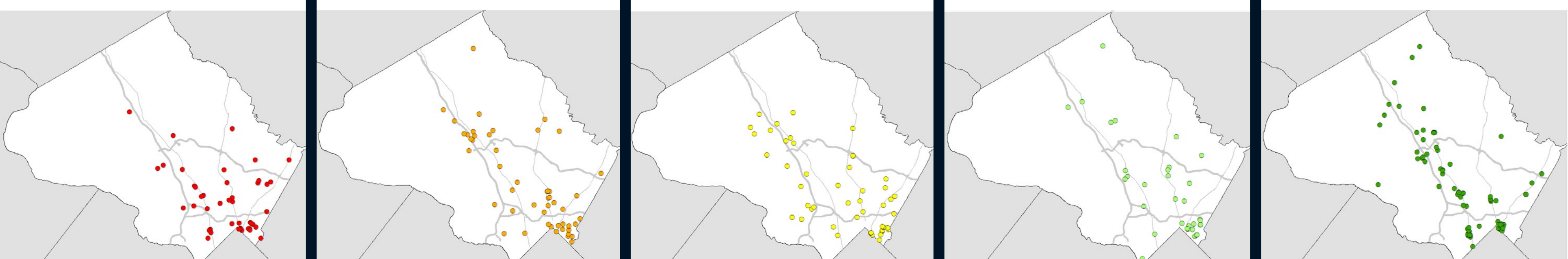
LIHTC Federal 1986	The low-income housing tax credit program provides tax incentives for affordable housing. Each state receives an annual allocation of tax credits which are then administered to qualifying projects. The affordability period is 30 years.
Section 8 Federal 1974	HUD provides Section 8 vouchers to local public housing authorities. The vouchers can be project-based (specific location), or tenant-based (flexible location). The voucher covers the difference between the fair-market rent of the unit and the amount the tenant can afford to pay in rent (30% of household income)
FHA Federal 1934	The Federal Housing Administration insures mortgages for affordable housing sites. The FHA insures a variety of loan types including new construction, rehabilitation, and re-financing, among others. Loan terms are typically 35 to 40 years.
MPDU County 1974	The County requires between 12.5%-15% of new housing units (in projects with 20+ units) to be moderately price dwelling units. There are both renter and owner-occupied MPDU options. Affordability ranges are typically 65%-70% of AMI, and the required affordability period is now typically 99 years.
HOME Federal 1990	HUD provides HOME funds to states/counties/cities to expand affordable housing options. Eligible uses of HOME funds include tenant-based rental assistance, housing rehab, homebuyer assistance, site acquisition, and new construction. There are matching requirements for HOME funds. The affordability period is typically 15-20 yrs.
Other	Includes a variety of other Federal/State/County housing programs: Section 202, 811, 236 (Federal), Rental Housing Production Program, Partnership Rental Housing Program, Multifamily Bond Program (State), PILOT, Housing Initiative Fund (County)

Deed-Restricted Inventory | Subsidy Expirations

The expiration timeline for the deed-restricted rental inventory is spread out over nearly 100 years. After the subsidy control period expires, some of the rental units could be lost from the deed-restricted inventory, particularly if the properties are owned by for-profit companies and are in desirable locations. Nearly 7,000 units, which is approximately 38% of the total deed-restricted inventory has subsidy expirations that will occur in the 2020s and 2030s. Most of these near-term expirations are in buildings that are more than 30 years old (approximately 5,000 units), many of which are either early LIHTC projects, or early MPDUs. Notably, about half (47%) of the units that are set to expire in this current decade are located inside of the beltway, and many of these units are near transit infrastructure and are in areas of the County that have experienced development pressures in recent years. While a significant portion of the total inventory is expiring in the next 2 decades, it's important to note that about 15% of the inventory have deed restrictions stretching beyond 2100. Most of these longer-term deed-restricted units are recently built MPDUs.

Deed-Restricted Rental Inventory by Expiration Decade

% of inventory	*15%*	*23%*	*22%*	*16%*	*17%*
# of units	**2,758**	**4,168**	**3,902**	**2,849**	**3,045**



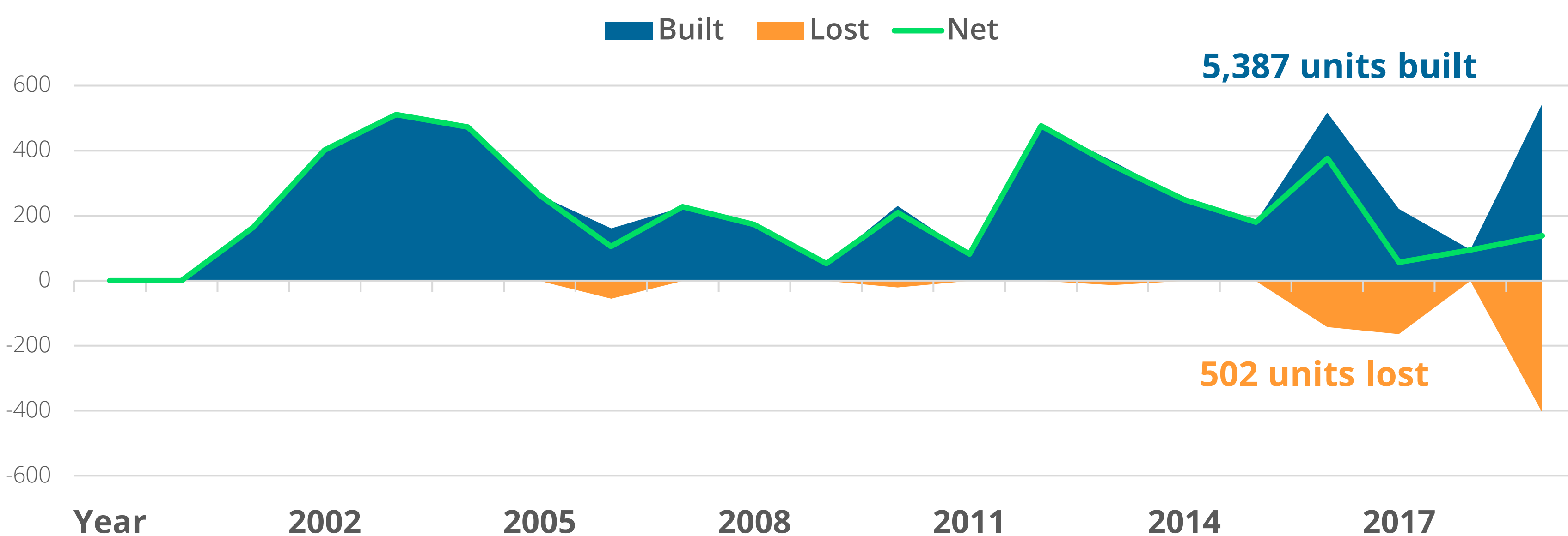
2020s	**2030s**	**2040s**	**2050s**	**2060+**

Source: *DHCA, NHPD, HUD, MD Dept. of Assessments and Taxation, Montgomery County Property Tax Records*

Overall, the County has been gaining deed-restricted rental housing stock at a faster rate than it is being lost. Since 2000, approximately 502 deed-restricted rental housing units have been lost from the inventory. Most of these were Section 8 units located within larger market-rate rental properties. During this same time period (2000 to 2019), approximately 5,387 deed-restricted rental units have been added to the inventory, most of which are MPDUs.

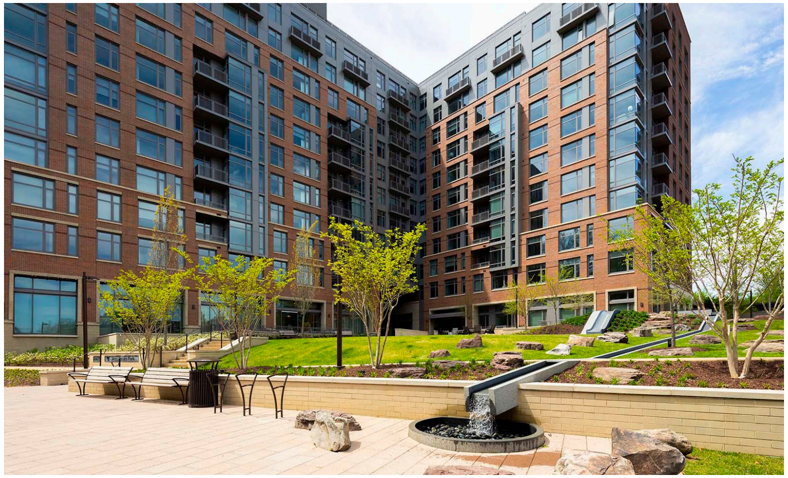
In 2000, the County began to implement preservation strategies for the deed-restricted rental housing stock that was at risk of being lost. A series of tools and policies have been used (often in tandem) over the years to effectively preserve deed-restricted rental housing in the County. Some of these strategies include: redevelopment, acquisition, rehabilitation, use of a PILOT (payment in lieu of taxes) as a tax-abatement tool to lower the overall tax burden of properties that have deed-restricted units, rental agreements that provide cash payments from the County to rental property owners to keep the rents on specified units below market levels, covering rent payments when Section 8 voucher payments from HUD are delayed, and covering maintenance and repair costs of deed-restricted rental units.

Net Change in Deed-Restricted Rental Housing 2000 – 2019



Source: DHCA, NHPD, HUD, MD Dept. of Assessments and Taxation, Montgomery County Property Tax Records

Case Study - Preservation through redevelopment: The Lindley is an example of how creative public-private-philanthropic partnerships can bring new life to aging properties in the deed-restricted inventory. Using a combination of public and private equity on an HOC-owned site, the County was able to leverage the value of additional density in a transit-proximate area to replace 68 garden-style deed-restricted units that were 70+ years old with 200 high-quality mixed-income apartment units in a new building along the Purple Line. Eighty of the units are designated as MPDUs. Of those 80, 40 are at 50% AMI, and 40 will be workforce housing units. Some of the affordable units are 3-bedroom units, which provide options for families. The project also contains 62 for-sale brownstone townhouses, of which a share are MPDUs. Deed-restricted units on the property will remain affordable until 2117.



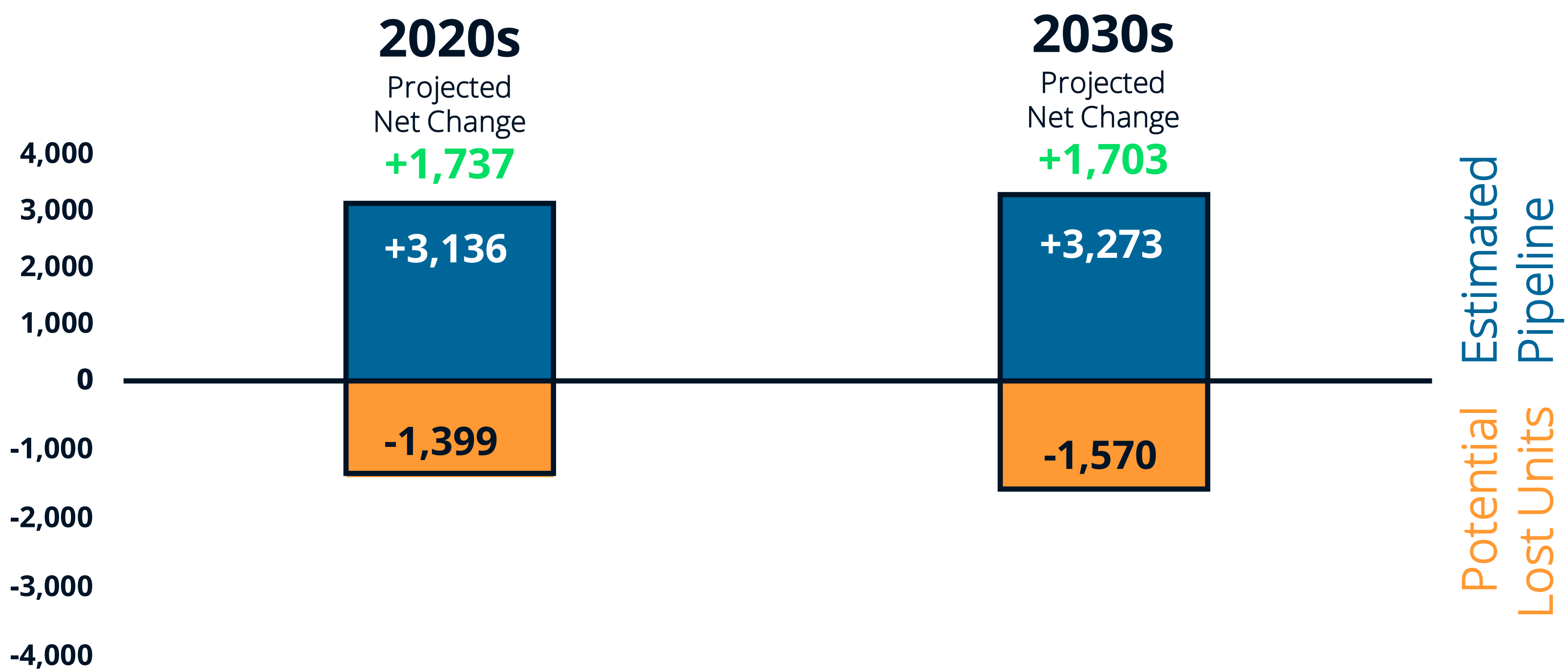
Case Study - Preservation through protection: The Montgomery Paint Branch/Yorkshire Apartments are an example of the County using proactive engagement with for-profit apartment owners to preserve deed-restricted units and protect low-income tenants from rent increases. There are over 850 units in total, most of which are market-rate. Of those, 149 are deed-restricted units. Of the deed-restricted units, 49 are under a Section 8 Housing Assistance Payment (HAP) contract that will be expiring in 2022. The entire property is being acquired by new ownership, which plans to rehab the units, and increase rents. The County negotiated an agreement with the new owner to extend the HAP contract on the 49 units, and also provide an additional 30 units at 40%-60% AMI. The County is providing a suite of incentives including tax-relief (entering a new PILOT with the new owners), cash payments (rental agreement with County to cover rent delta on the 30 units), and compensation for administration of the 79 deed-restricted units. The HAP will be extended for 10 years (from 2022), and the rental agreement will be 5 years from the time of acquisition.

Source: *DHCA*

Deed-Restricted Inventory | Estimated Future Trends in Net Loss/Gain

Of the nearly 7,000 deed-restricted rental units that are set to expire in the next 20 years, about 60% of them are owned by non-profit entities and are therefore classified as having a lower risk of being lost upon expiration. Over the years, most non-profit and mission-based housing owners have worked with the County to find ways to extend affordability periods. The remaining 40%, about 3,000 units, are owned by for-profit companies and have the potential of being lost from the inventory. Based on the anticipated development pipeline, which includes projects currently under construction, projects that are approved but not yet built, and projects that are under consideration/review, the County is projected to have a net gain of approximately 3,440 deed-restricted rental housing units over the next 2 decades. While development appears to be on track to outpace the unit loss rate, the AMI levels of the newly constructed units are likely to be higher than the units that have the potential of being lost. Most of the units in the pipeline are MPDUs, and most of the units with upcoming expirations are LIHTC and Section 8 units.

Estimated Net Change in Deed-Restricted Rental Housing Inventory, 2020s and 2030s



Source: DHCA, NHPD, HUD

Deed-Restricted Inventory | Establishing Risk Criteria

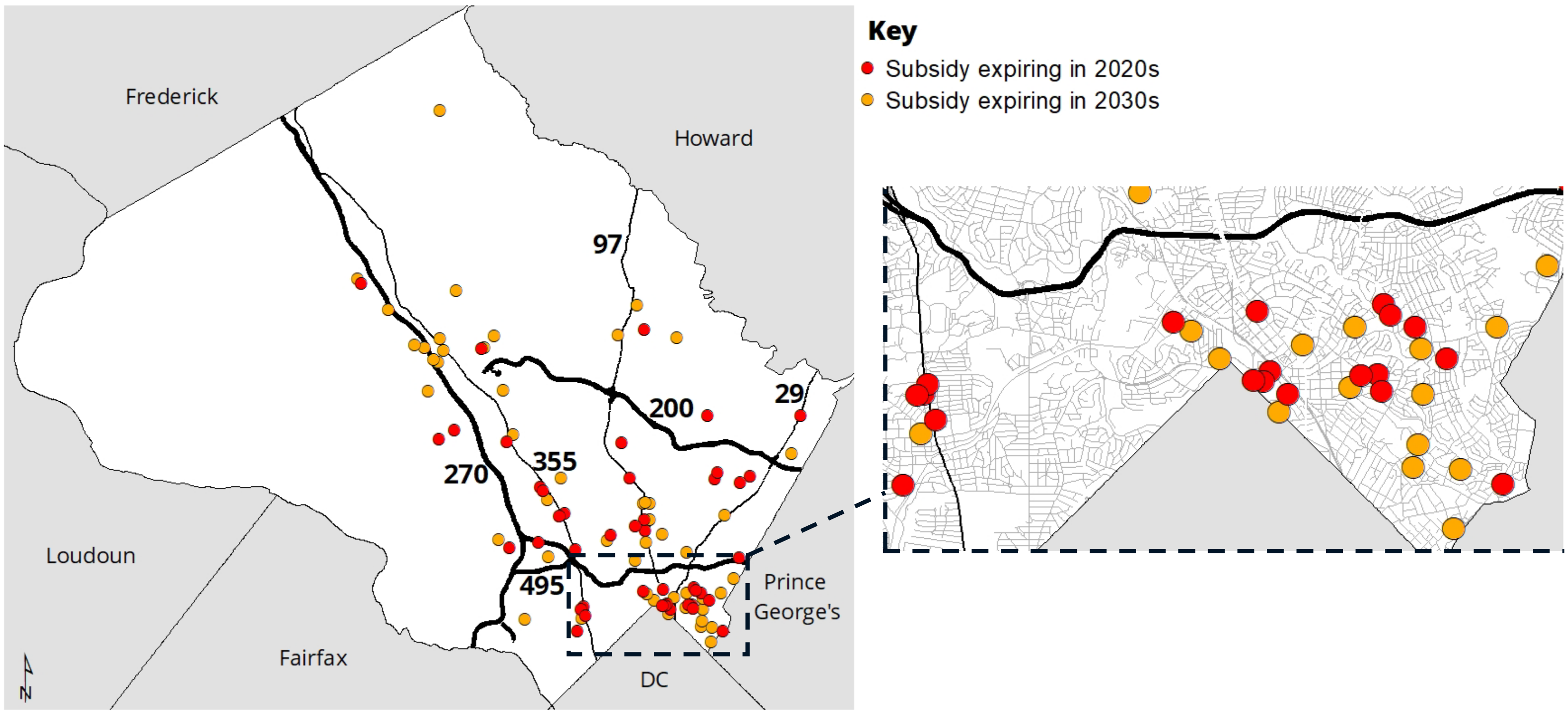
A set of risk criteria was applied to the deed-restricted rental housing inventory in Montgomery County to assess the level of loss risk for this housing stock, and to identify potential high-risk properties. The following risk criteria and risk-assessment provide a starting point for prioritization of activities and strategies related to deed-restricted housing preservation.

Risk Criteria	Description
Upcoming subsidy expirations	Subsidy expirations set to occur in the 2020s and 2030s. Property owners with near-term expirations are more likely to explore options ahead of the expiration date, which could include new ownership, rehabilitation, renovation, and redevelopment, all of which could impact affordability.
Ownership type	For-profit ownership or non-profit ownership. Properties owned by for-profit entities are more likely to be lost from the deed-restricted rental stock once the subsidy compliance period ends. Properties that are owned by non-profit and mission-based entities are more likely to work with the County to find solutions to extend the affordability period to align with the goals, mission, and vision of their organizations.
Age of buildings	The age of a building can play a significant role in the decision-making process of apartment owners. Many of the decisions can directly impact affordability. Typically, if a building is 30 years or older, renovations, rehabilitation, and redevelopment become more common scenarios. Major investments into a property are more likely to trigger a rent increase and could therefore impact the affordability.
Proximity to transit	Properties near transit infrastructure are more likely to command higher market rents when subsidy expirations expire, and in some cases are more likely to be facing redevelopment pressures.
Rent trends in neighborhood	Deed-restricted rental properties located in neighborhoods with rising rent trends are more likely to lose affordability when the subsidy compliance period expires.
Income trends in community	Rising income levels in communities around deed-restricted rental properties could have an impact on market-rents, and therefore increase the possibility of rent increases when the subsidy compliance period expires.

Risk Criteria | Upcoming Subsidy Expirations

The risk assessment focused on properties with subsidy expirations that will occur in the 2020s and 2030s. There are approximately 7,000 units that will have expirations in these two decades. Many of these buildings are located inside of the beltway and are near areas of the County that have had increased development pressure such as Bethesda and Silver Spring. While some of these near-term expirations are set to occur within the next year, most of the units will expire several years out, which allows time to utilize tools and strategies to proactively engage with the ownership of these sites to preserve the affordability of the units that best align with the County's goals and priorities.

Rental Inventory with Subsidy Expirations 2020s and 2030s

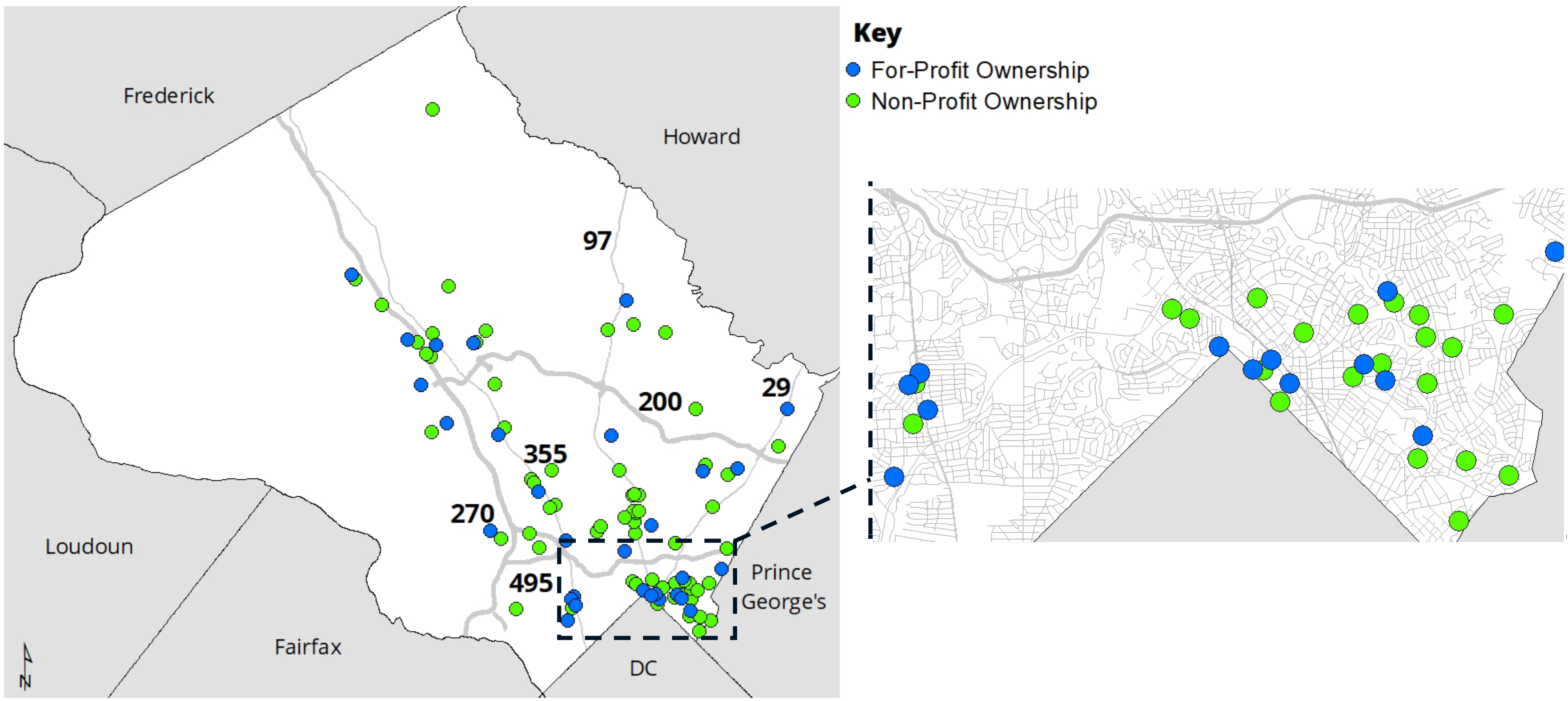


Source: DHCA, NHPD, HUD

Risk Criteria | Ownership Type

The type of ownership, whether it's a non-profit entity or a for-profit company, can be an important indicator of the level of loss-risk of a deed-restricted property. Nearly 3,000 of the total 7,000 units that have subsidies expiring in the next 20 years are owned by for-profit companies. These properties are considered to have a higher risk of being lost when their subsidy control period ends. The affordability of the remaining 4,000 units that are owned and/or controlled by non-profit entities are less likely to be lost when the subsidies expire. Of the properties owned by for-profit companies with upcoming subsidy expirations, nearly half (45%) are in Silver Spring in and around the CBD.

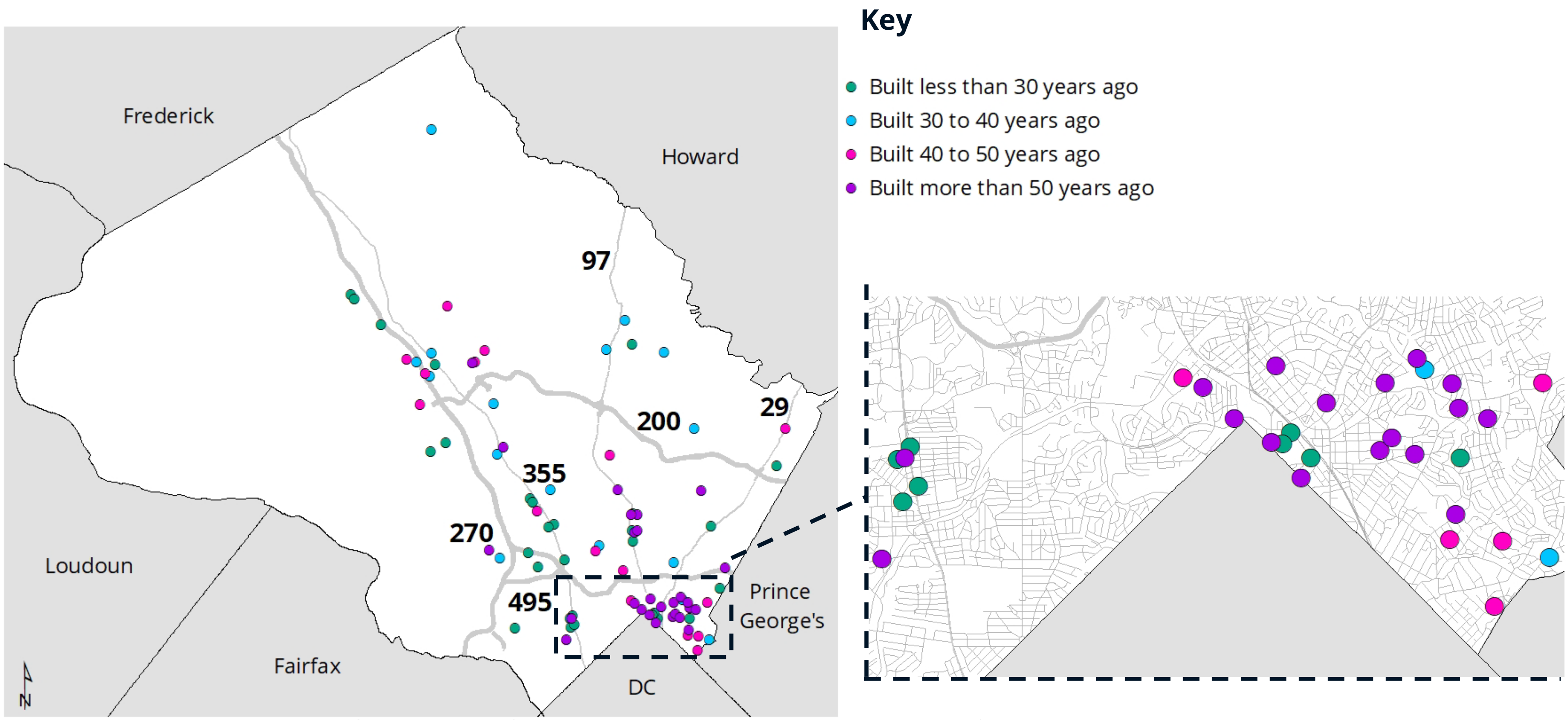
2020s/2030s Subsidy Expirations by Ownership Type



Source: DHCA, NHPD, HUD, MD Dept. of Assessments and Taxation, Montgomery County Property Tax Records

As buildings age past 30 years, they are more likely to need investments through either renovations or redevelopment. There are nearly 5,000 units in the deed-restricted inventory that are over 30 years old and have subsidy expirations within the next 2 decades. When the subsidy control period ends on these older units, some property owners could opt for major renovations which could also lead to rent increases. If a building is in a desirable location and/or the property is notably old, in some cases, if it is not in a historic preservation district, it could trigger a full redevelopment of the site. Of the units set to expire over the next 20 years, about 20% were built in the 1960s, making them between 40 and 50 years old.

2020s/2030s Subsidy Expirations by Age of Property

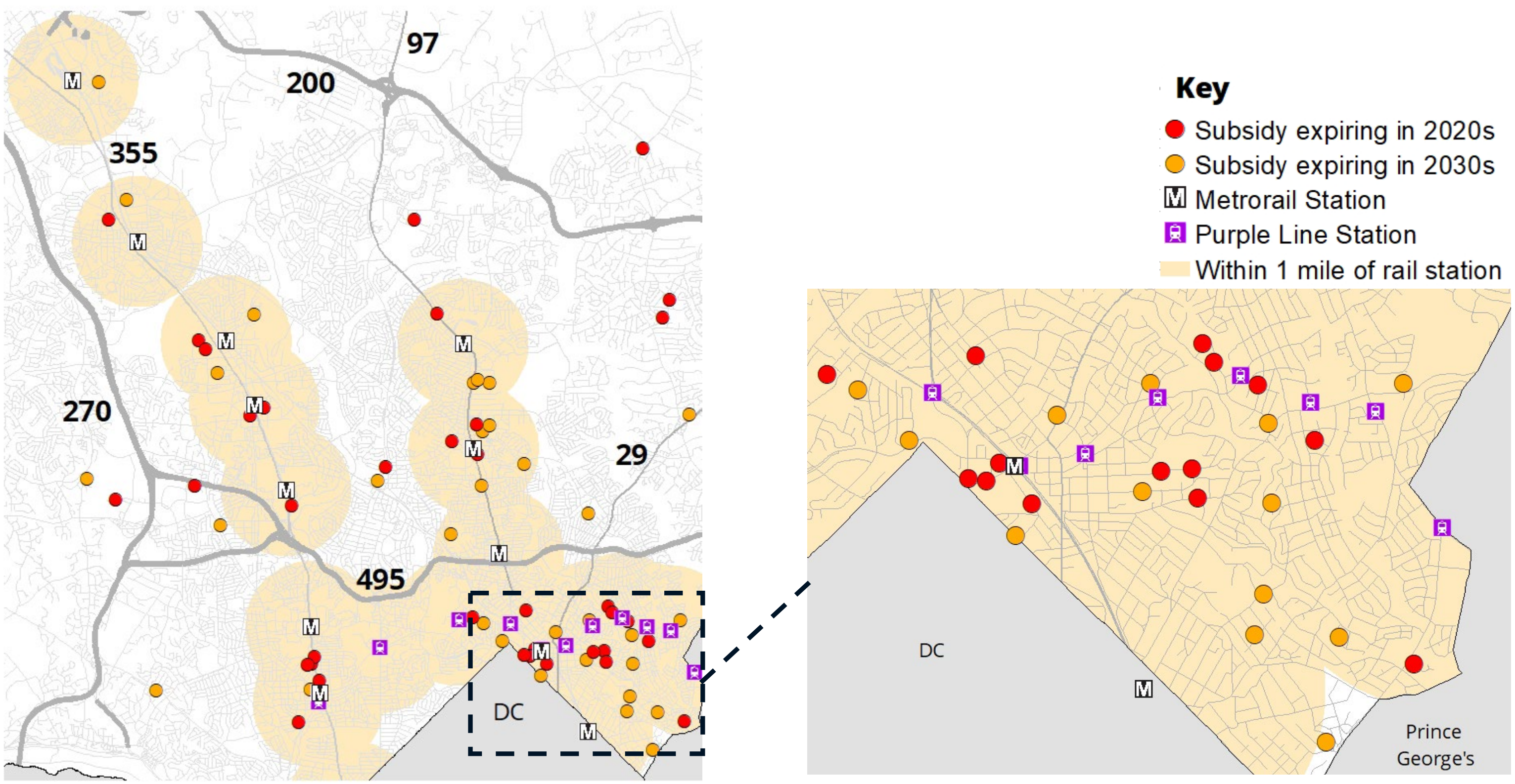


Source: DHCA, NHPD, HUD, MD Dept. of Assessments and Taxation, Montgomery County Property Tax Records

Risk Criteria | Proximity to Transit Infrastructure

Deed-restricted units that are near rail transit are a critical subset of the overall housing stock in the County. These units provide affordable housing options that are linked and accessible to the regional transportation system, providing residents access to more jobs, amenities, and resources. While these transit-proximate units play an important role, they also face increased risk of being lost when their respective subsidy control periods end. About 62% of the deed-restricted units that are set to expire in the 2020s and 2030s are located within 1 mile of a rail transit station (existing or planned). Most of these units are clustered around the Silver Spring, Bethesda, and Wheaton Metrorail stations, all of which have experienced increased development activity/pressure in recent years. There are 2,085 deed-restricted units that are expiring in the next 20 years that are located within 1 mile of a Purple Line station.

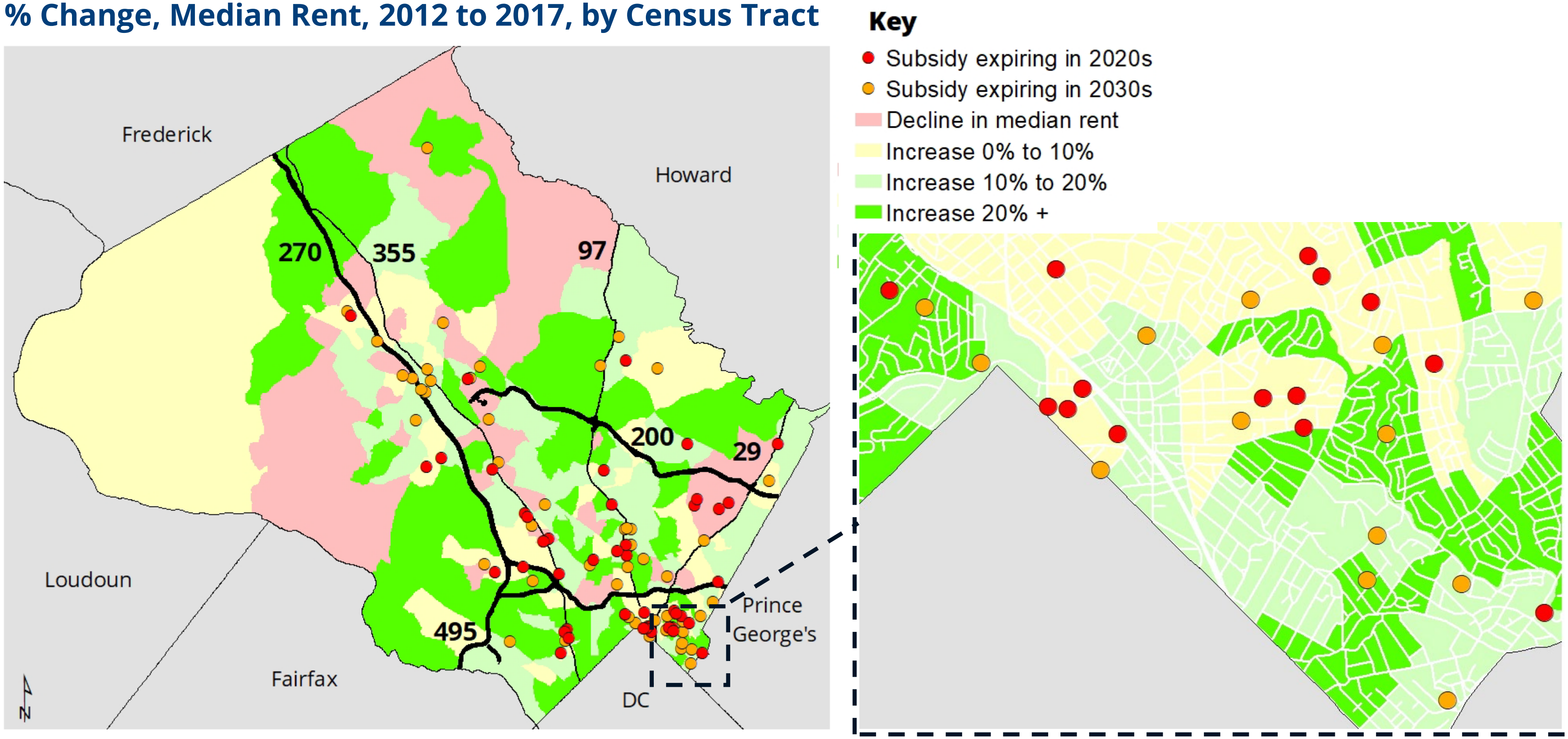
2020s/2030s Subsidy Expirations and Rail Transit



Source: DHCA, NHPD, HUD, WMATA, MDOT

As subsidy control periods expire, the rent trends in the surrounding neighborhoods in the preceding years can be an indicator of the affordability loss risk. Neighborhoods that have upward rent trends over several years are more likely to have market-rate rents that are higher than the deed-restricted unit rents, particularly in higher-cost markets. In addition to potential rent hikes when the subsidies expire, some properties that are located in neighborhoods that have experienced rapidly rising rents could reflect areas where redevelopment has occurred. This can lead to redevelopment of the deed-restricted property upon expiration and loss of affordability. Of the nearly 7,000 units that will expire over the next 20 years, 986 are located in census tracts where median rents rose 20% or more between 2012 and 2017.

% Change, Median Rent, 2012 to 2017, by Census Tract

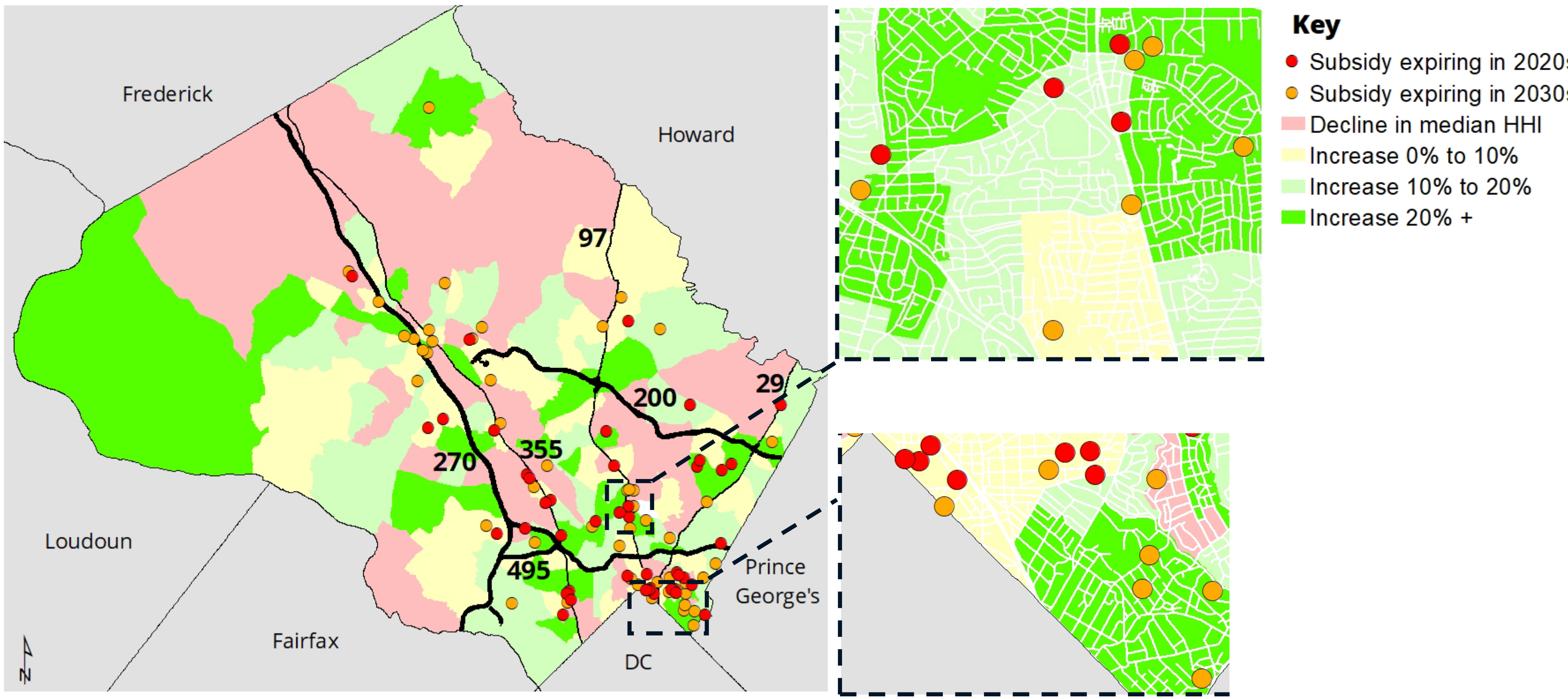


Source: DHCA, NHPD, HUD, U.S. Census Bureau 5-Year American Community Survey

Risk Criteria | Income Trends in the Community

Household income trends can have an impact on market rent levels in a community. Deed-restricted units that are located in areas where household incomes are trending up are more likely to have rent increases when the subsidies expire on those properties, either through transitioning to market rent levels in the existing buildings, or through redevelopment. Monitoring these income shifts in a community over time can help to identify properties that are most at risk of losing their affordability when the subsidy compliance periods end. More than 1,600 deed-restricted units that will expire over the next 2 decades are in census tracts that had a 20%+ increase in median household income between 2012 and 2017.

% Change, Median Household Income, 2012 to 2017, by Census Tract



Source: DHCA, NHPD, HUD, U.S. Census Bureau 5-Year American Community Survey

Risk Criteria | Properties Most At-Risk

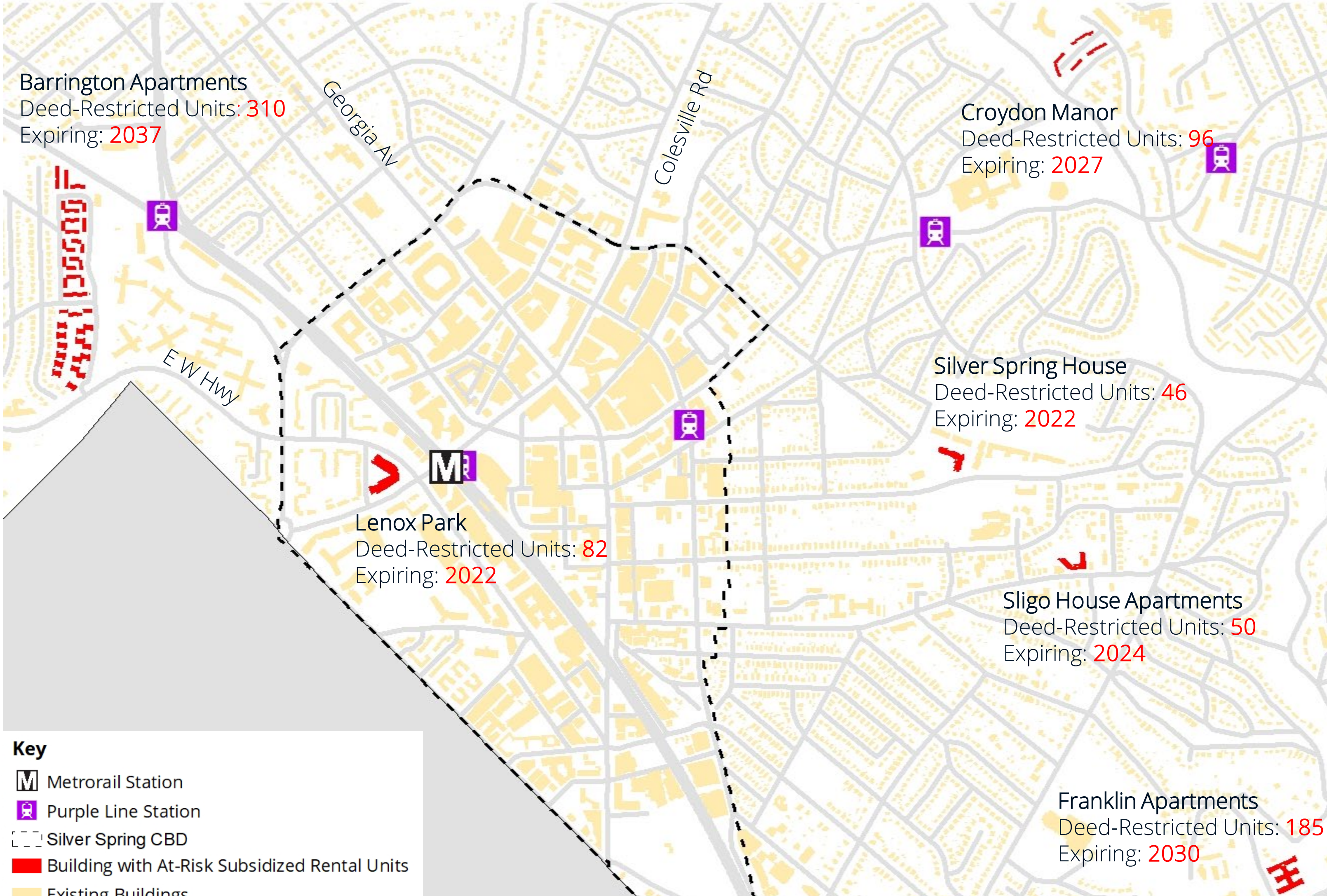
Based on the risk assessment, there are about 1,400 deed-restricted units that are the most at risk of losing affordability when their respective subsidy compliance periods expire over the next 2 decades. Notably, all these higher risk units are affordable below 60% AMI, many of which are at or below 30% AMI. All the higher risk units are owned by for-profit companies, have structures that were built 30+ years ago, and are located in neighborhoods with upward rent trends. Many of these neighborhoods are along the Metrorail and Purple Line corridors and have experienced increased redevelopment activity in recent years. Most of these higher risk units are subsidized through either LIHTC or Section 8. More than half of the higher risk units are located in and around the Silver Spring CBD.

2020s/2030s Subsidy Expirations, Higher-Risk Properties

									Census Tract Trends (2012 to 2017)	
Property Name	Subsidy Expiration	Subsidized Units	<30%	40% - 60%	60% - 80%	Rail Transit < 1 mile	Ownership Type	Building Age (Years)	Median Rent	Median HH Income
Heritage House	2021	100	100	0	0	Yes	For-Profit	39	13%	7%
Silver Spring House	2022	46	0	46	0	Yes	For-Profit	57	9%	1%
Lenox Park	2022	82	0	82	0	Yes	For-Profit	29	7%	1%
Sligo House Apartments	2024	50	0	50	0	Yes	For-Profit	61	9%	1%
Croydon Manor	2027	96	0	96	0	Yes	For-Profit	71	7%	11%
Fields At Bethesda	2029	369	0	369	0	Yes	For-Profit	67	9%	-3%
Franklin Apartments	2030	185	185	0	0	Yes	For-Profit	65	16%	26%
Fields Of Gaithersburg	2031	168	0	168	0	No	For-Profit	46	20%	15%
Barrington Apartments	2037	310	125	185	0	Yes	For-Profit	68	24%	-4%

Source: DHCA, NHPD, HUD, MD Dept. of Assessments and Taxation, Montgomery County Property Tax Records, Census Bureau 5-Year ACS

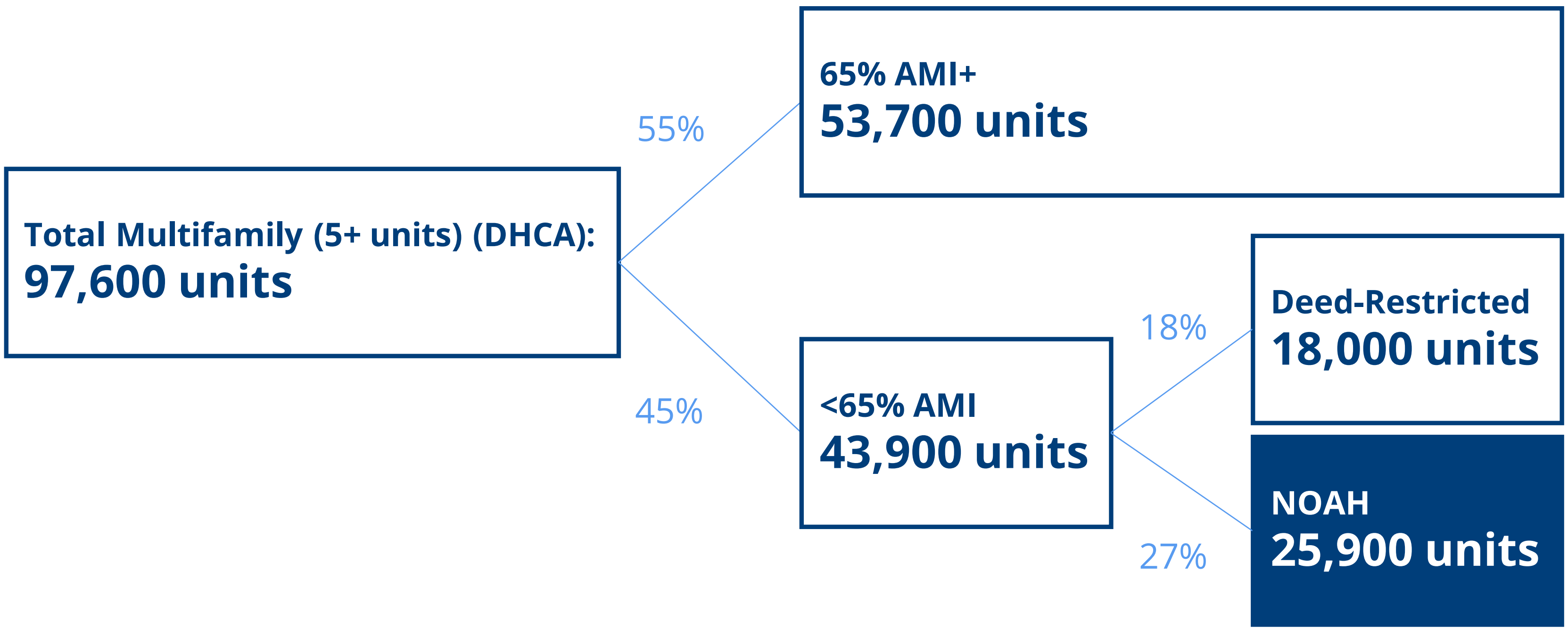
Risk Criteria | Properties Most At-Risk



Source: DHCA, NHPD, HUD, MD Dept. of Assessments and Taxation, Montgomery County Property Tax Records, WMATA, MDOT

Naturally Occurring Affordable Housing

80% of the County's multifamily housing stock is unrestricted—subject to market forces. 35% of these units (25,900 units) rented for less than 65% of AMI and are classified as naturally occurring affordable housing (NOAH).



Sources: DHCA, ACS 2018 1-year

NOAH | Key Takeaways

Montgomery County's rental housing stock is made up of **deed-restricted** and **unrestricted** housing units. While all deed-restricted housing is affordable at or below the income levels required by the program, unrestricted housing rents are subject to market forces. Factors like citywide rent pressure, unit quality, age, and other unit-, building-, and neighborhood-level attributes influence how much a landlord can charge in rent.

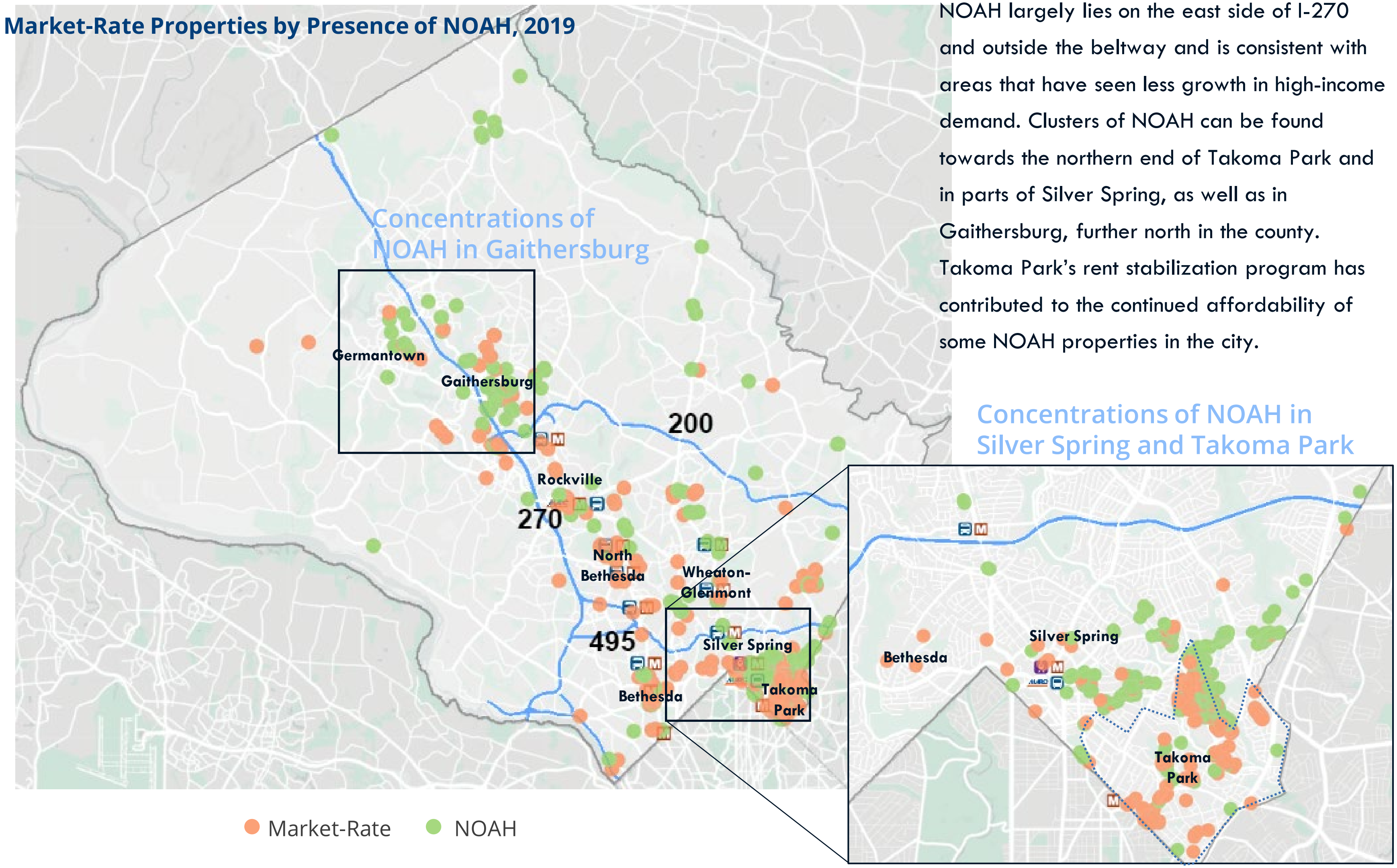
25,900 units are currently affordable to households earning at or below 65 percent of AMI. The unrestricted units at these rent levels are considered to be *naturally occurring affordable housing*.

Key Takeaways

- **78% percent of all NOAH housing was built before 1990, with a plurality built from 1960 to 1989.**
- **Between 7,500 to 11,000 units of NOAH are projected to be lost between 2020 and 2030.**
- **The largest stock of NOAH is in smaller buildings—with fewer than 20 units.**
- **NOAH largely lies on the east side of I-270 and outside the Beltway and is consistent with areas that have seen less growth in high-income demand.**
- **Property ownership transfers correlate closely with rent shifts and loss in NOAH.** Between 2010 and 2019, NOAH properties made up over half (57%) of property transfers of non-deed-restricted buildings.
- **Proximity to transit is a strong signal for loss in units under $1250, especially for stations inside the beltway.**

NOAH | Location

Market-Rate Properties by Presence of NOAH, 2019



NOAH largely lies on the east side of I-270 and outside the beltway and is consistent with areas that have seen less growth in high-income demand. Clusters of NOAH can be found towards the northern end of Takoma Park and in parts of Silver Spring, as well as in Gaithersburg, further north in the county. Takoma Park's rent stabilization program has contributed to the continued affordability of some NOAH properties in the city.

Source: DHCA

NOAH | Establishing Risk Criteria

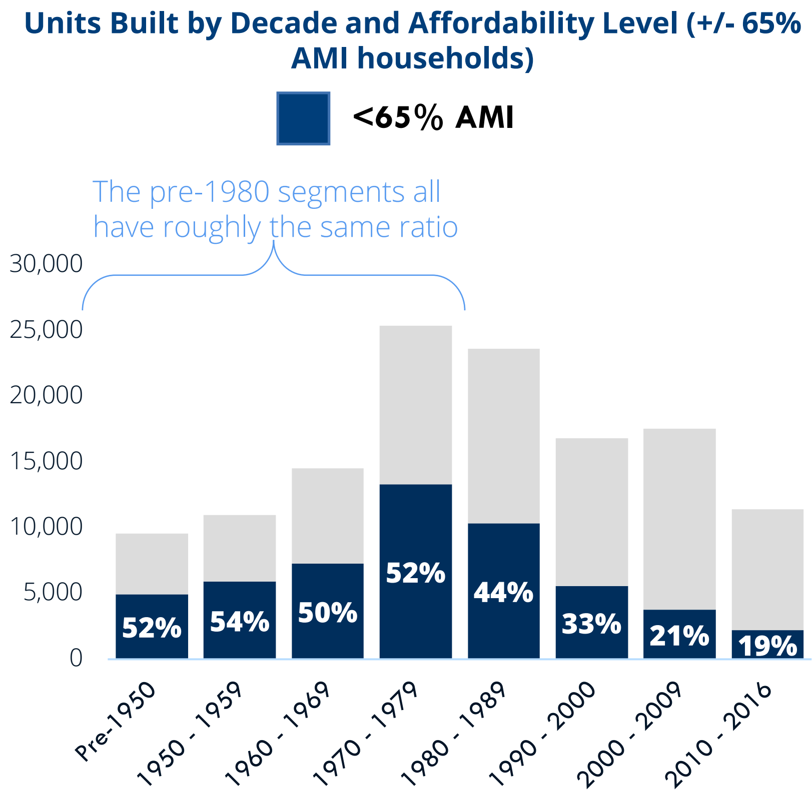
Through a multiple-regression we found the first three criteria below to be the leading historical indicators of NOAH loss in the long term, analyzing rent trends since 2000. These were the key indicators we used in predicting future NOAH loss.

We also examined correlations with several other criteria whose additional effects on rent growth (beyond correlations with age, type, location) are less evident or consistent; these merit consideration and inclusion when evaluating risk.

Independent Variables ***Source**: Assessment Database*	**Dependent Variable** ***Source**: DHCA*
• Building Age • Building Type and Size • Location—proximity to transit • Renovation • Property Transfers • Income Trends • Owner Type	DHCA rents per SF – translated to Affordable versus not at 65% AMI

Sources: DHCA, ACS 2018 1-year

78% of units affordable to households earning up to 65% AMI were built before 1990.



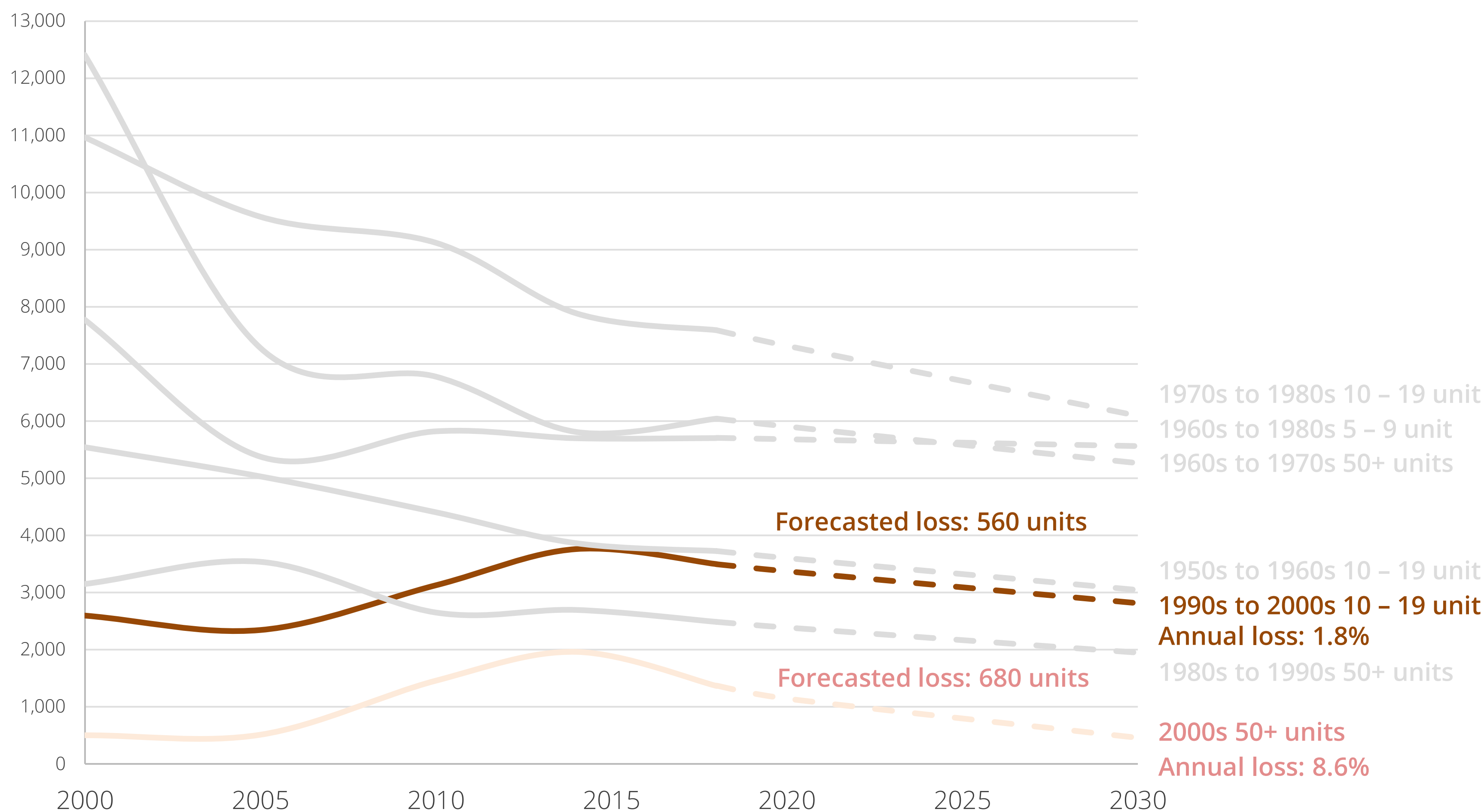
Sources: DHCA, ACS 2018 1-year, CoStar

NOAH inventory in the County is relatively old overall, with the median unit built in the late 1960s and early 1970s. Of the housing stock, more than three in four were built more than 30 years ago, and almost half were built in the 1960s and 1970s. As this inventory continues to age, maintenance, repair and redevelopment are increasingly the higher risks for these units, as both affordability and safety of the unit are required outcomes.

As market pressure increase, these units are unlikely to remain affordable. Private investors are increasingly buying older housing stock to renovate or redevelop. The average per-unit cost to investors for buildings has increased more than 9% annually between 2010 and 2020.

Risk Criteria | Future Trends by Building Typology

There are fewer newer NOAH units (built after 1990s), but they are losing units at a faster rate



Sources: DHCA, ACS 2018 1-year

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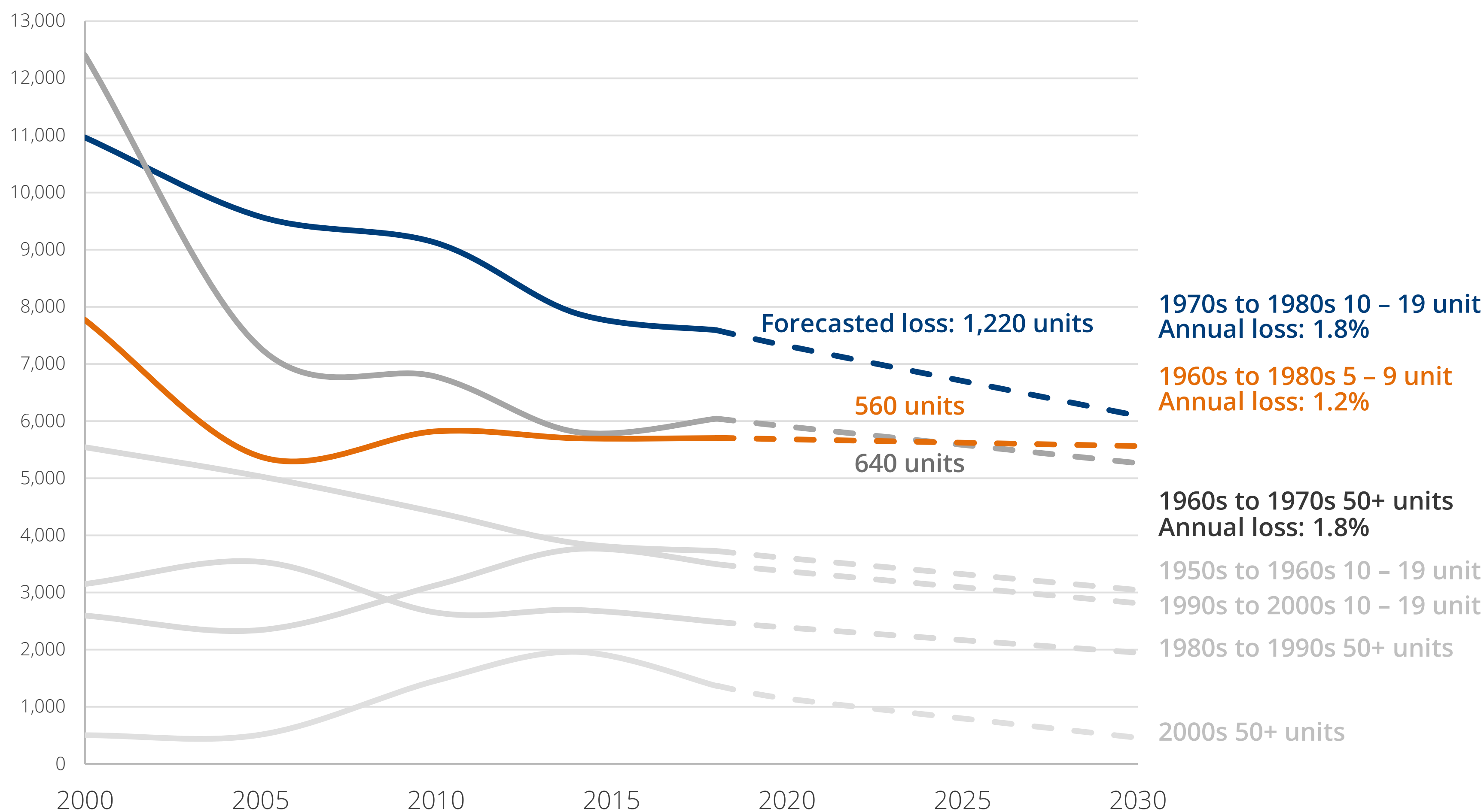
Risk Criteria | Future Trends by Building Typology

Older units built between the 1960s and 1970s are projected to be lost slower rate, but account for a larger share of lost units.

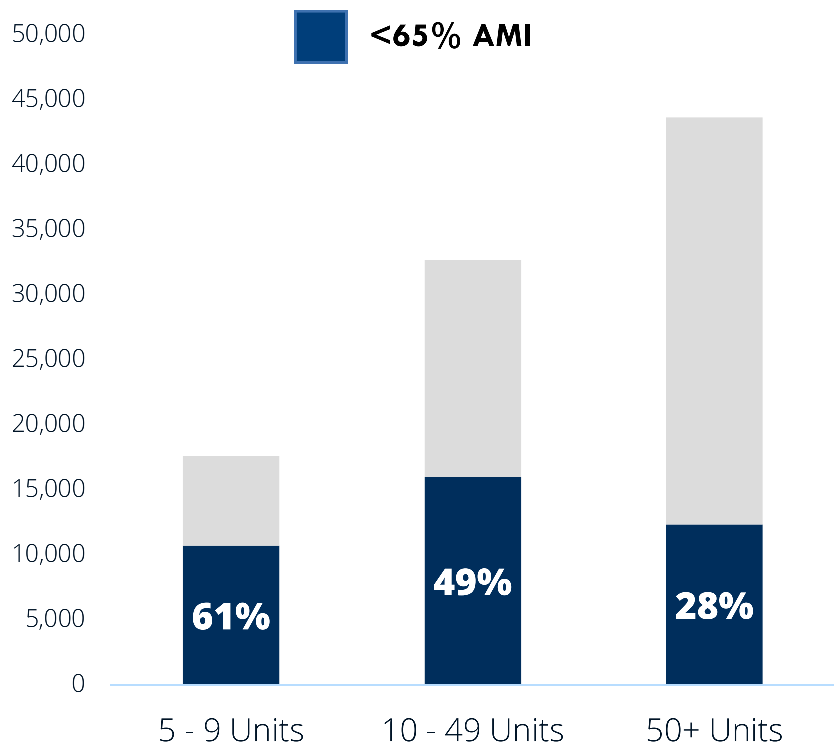


Sources: DHCA, ACS 2018 1-year

Risk Criteria | Building Size

Over half of units in buildings with fewer than 50 units are affordable to households earning up to 65% of AMI.

Units Built by Decade and Affordability Level (+/- 65% AMI households)



Sources: DHCA, ACS 2018 1-year

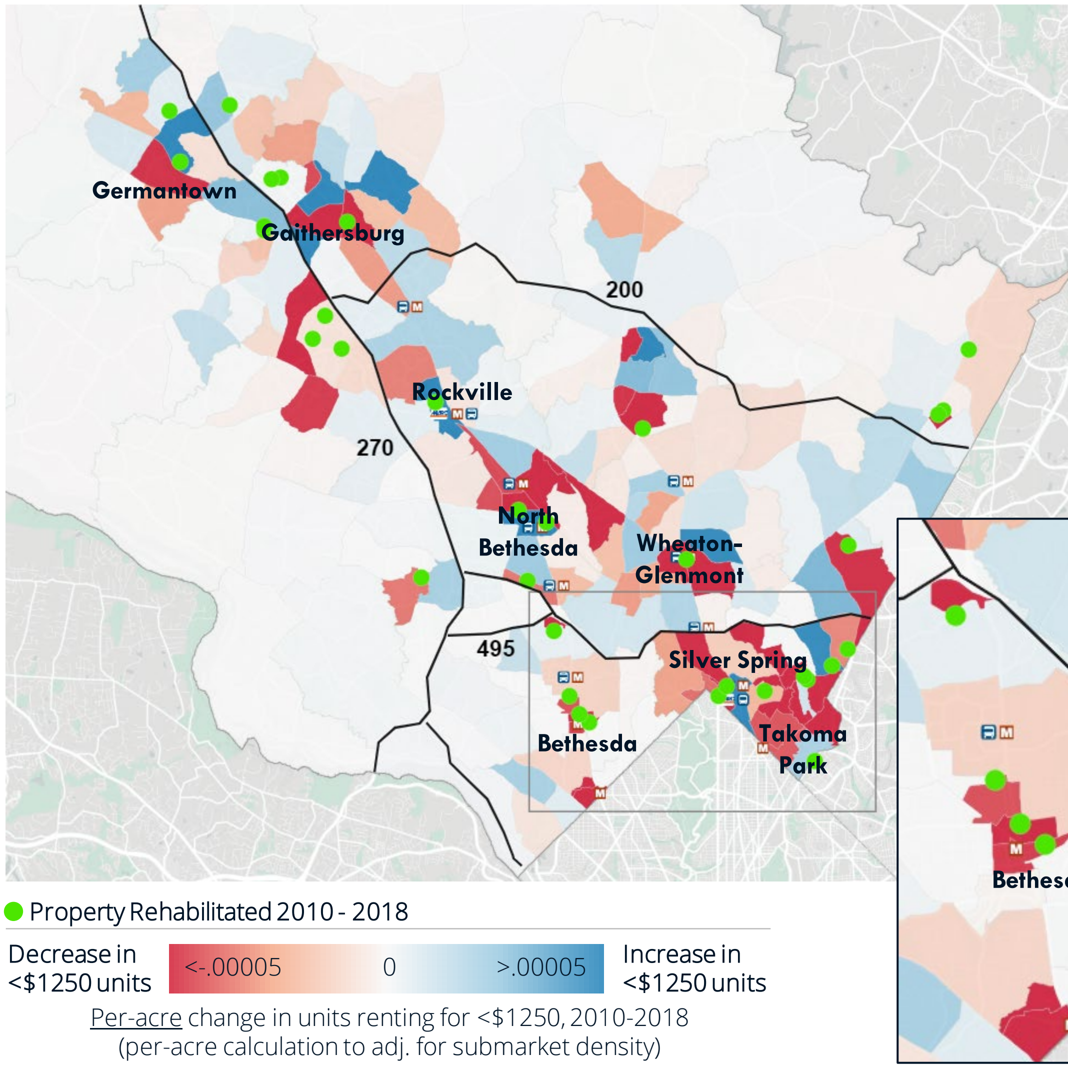
When accounting for deed-restricted units, affordable units are more likely to be in in smaller properties than larger ones. This is especially true for 5 – 9 unit housing structures within the Beltway.

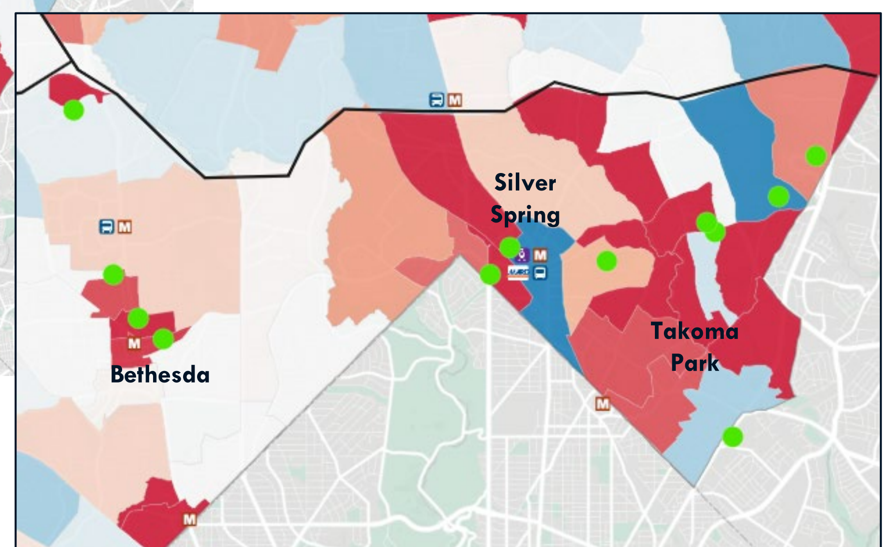
As the number of units in a multifamily rental property increases, the likelihood that the property includes unrestricted NOAH units decrease. Only 28% of units in buildings with 50+ units are naturally affordable. This is likely due to the capital structure and presence of professional building management in these properties that expect a steady annual increase in the property's income.

Single-family and small multifamily units (1 – 4 units) were not part of the NOAH analysis but have an affordability share of around 60%, similar to the 5-9 unit housing structures.

Shift in Rental Units Priced $1250 and Below, 2010 – 2018 + Properties Rehabilitated Between 2010 – 2019

The concentration of properties that have undergone significant renovation (as recorded in CoStar) does not perfectly correlate with submarket rent trends. Rehabilitated properties correlate more closely to loss of NOAH in submarkets closer to the beltway, whereas in outer submarkets, that correlation is less clear.





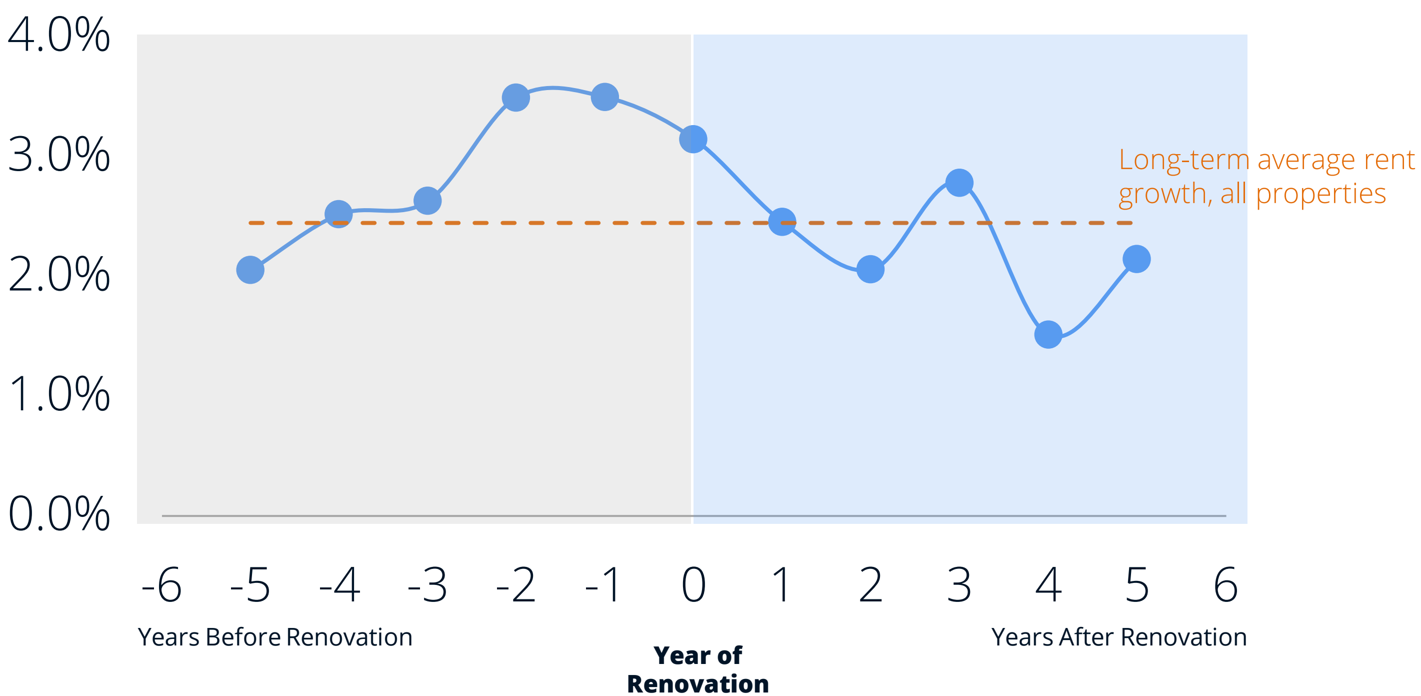
Sources: 2018 ACS 5-Year Estimates; CoStar

Risk Criteria | Rehabilitation

Looking at time series rent trends for individual rehabilitated properties, rehabilitation does not appear to be a leading indicator of NOAH rent growth. On average, for properties that underwent rehabilitation, rent growth peaked in the two years before the date of renovation, but rent growth fell back to average or below-average rates post-renovation.

This suggests that owners are likely to raise rents even without a renovation, especially if there is enough rent growth pressure within a submarket to justify an increase in rents without capital investments, **likely to sell their properties.** Rehabilitation may then be pursued after a period of higher rents and greater cash flow, and to sustain a continued growth in rents.

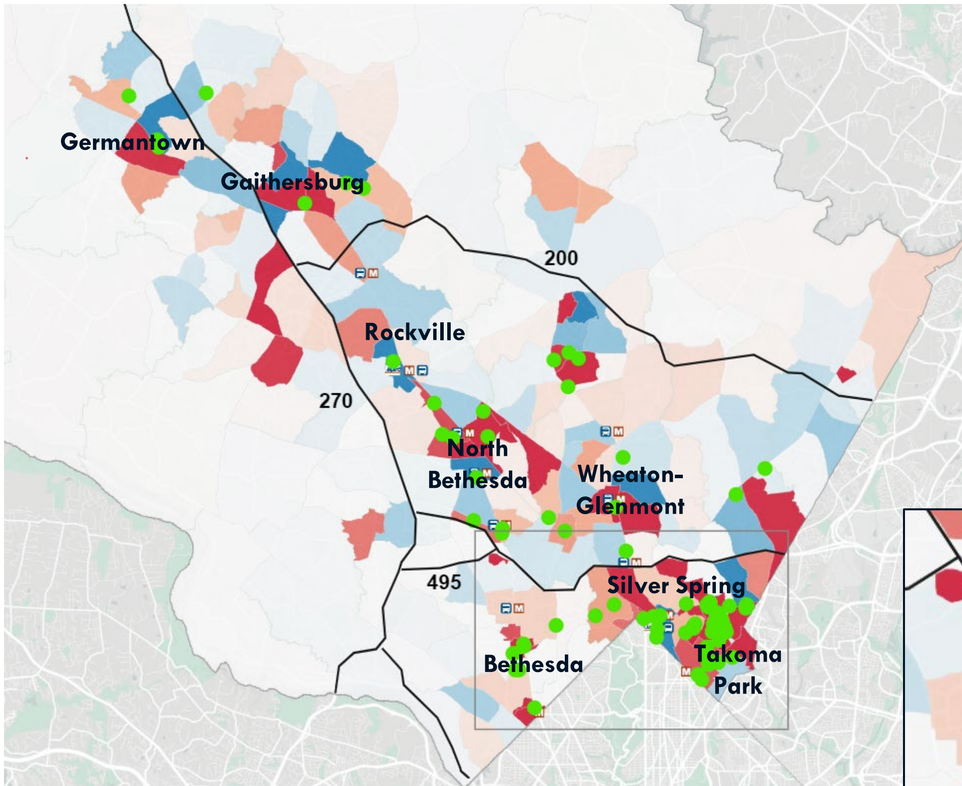
Average Rent Growth Relative to Year of Renovation, Rehabbed Properties in DC-MD-VA Metro Area*



*Regional average used such that analysis captures higher and more significant volume of data on rehabbed properties.
Source: CoStar

Risk Criteria | Property Transfers

Shift in Rental Units Priced $1250 and Below, 2010 – 2018
+ Properties With a Transfer in Ownership Between 2010 – 2019



● Property Transferred 2010 - 2019

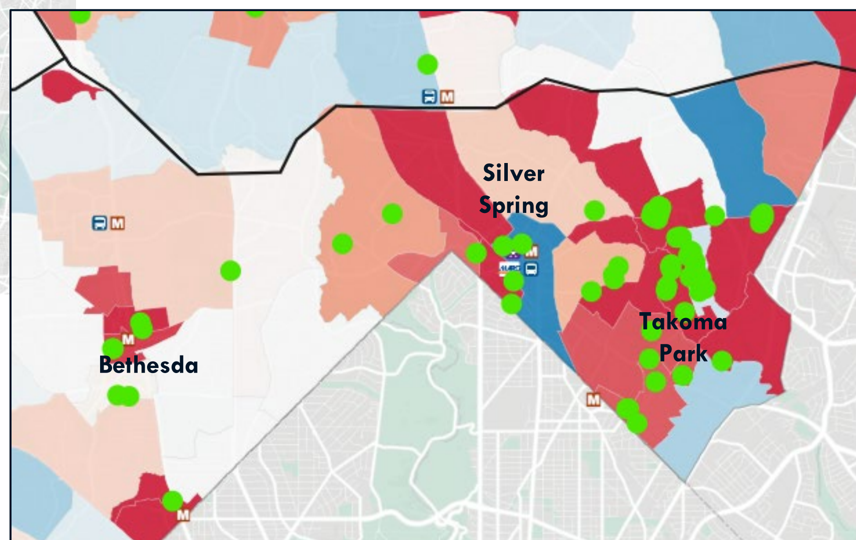
Decrease in <$1250 units | Increase in <$1250 units

Per-acre change in units renting for <$1250, 2010-2018
(per-acre calculation to adj. for submarket density)

Sources: 2018 ACS 5-Year Estimates; MoCo Parcel Database; DHCA Data

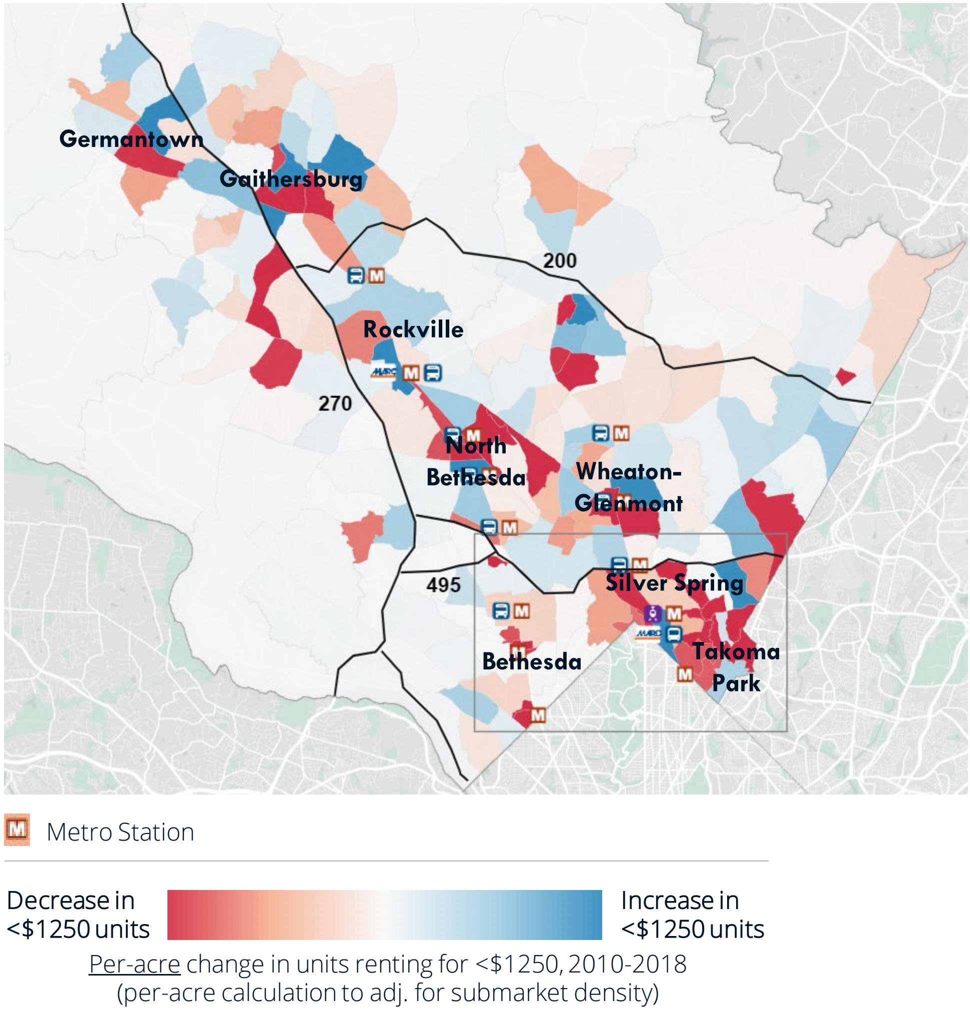
Unsurprisingly, property ownership transfers correlate closely with loss in low-rent units. This correlation makes a case for a robust tenant opportunity to purchase program, so that there is a chance to intervene.

Moreover, a *majority* of property transfers in Montgomery County entail NOAH properties: between 2010 and 2019, NOAH properties made up 57 percent of property transfers of non-deed-restricted buildings. This indicates that NOAH properties are a target investor product within this market.



Risk Criteria | Proximity to Transit

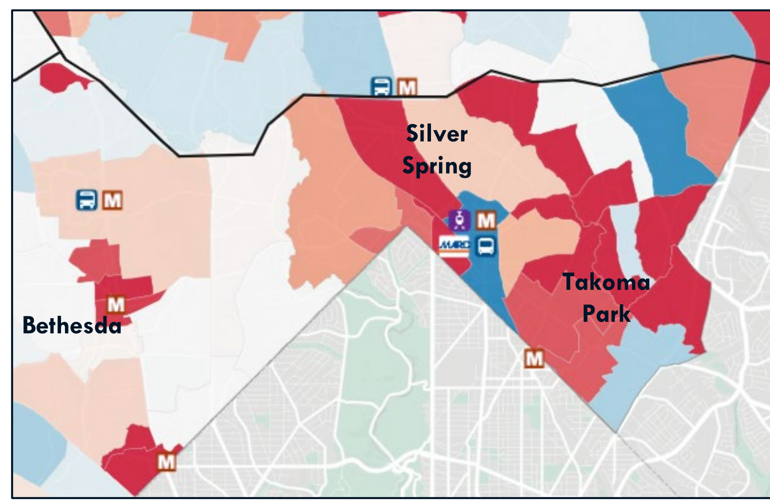
Shift in Rental Units Priced $1250 and Below, 2010 – 2018 + Existing High-Capacity Transit Facilities



Sources: 2018 ACS 5-Year Estimates; MoCo Parcel Database; DHCA Data

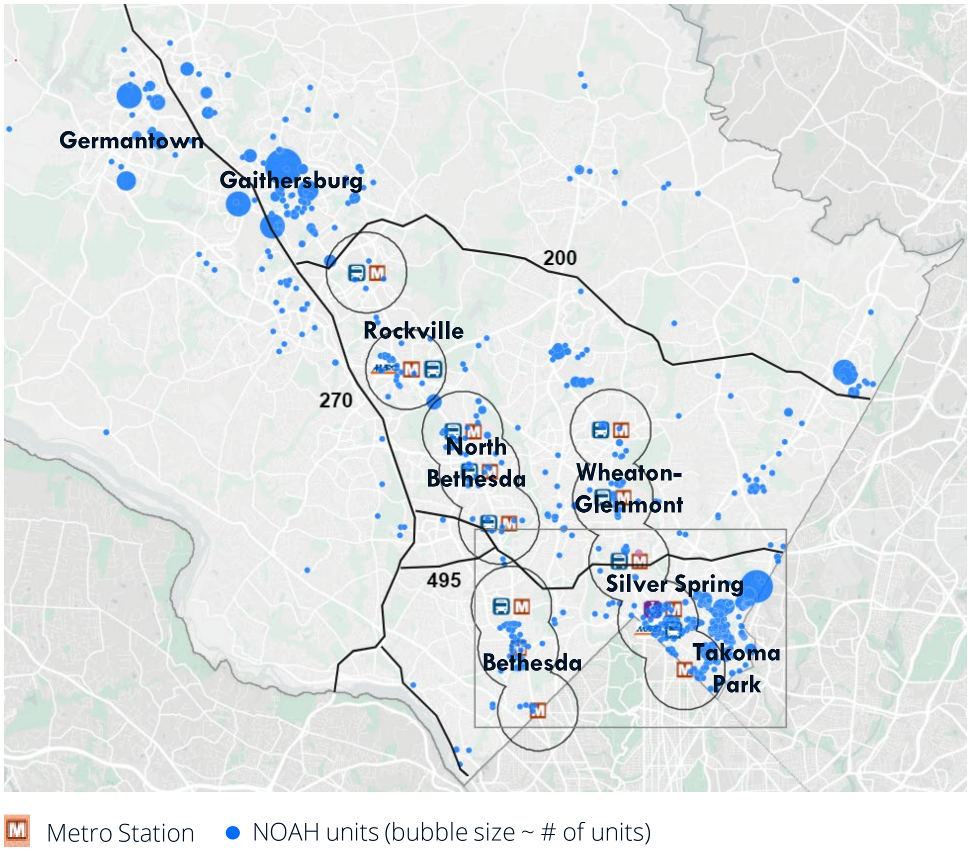
Proximity to transit is a strong signal for loss in units under $1250, especially for stations inside the beltway.

While proximity to transit results in lower personal vehicle usage, greater access to amenities and jobs, and other positive externalities, safeguards are often required to ensure that property surrounding transit investments remain affordable to existing families. According to the Center for Neighborhood Technology, residential property values perform more than 40% better when located within a half-mile of public transportation and retain this value when compared to other properties.



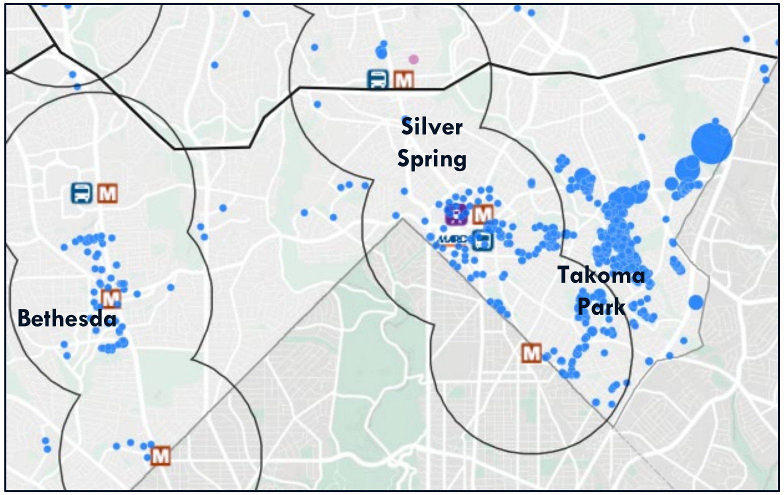
Risk Criteria | Proximity to Transit

Inventory of NOAH Properties
+ 1-Mile Radii Around Existing High-Capacity Transit Facilities



Roughly 2,300 (or 8% of all NOAH units and 2% of the total housing stock) are “at risk” due to proximity to transit.

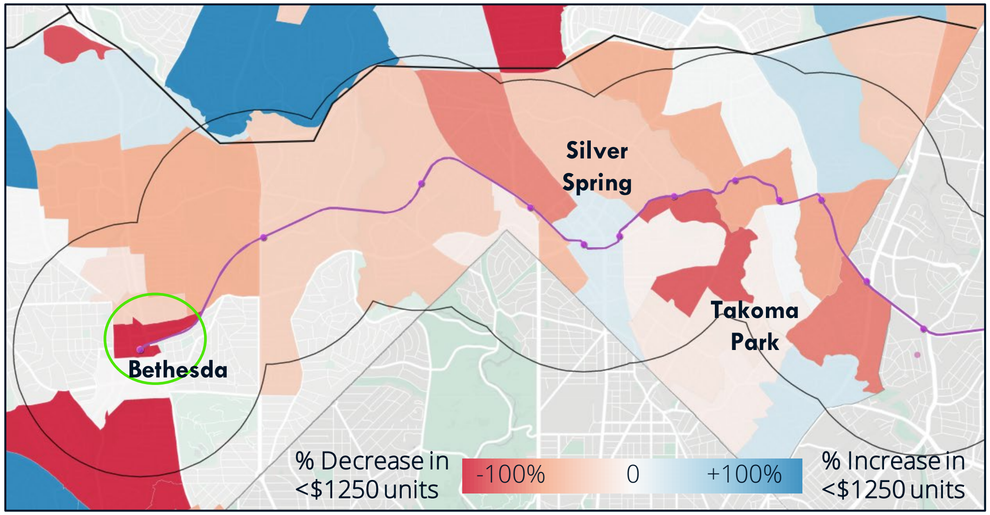
Market-rate properties that contain NOAH and are located within a mile of transit tend to be larger in size, with an average of 72 units versus 55 units total in each property (including market-rate units renting for above and below rents affordable to 65% AMI households). These transit-proximate NOAH properties have a lower average number and share of actual NOAH units within the property—NOAH properties near transit have an average of 27 NOAH units (or 37% of all market-rate units) whereas NOAH properties outside of the one-mile radius have an average of 38 NOAH units (or 69% of all market-rate units).



Sources: 2018 ACS 5-Year Estimates; MoCo Parcel Database; DHCA Data

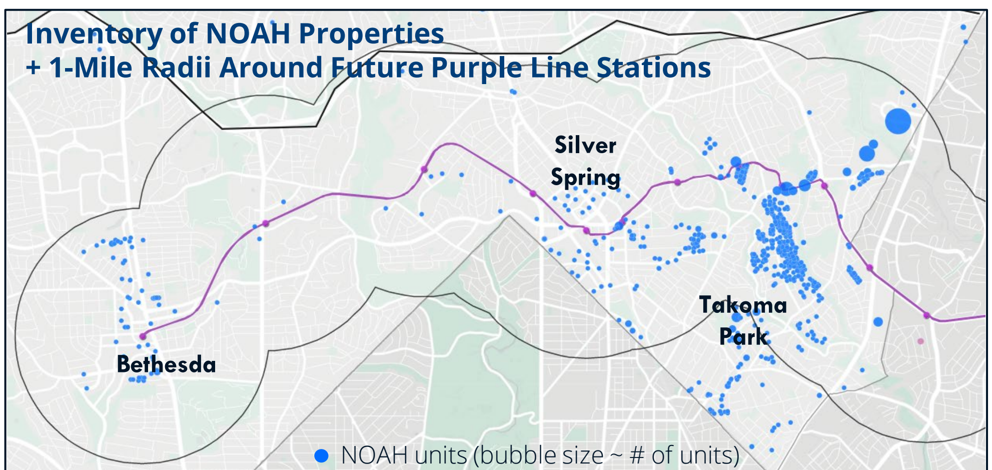
Risk Criteria | Proximity to Transit – Purple Line

Percent Shift in Rental Units Priced $1250 and Below, 2010 – 2018
+ Prospective Purple Line Stations



Purple Line

Inventory of NOAH Properties
+ 1-Mile Radii Around Future Purple Line Stations



Sources: 2018 ACS 5-Year Estimates; MoCo Parcel Database; DHCA Data

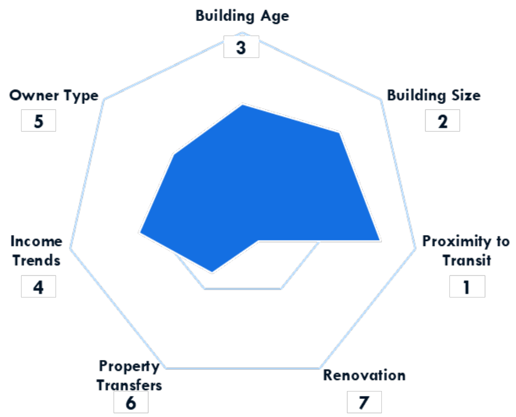
Areas along the planned Purple Line have already demonstrated a rapid decrease in low-rent units in the past decade. The loss of low-rent units has been most rapid around the Bethesda Metro station (see green circle).

The future Purple Line will add additional stress to the existing NOAH stock. Roughly 5,200 (or 19 percent of) NOAH units are located within a 1-mile radius of future Purple Line stations. About a quarter of these units (or 1,400 units) are already located within a mile of an existing high-capacity transit facility, but the Purple Line will affect an additional 3,800 NOAH units, largely in areas further to the east, where a loss of NOAH units has not been as pronounced as in the west.

With the knowledge that proximity to transit will incentivize and accelerate the loss of NOAH, policies such as rent stabilization—the efficacy of which has been evident in Takoma Park—will be important in preserving affordable units in desirable and accessible locations.

Based on our findings, proximity to transit, building size, income trends, and building age are the greatest risk indicators for NOAH units to lose affordability.

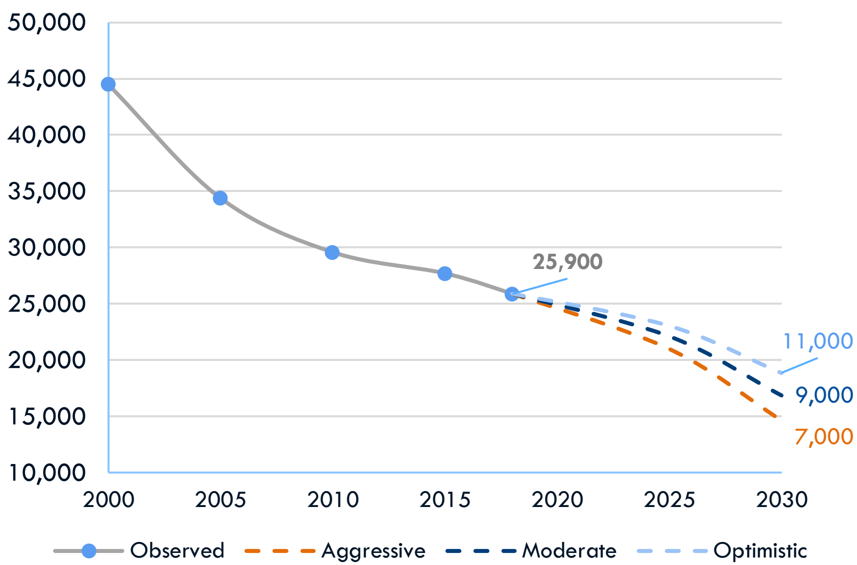
	Indicator
Building Age	While we did not find a linear relationship, we found that older units built between the 1960s and 1970s have the greatest risk for redevelopment or increase in prices as the neighborhood around them shifts.
Building Size	Smaller buildings are more likely to be affordable, but are losing affordability rapidly as 5 – 9 unit buildings are sold to larger investors. Larger properties that are affordable are most likely to be deed-restricted.
Proximity to Transit	Proximity to transit and new infrastructure is the strongest indicator for increase in assessment land values and rents, although jurisdictional zoning and transit access (not just proximity) remain key confounding variables.
Renovation	Although a large capital investment suggests an increase in future revenue, the data remains unclear on the quantitative effect on rents in Montgomery County. More longitudinal data may be required to assess long-term impacts.
Property Transfers	Property transfers and sales are a lagging indicator of NOAH risk—as investors see increasing rents, more transfer activity occurs.
Income Trends	While the analysis considered multiple demographic trends, changes in tract-level income shows the greatest risk of NOAH loss.
Owner Type	Consistent with findings around building size, larger property owners (with 10+) units tend to own properties at risk of loss.



Sources: DHCA, ACS 2018 1-year

Based on these criteria, we forecast a loss of NOAH between 7,000 – 11,000 units by 2030.

Properties classified as NOAH 2000 – 2030 (forecast)



Using the weighted coefficients of each of the analyses for the factors detailed in the previous section, we forecast a loss of 7,000 – 11,000 NOAH (non-income restricted) units by 2030. These losses are estimated to be in the following typologies, categorized by decade built and size of building.

Common NOAH Typologies by Category

Typology	Total Units <65% AMI	Median Rent 2018	Annual rent Growth (2010 - 2018)
1970s - 1980s 10 - 19 unit	5,080	$1,583	0.78%
1960s - 1970s 50+ unit	4,046	$1,571	0.56%
1990s - 2000s 10 - 19 unit	2,342	$1,671	0.18%
1960s - 1980s 5- 9 unit	3,817	$1,698	0.66%
1950s - 1960s 10 - 19 unit	2,493	$1,513	1.14%
2000s 50+ unit	917	$2,122	0.34%
1980s - 1990s 50+ unit	1,662	$1,800	0.17%
Total	**20,357**		

Sources: DHCA, ACS 2018 1-year

Preservation Framework

Preservation Framework| Overview

This section will assess the County's approach to preservation— along with the policies, programs, and resources available to prevent the erosion of the housing stock affordable to lower-income households.

For the purpose of this analysis, **preservation is defined as any action that extends the deed-restricted status of an affordable rental housing unit or converts an unrestricted naturally occurring affordable housing (NOAH) unit to deed-restricted to ensure affordability remains in place.**

Under this definition, successful preservation is tied to the net number of affordable units in each area and at a specific affordability/AMI level, and not necessarily tied to the ongoing affordability of a specific unit or building. Thus, a total site redevelopment that provides for one-for-one replacement of affordable units at the same income level (or at deeper levels of affordability) would be an example of a successful preservation intervention.

Conversely, it would only be a partial success if a physical structure is maintained/improved, but post-rehabilitation affordability was at 60% AMI instead of 30% AMI (unless such deeply affordable units were replaced elsewhere).

Potential loss by 2030:

7,000 – 11,000

NOAH units estimated at risk of loss

1,400

Deed-Restricted units expiring

Preservation Framework| Unit Loss

There are four key ways in which a housing unit can be lost from the affordable stock. Each has different implications for how we approach preservation.

Physical Deterioration	As a NOAH or deed-restricted affordable property ages, there is insufficient investment in the property to maintain habitability, and the property is eventually removed from the building stock. This can result from insufficient cash flow from operations, poor management and/or intentional neglect.
Erosion of affordability via rent increase	If rents in NOAH properties increase faster than tenant incomes, eventually some rental units will no longer be considered "affordable," despite no other changes to the property, building, or business model.
Value-add Investment	In response to market demand from middle- and high-income rental properties, NOAH or expiring deed-restricted properties may undergo light-to-moderate rehabilitation to improve the property to be repositioned in the rental market or convert to for-sale condominiums. This process may be initiated by a transfer in ownership.
Redevelopment	In areas where the market can support redevelopment, an owner may completely redevelop a NOAH or expiring deed-restricted property, which can include a full rehabilitation, demolition and new construction, or a combination of both approaches. Such properties are generally targeted at the top of the market to offset the major investment in the property.

Preservation Framework| Preservation Approaches

There are two primary conditions required to preserve a property:

1. Achieve a sustainable financial position.	The property must generate a net operating income (NOI) to sustain operations and repairs. If a property cannot sustain itself through NOI, it is at risk of being lost through lack of upkeep or be sold through a distressed sale.
2. Protected from exposure to market pressure.	There are a two key ways to ensure that properties are not exposed to existing market pressures: • A legal restriction, policy or loan agreement that regulates the increase of rent on the property; or • Transferring ownership to non-profit motivated owners (mission-oriented nonprofits, tenant ownership.)

There are three primary intervention points to preserve buildings: change in **ownership**, **recapitalization**, and **redevelopment**.
When a property is bought or sold, facilitating transfer to mission-driven ownership can restrict rent increases. The property must generate a net operating income (NOI) to sustain operations and repairs. If a property cannot sustain itself through NOI, it is at risk of being lost through lack of upkeep or be sold through a distressed sale.

Preservation Framework| Policy Categories

There are four key policy categories in which different permutations of preservation approaches can be combined to develop a sustainable preservation framework for Montgomery County.

Land use and planning	Leveraging the rules governing or guiding development within a jurisdiction (including zoning codes and area plans) to incentivize or require preservation of affordability.
Tenants' Rights	Leveraging the rules that govern how various stakeholders (owners, property managers, developers) participate in the market to preserve affordability and protect tenants.
Subsidy: • **Capital Financing** • **Operating Subsidy and Cost Reduction**	• Providing the financial resources necessary to undertake preservation interventions. • Operating subsidy/cost reduction: Offering incentives and resources that make it financially feasible for landlords/owners to offer reduced rents to lower-income tenants.
Strategy and outreach	Analyzing preservation needs, opportunities, approaches, and interventions in the local context; and coordinating and executing efforts (often across agencies) to achieve identified goals and targets.

The most appropriate preservation approach and intervention is likely to depend on multiple factors, including but not limited to: the type of unit (NOAH, expiring deed-restricted); risk of loss; most likely loss type(s); property characteristics (scale, building typology, location, redevelopment potential); and priorities for resource allocation. **All these tools will be required for an effective preservation framework.**

Preservation Framework| Summary of Loss Types

	Physical Deterioration	Erosion of Affordability via Rent Increase	Value-Add Investment	Redevelopment
Risk in Montgomery County	**Minimal.** This type of loss is more commonly associated with weak housing markets or submarkets where rents are low (limiting the upside of upkeep/investment in a property) and/or redevelopment potential is minimal. Absent a major downturn in the regional housing market, risk related to this issue is limited to the unlikely scenario in which existing rent-restricted affordable or public housing properties with long-term/permanent use restrictions lack access to the capital necessary to rehabilitate the property for a length of time sufficient to exhaust all reserves.	**Significant.** Consistent with trends across the DC metropolitan region, rents of existing multifamily properties have on average been increasing. Increases in the number of renter households, increases in the number of higher-income renter households, and the failure of regional rental supply to increase commensurate to supply have contributed to the upward trajectory of market prices.	**Significant**, similar to ***Erosion of Affordability via Rent Increase.***	**Significant,** though concentrated in certain submarkets. For currently cash-flowing properties, the strength of the Montgomery County rental market often means it is more profitable to defer redevelopment and either continue to gradually push rents upward or undertake the "Value -Add" approach. Risk of loss of affordable units due to redevelopment is concentrated in the sub-markets where the developer can achieve substantial increases in density
Impact of Loss on Low & Moderate Income Tenants	**Most severe,** with existing residents suffering from poor living conditions and subsequent displacement.	**Substantial.** These units still represent the "lower-cost housing stock" relative to the broader market, even if no longer meeting the technical definition of naturally occurring affordable housing. However, rising rents increase cost burden on lower income tenants, decreasing housing stability, and potentially lead to voluntary or involuntary displacement.	**Substantial.** Rent increases in the value-add context tend to be larger and more sudden. The rehabilitation process can directly lead to displacement, as tenants are forced to move out and may not be able to afford a completed, post-renovation unit.	**Substantial.** Redevelopment generally results in the displacement of all tenants in affected buildings.

Preservation Framework| Potential Approaches and Interventions

Potential Approaches and Interventions

Physical Deterioration	Erosion of Affordability via Rent Increase	Value-Add Investment	Redevelopment
Facilitate transfer to mission-driven ownership: • Targeted acquisition capital • **Permanent financing/gap resources** • Transfers of development rights **Rehabilitate property** • Zoning/code barrier removal for non-conformance unrelated to health and safety • **Rehabilitation capital** • **Property tax relief** **Encourage responsible stewardship** • **Code Enforcement** • **Tenant protection policies** • **Landlord outreach/technical assistance**	**Facilitate transfer to mission-driven ownership:** • Targeted acquisition capital • **Permanent financing/gap resources** • Transfers of development rights **Facilitate lower rents in current ownership structure** • **Comprehensive Rental Agreements** • **Property tax relief** • Rehabilitation capital with affordability requirement • Zoning/code barrier removal • **Provide direct rental assistance** • Master lease units • Rent regulation/stabilization*	**Facilitate transfer to mission-driven ownership:** • **Right-of-first-refusal/opportunity to purchase laws** • Targeted acquisition capital • Transfers of development rights • **Permanent financing/gap resources** **Facilitate lower rents in current ownership structure** • **Comprehensive Rental Agreements** • **Property tax relief** • Rehabilitation capital with affordability requirement • **Zoning/code barrier removal** • **Provide direct rental assistance** • Master lease units	**Facilitate transfer to mission-driven ownership:** • **Right-of-first-refusal/opportunity to purchase laws** • Targeted acquisition capital • Transfers of development rights • **Permanent financing/gap resources** **Facilitate equitable redevelopment** • **Inclusionary housing requirements/incentives** • **Small area planning incentives** • Site-specific redevelopment incentives • Transfers of development rights • **Permanent financing/gap resources and property tax relief for affordable units** • **Provide direct rental assistance**

Interventions listed in blue are currently utilized by the County to a significant degree.

* *With the exception of Takoma Park*

Policy Inventory and Evaluation

This section provides an evaluation of County's substantial current interventions that support housing preservation.

This process includes four core tasks performed in an iterative manner: an inventory and review of existing County policies; a benchmarking exercise comparing the County's overall approach and specific interventions to national best practices; a benchmarking exercise comparing the County's overall approach and specific interventions to existing needs to identify potential gaps; and an overall evaluation to identify opportunities to fill gaps and increase opportunities to preserve affordable housing.

Local Policies

- Strategy and Outreach
- Capital Financing
- Land Use
- Operating Subsidy
- Policy & Regulatory

Best Practices

- National scan
- Comparable markets

Evaluation

- Assessing existing policy
- New policy opportunities

Gap Analysis

- Benchmarking to unmet needs

Data/information sources reviewed as part of this evaluation include but are not limited to:

- Publicly available websites and program documents;
- Enabling legislation and administrative procedures;
- Planning, budgeting, and outcome reporting documents;
- Interviews and written correspondences with practitioners involved in implementing County interventions;
- Proprietary database of approximately 3,750 records of policies, best practices, and research related to housing, urban planning, and community development.

Policy Inventory and Evaluation | Overview

The following table illustrates the County interventions and other potential policies that could be considered by the County to address preservation needs.

	Strategy and Outreach	Capital Financing	Land Use	Operating Subsidy	Policy and Regulatory
Current County policies	• County-led research, assessment and strategy development • Apartment Assistance Program & Owner/Landlord Supports	• Housing Initiative Fund • HOC Multifamily Mortgage Financing Program	• MPDU program • Area/sector plans • Density averaging	• Rental Agreements • Rental Assistance Payments • Payments-in-lieu-of-taxes (PILOTs)	• Right-of-first refusal policy • Voluntary Rent Guidelines • Tenant protection policies • Landlord-Tenant Mediation • Housing Code Enforcement
Additional resources from 3rd party entities	N/A	• Low-Income Housing Tax Credit and MD DHCD multifamily financing programs • HUD Rental Assistance Demonstration • National Capital Strategic Economic Development Fund • Mission-driven capital/acquisition funds • Minor rehabilitation capital	N/A	• Project-based rental assistance	N/A
Potential new/enhanced interventions	N/A	• Capital for light-to-moderate rehabilitation • Targeted acquisition funding • Value-capture opportunities • Expanded dedicated capital for small-scale acquisition	• Site-specific redevelopment incentives • Lifting some regulatory barriers for smaller projects	• Property tax credits for reduced rents • Master leasing	• Rent regulation (control or stabilization) • Demolition taxes

A comprehensive preservation strategy must involve the redevelopment and replacement of certain units.

Affordable housing funding sources are insufficient to bring all affordable properties under mission-driven ownership and/or to incent existing owners to maintain lower rents. Aside from the fiscal limitations, preservation of existing *buildings* is not always desirable in a growing community, as some buildings may be obsolete and/or specific neighborhoods may be ideal for growth (particularly those near transit and other critical infrastructure/services).

Local governments can leverage the rules governing or guiding development within a jurisdiction to incentivize or require preservation of affordability, primarily through zoning code provisions, area plans, and other elements of the regulatory framework that governs development within the jurisdiction.

A successful strategy:

1. Ensures that new growth is inclusive,
2. Proactively creates opportunities for owners and developers to maintain and/or create new affordable housing units;
3. Removes barriers and perverse incentives that can erode affordability.

The County's inclusionary zoning ordinance is among the most productive in the United States, and planning efforts often proactively account for affordable housing needs in a detailed manner. While this level of detail and planning control may restrict flexibility or add costs, it has generally expanded the number of units that are affordable.

Description

Montgomery County's Moderately Priced Dwelling Unit (MPDU) program is the County's inclusionary zoning policy, requiring a minimum of 12.5% affordability in developments of 20 units or more, and providing additional density incentives to reach higher levels of affordability. Affordable units are generally produced on-site, though the MPDU policy (as stipulated in Executive Regulation 11-18AM) allows for alternative compliance through land transfer, provision of units at an alternative location, or alternative payments.

Maximum rents for MPDU units are initially established based on 30% of the income limit (65-70% AMI), adjusted for household and unit size. Future rent increases must follow the County's Voluntary Rent Guidelines (Slide TBD), which are based on the Consumer Price Index (CPI) for the Baltimore-Washington Metropolitan Area.

Current regulations require a 99-year affordability commitment for MPDU units. However, prior iterations of program regulations required shorter affordability commitments, creating the need for preservation of expiring MPDUs.

Assessment based on Best Practices

The MPDU program is highly productive relative to most inclusionary zoning policies and is critical to ensuring that a portion of new growth is affordable and replaces a portion of affordable units lost from the affordable rental stock.

Given the program's focus on economic integration, alternative compliance is relatively rare. Based on the amount of funding leveraged by HIF, allowing more properties to offer fees-in-lieu could potentially produce more units, but would cut against inclusion goals and rely on the availability of sites and additional funding sources.

The County has successfully utilized several tools to preserve expiring MPDUs. Preservation efforts include entering into Rental Agreements in exchange for DHCA rental assistance payments in the amount of the foregone rent.

Inflation in recent years increased faster than incomes at the lower-end of the income spectrum. As such, tying rent increases to CPI has contributed to some MPDUs becoming unaffordable to households at the targeted income levels. A 2018 evaluation of the MPDU program found that 50% of MPDU renters spent 35% or more of income on housing (though this is not exclusively attributable to indexing issues).

Source: Urban Ventures. "MPDU Program: Analysis of Current Program and Research On Other Localities' Inclusionary Zoning Programs." June 7, 2018.

Description

Area/sector plans that provide aggressive affordable housing incentives/requirements can provide for the replacement/preservation of affordable units in a redevelopment context in conjunction with MPDU inclusionary policies. Montgomery County addresses smaller-area growth and development in a variety of ways, including through sector, neighborhood or area master plans.

Examples of how the plans have been used to advance affordable housing efforts include:

- Conducting affordable housing analysis as part of plan (Long Branch)
- Establish goals for planning areas, such as a no-net-loss of affordable housing (Takoma/Langley Crossroads)
- Rezoning of specific districts to encourage the types of development that generate MPDUs (White Flint)
- Establishing or increasing the relative weight for affordable housing provision as part of public benefit point evaluation (Bethesda, White Flint)
- Establishing the preservation of NOAHs and/or provision of MPDUs above 15% as the top priority for public benefit points (Bethesda)
- Rezoning and/or providing additional height, density, or other land use incentives for affordable housing provision, including higher levels of MPDUs (Bethesda, Takoma/Langley Crossroads, Long Branch)
- Maintaining existing zoning designations with the explicit purpose of discouraging redevelopment of specific NOAH properties (Long Branch)
- Providing provisions for the use of public land (or co-location of public facilities) for community purposes, including affordable housing (Takoma/Langley Crossroads)

Benchmarking Resources:

- Arlington County, VA. "Columbia Pike Neighborhoods Form Based Code." https://building.arlingtonva.us/permits/form-based-code/neighborhoods/.

Land Use and Planning | Area/sector plans

Assessment Based on Best Practices

The County has incorporated a robust set of tools for affordable housing production within various area/sector plans, consistent with national best practices. However, data on the number of affordable units produced or preserved through area/sector planning provisions was unavailable, limiting the scope of the assessment.

Maintaining zoning designations to discourage redevelopment does not necessarily protect against erosion of affordability via rent increase or loss due to value-add investment. In certain market contexts, a lack of additional available density can lead to "downsizing," in which modest apartments are demolished and replaced by luxury for-sale townhomes.

Recommendations

The County could track and analyze data by area/sector plan geography to better evaluate whether affordable housing production and preservation goals are being achieved. This data can be used to calibrate land use incentives (such as density bonuses, parking reductions, etc.) in future planning efforts.

DHCA could be brought into individual area/sector planning processes as a full partner to better coordinate funding and land use interventions.

Plans could allow greater opportunities for market-rate infill in exchange for preserving affordable units. For example, Arlington, VA's Columbia Pike Form-Based Code allows for additional density/height in undeveloped spaces of existing properties (such as surface parking lots) in exchange for preserving a portion of the existing units as affordable, providing longer-term affordability and minimizing near-term displacement of current residents.

Benchmarking Resources:

- Arlington County, VA. "Columbia Pike Neighborhoods Form Based Code." https://building.arlingtonva.us/permits/form-based-code/neighborhoods/.

Description

Flexibility in the allocation of development rights can be utilized to preserve priority existing uses, such as open space, agricultural land, and affordable housing. This flexibility is often referred to as a "transfer of development rights (TDR)," though other forms exist.

Montgomery County has an established TDR policy for preserving farmland and farming in the Agricultural Reserve. **In addition, the Montgomery County zoning ordinance (Article 59-4.5.2) allows floor-area-ratio (FAR) to be averaged between two or more directly abutting or confronting properties in Commercial/Residential zones, two or more non-contiguous properties in CRT or CR zones within a quarter mile, or when located in a designated master-planned density transfer area.** In order to be eligible, development plans must meet or exceed specified "public benefits" point standards. Both sites must be part of the same site/sketch plans.

Assessment Based on Best Practices

TDR and density averaging policies are theoretically promising and have been successfully applied in the context of agricultural/open space preservation. However, successful examples of affordable housing production/preservation via TDR are less prevalent.

No examples of affordable housing preservation using FAR Averaging were identified in Montgomery County, though one example of a successful senior housing construction effort was reviewed. This land use flexibility was not designed for the express purpose of preserving affordable housing. Conversely, the County's agricultural-focused TDR policy had preserved more than 52,000 acres as of 2016.

Based on reviews of national and local literature, provisions requiring both sending and receiving sites to be part of the same siteplan and geographically proximate likely contribute to the limited utility of FAR averaging for affordable housing.

Benchmarking Resources:

- King County, WA. "King County Transfer of Development Rights Bank." https://www.kingcounty.gov/services/environment/stewardship/sustainable-building/transfer-development-rights/bank.aspx
- King County, WA. "South Lake Union, Denny Triangle, & Commercial Core.." https://www.kingcounty.gov/services/environment/stewardship/sustainable-building/transfer-development-rights/receiving/Seattle-tdr.aspx
- King County, WA. "TDR Bank Sales." https://www.kingcounty.gov/services/environment/stewardship/sustainable-building/transfer-development-rights/bank/bank_sales.aspx
- HUD Office of Policy Development and Research. "Transfer of Development Rights and Affordable Housing." September 2009. https://archives.huduser.gov/rbc/archives/newsletter/vol8iss5_2.html

Recommendations

To better enable affordable housing preservation, the County could adopt an affordable housing preservation TDR program. Program development can be informed by the lessons from the more successful County agricultural TDR program. Specifically, the County should consider a more flexible program that designates sending and receiving sites (or neighborhoods) but does not require that both elements be part of the same development effort or be conducted simultaneously.

Precedent: King County and the City of Seattle have created a joint TDR bank that combines the goals of agricultural preservation and new dense urban development. Development rights purchases are coupled with payments for affordable housing, and mixed income properties have been developed through the purchase of development rights. The City of Seattle also has a legacy TDR program focused on affordable housing preservation, using the non-contemporaneous sending/receiving site model. The program helped preserve nearly 1,000 affordable units.

Benchmarking Resources:

- King County, WA. "King County Transfer of Development Rights Bank." https://www.kingcounty.gov/services/environment/stewardship/sustainable-building/transfer-development-rights/bank.aspx
- King County, WA. "South Lake Union, Denny Triangle, & Commercial Core.." https://www.kingcounty.gov/services/environment/stewardship/sustainable-building/transfer-development-rights/receiving/Seattle-tdr.aspx
- King County, WA. "TDR Bank Sales." https://www.kingcounty.gov/services/environment/stewardship/sustainable-building/transfer-development-rights/bank/bank_sales.aspx
- HUD Office of Policy Development and Research. "Transfer of Development Rights and Affordable Housing." September 2009. https://archives.huduser.gov/rbc/archives/newsletter/vol8iss5_2.html

Policy Gap: Express-purpose preservation plans

Potential Intervention	Description	Examples and Precedents
Site- or type-specific redevelopment incentives	Jurisdictions can adopt plans and incentives focused on specific high-importance sites. These can either be conducted in advance of any redevelopment effort or as part of the negotiations with a developer/property owner for site-specific regulatory relief/additional entitlements. Efforts can focus on either an individual property (or neighborhood) or a specific property typology (for example, garden-style apartments near transit/mixed-use corridors). The same regulatory flexibilities described in area/sector planning apply to this intervention as well.	The City of Alexandria, VA adopted the South Patrick Street Housing Affordability Strategy and Residential Affordability Zone to preserve large-scale, deeply affordable properties in a neighborhood at risk of gentrification-related displacement.

Policy Gap: Removing land use, zoning, and building code barriers to efficient redevelopment

Potential Intervention	Description	Examples and Precedents
Proactively address non-conforming properties	Older properties built before the adoption/update of modern zoning codes may have significant nonconformities. Such nonconformities (for example, units above maximum densities, lower parking ratios) may reduce the viability of efforts to preserve affordability in the context of rehabilitation or redevelopment. "Grandfathering in" non-conforming uses and/or creating safe-harbors" for pre-existing non-conforming conditions can make preservation a more viable option. While health and safety efforts are critical, in some contexts it is important to consider the counterfactual – is requiring full compliance preventing some rehabilitation/redevelopment efforts from moving forward, thus preventing incremental improvements in living conditions? Practitioners interviewed for this research identified non-compliance as a challenge in several contexts. Cited provisions included parking ratios, energy codes, and sprinkler requirements. Addressing these issues led to incremental costs and delays to obtain waivers and/or meet updated standards.	Boulder Ordinance 8715 allows for the reconstruction or restoration of non-conforming, permanently affordable properties without having to address compliance issues related to parking, units per acre, amount of open space, or lot area per unit, if the project did not increase non-conformity.

Local jurisdictions can leverage the rules that govern how various stakeholders (owners, property managers, developers) participate in the market to preserve affordability and protect tenants.

A successful strategy:

1. Expands opportunities for mission-driven entities to participate in the market.
2. Provides tenant protections and restricts predatory behavior, particularly in the context of property sale and/or redevelopment.
3. Promotes housing quality, balancing enforcement with assistance to lower-capacity landlords.

Montgomery County has incorporated several effective policy and regulatory tools to advance preservation goals, including rent stabilization and the Right-of-First Refusal to purchase certain multifamily properties. Other interventions support preservation in a less direct, though complementary, manner.

Description

Chapter 53A of the Montgomery County Code grants DHCA, HOC and certified tenant groups a Right of First Refusal (ROFR) to match residential contracts to preserve affordable housing when certain properties are offered for sale. The ROFR provides the County with the right to match a contract in all executed significant terms. The ROFR applies to rental properties built prior to 1981 and in the context of condominium conversions. The total timeline to fully exercise a ROFR is 180 days from the point at which notice of sale was provided to the County.

In lieu of the ROFR, a private owner can offer a plan to retain affordable housing for a minimum of 5 years utilizing the County's voluntary rent guidelines. Acceptance of such plans is at the sole discretion of the County.

Assessment based on Best Practices

In general, ROFR policies make mission-driven entities more competitive when an affordable property is offered for sale, especially in strong markets. Local practitioners spoke to the importance and effectiveness of the ROFR, in conjunction with the County's full suite of capital tools.

The number of ROFR offers submitted to the County dramatically outstrip County resources There were 184 ROFR offers received from 2015-2019, totaling 37,088 units and $7.8 billion in capital, with an average cost per unit ranging from $180K to $240K. During this time, the County facilitated 8 acquisition, 2 agreements not to convert, 10 executed rental agreements, and 8 capital investments with regulatory agreement. Some properties offered for sale included MPDUs with ongoing deed restrictions, obviating the need to exercise the ROFR (see following slide).

Recommendations

The ROFR is an effective tool that can be enhanced by providing additional HIF resources for acquisition and Rental Agreements.

The County could also consider changing the property eligibility date (properties built before 1981) to a later date or indexing the eligibility date to a given property age (i.e., ROFR could apply to all properties built more than 40 years ago). Though newer HIF-subsidized properties must offer the County a ROFR, there are 40,423 market rate units built in the 1980s and 1990s. Nearly 40% of these units are affordable today, but the analysis in section TBD demonstrates that these units are exiting the affordable stock at the fastest rate. If an adjustment to the eligibility date is considered, proactive measures may need to be taken to prevent a rush to sell formerly exempt properties before the change goes into effect.

Recent ROFR Interventions Facilitated by Montgomery County

Properties	FY 2015	FY 2016	FY 2017	FY 2018	FY 2019
Acquisition	1	2	1	4	0
Agreement Not to Convert	1	0	1	0	0
Rental Agreement	2	3	4	0	4
MPDUs	1	3	3	1	0
Capital Investment & Regulatory Agreement	3	1	1	3	0
Total	**8**	**9**	**10**	**8**	**4**

Units	FY 2015	FY 2016	FY 2017	FY 2018	FY 2019
Acquisition	4	18	864	295	0
Agreement Not to Convert	0	0	19	0	0
Rental Agreement	1,390	563	2,098	0	631
MPDUs	379	849	1,391	302	0
Capital Investment & Regulatory Agreement	223	686	40	606	0
Total	**1,996**	**2,116**	**4,412**	**1,203**	**631**

Source: DHCA data

Description

Montgomery County publishes and annually updates Voluntary Rent Guidelines that can inform landlords of what could constitute a "reasonable" rent increase based on the costs of operating and maintaining a property. The guidelines are established using the Consumer Price Index for the Baltimore-Washington Metropolitan Region.

For most properties, the Guidelines are advisory only. However, the County also uses these Guidelines to set a binding limit on rent increases for rental MPDUs and properties under Rental Agreements or receiving other forms of County subsidy.

Assessment Based on Best Practices

As an advisory tool, Voluntary Rent Guidelines are helpful but have limited impact.

The County's use of the Guidelines to limit rent increases in MPDUs and other County-assisted properties limits administrative burden, but can contribute to cost burdens for lower income tenants if CPI increases faster than incomes.

Recommendations

The County could consider whether there are additional low-cost incentives that it can provide for landlords to adhere to the Voluntary Rent Guidelines, in addition to the existing programs of tying rent increases to increases in AMI,

Tenants' Rights | Additional County Policies

Intervention	Description	Local Applicability	Opportunities
Tenant Protection Policies and Landlord Tenant Mediation	Policies that protect the rights of existing tenants can ensure that lower-income households have an opportunity to mitigate any harm associated with the property sale (and potentially rehabilitation/redevelopment). These policies may include just cause eviction and adequate notification standards. In establishing a minimum time standard for transfer of the property, such policies do not preserve housing per se, but can be complementary with opportunity to purchase or other acquisition-focused interventions.	Renter Protection Bill 19-15 (as described in Montgomery County Landlord Tenant Handbook) establishes protections and obligations for both landlords and tenants. Relevant topics addressed include fair housing laws, required and prohibited lease provisions, security deposits, notices, and lease termination, among others. Notably, Montgomery County prohibits source-of-income discrimination, prevents more than a single rent increase over a 12-month period, requires 90 days written notice of rent increases, and two-month notice-to-vacate requirements. The County also provides Landlord-Tenant Mediation services to resolve disputes, divert routine cases outside of the court system, and disseminate information on the rights and obligations of both tenants and landlords.	Given the up-to-180-day process for ROFR execution, tenant notice laws are unlikely to significantly enhance opportunities to preserve for-sale rental properties. The prohibition of source of income discrimination is a best practice that may be particularly beneficial in the context of COVID-19. To the extent that federal, state, and/or local resources are provided for rental assistance (on a temporary or ongoing basis), landlords would be required to accept these payments. It was outside the scope of this evaluation to compare Montgomery County policies from the perspective of tenant rights/protections.
Housing Code Enforcement	Code enforcement measures help preserve housing quality, prevent predatory practices (such as equity stripping preceding a sale) that can harm resident health, and can be used to introduce property owners to County resources that can improve a property (with or without the application of affordability restrictions.	Montgomery County's FY 2020 budget request included more than $4.3 million for code enforcement activities. As discussed in slide TBD, the County's Apartment Assistance Program was established in part to support landlords in bringing properties up to code.	Coordination between the Apartment Assistance Program, code enforcement, and Landlord-Tenant Mediation could be enhanced to identify the most challenging properties for more intensive focus (and potential prioritization if the property is marketed for sale).

Tenants' Rights | Potential New Interventions

Policy Gap	Potential Intervention	Description	Examples and Precedents
Lack of binding tools to limit cost increases in unrestricted properties.	**Rent regulation (control or stabilization)**	Rent regulations refers to a broad suite of policies (often colloquially referred to under the umbrella term "rent control") that limits the rents that private landlords may charge tenants. There can be significant variation in program design related to the applicable properties, the level of oversight in rent setting, and the permitted level of rent increase. The effectiveness of rent regulation is the subject of significant debate among economists and housing practitioners, with proponents focusing on resident stability and skeptics asserting that adverse consequences offset any benefits. Unfortunately, existing empirical evidence focuses on "legacy" programs that bear little resemblance in policy detail to rent regulations most often under consideration today – "circuit breaker" policies that cap annual rent increases at a percentage amount plus inflation.	The City of Takoma Park has a legacy rent control program. Both Oregon and California have adopted statewide rent stabilization laws that cap annual rent increases at inflation plus 7% and 5% respectively. In April 2020, the Montgomery County Council adopted an emergency rent relief bill in response to the COVID-19 pandemic that limits rent increases during or within 90 days following the statewide public health emergency to 2.6% (according to Voluntary Rent Guidelines).
Disincentives to removing older properties from the housing stock	Demolition taxes	Demolition taxes apply when an eligible property type is being demolished and replaced by a less affordable asset class. Demolition taxes can make preservation a more economically viable alternative and proceeds can be used to fund affordable housing activities. Policy exceptions in the case of vacant and dilapidated housing could protect against negative externalities (such as preventing reinvestment in a blighted property) in weaker submarkets where teardowns of modest but viable priorities is less of a problem.	Highland Park, IL has instituted demolition taxes to maintain building stock diversity and disincentivize teardowns.

Jurisdictions and mission-driven developers need a variety of capital tools to execute a comprehensive preservation strategy.

Facilitating transfer to mission-driven ownership and rehabilitating and recapitalizing the property are particularly capital intensive. Despite these costs, there are clear benefits to undertaking these approaches, which can include:

- Directly preserving existing units increases the likelihood that existing low-income and vulnerable tenants will not be displaced
- Some research indicates that preservation using these approaches may be less costly than relying primarily on the new construction of subsidized deed-restricted affordable housing to meet the needs of low-income renters.
- Providing capital for acquisition can have both near- and long-term benefits: preserving affordability today, while serving as a form of "land banking" for future equitable redevelopment efforts.

A somewhat unique element of Montgomery County's capital landscape is the Housing Opportunities Commission's (HOC) status as a housing finance agency. This gives the County an additional source of resources unavailable to many other similarly situated jurisdictions. In its role as developer/owner, HOC also is critical in directly preserving affordable housing.

The main challenge to the County is that preservation needs outstrip the amount of resources necessary to bring all or most at-risk ownership under mission-driven ownership or long-term use restriction. In the last decade, the County preserved 6,189 units. Though this number is impressive, simply maintaining current production would result in the further erosion of the affordable rental stock. As such, success likely relies on a combination of approaches, including increasing resources, identifying lower-cost preservation opportunities, creating incentives for profit-oriented owners to maintain lower rents, and utilizing land use and planning tools to leverage new growth in support of preservation.

A Successful Strategy:

1. Local practitioners have a robust set of resources to facilitate preservation efforts.
2. Stakeholder interviews and benchmarking indicate that the resources are substantial in amount, well-managed, and efficiently coordinated.

Sources: Jeffrey, Lubell, and Sarah Wolff. "Variation in Development Costs for LIHTC Projects." Abt Associates, August 30, 2018. https://www.ncsha.org/wp-content/uploads/2018/09/Final-LIHTC-Costs-Analysis_2018_08_31.pdf.

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Policy Inventory and Evaluation | Capital Financing (continued)

This matrix illustrates common sources and uses of capital for preservation.

	LIHTC	HFA Products	Local Trust Funds	TIF Funding	Federally backed resources (1)	CDFI / Mission Based Capital	Private Finance	Other Resources (2)
Predevelopment			B		B	B		B
Short-term acquisition/bridge			B	A		B	B	
Mid-term hold/operation (3)		B	B			B		
Permanent equity	B							
Permanent debt		B		A	B	B		
Permanent gap resources (4)		B	B	A	B			
Rehabilitation/recapitalization resources	B	B	B	A	B	B	B	B

A: Currently not utilized in Montgomery County

B: Used for preservation in Montgomery County

(1) These may include: HOME/CDBG funding, Rental Assistance Demonstration funds, National Housing Trust Funds, Choice Neighborhoods grants, FHA and GSE products, among others.
(2) These may include: smaller government programs, and developer self-financing, among others.
(3) For the purpose of this matrix, “mid-term” is defined as 3-10 years.
(4) These may include: soft seconds, mezzanine products, forgivable loans, equity equivalent capital, and grants for rent buy-downs, among others.

Description

The Housing Initiative Fund (HIF) is Montgomery County's local housing trust fund and the primary mechanism for providing affordable housing capital. Created in 1988, the HIF provides loans to nonprofit developers, rental property owners and for-profit developers for the construction and preservation of affordable and special needs rental housing. Other activities funded through the HIF include rental assistance, homeless funding, neighborhood development, and some homeownership activities (including down-payment assistance). HIF is funded through local revenue sources, primarily general revenues and proceeds from County taxable limited obligation bonds for affordable housing. Other sources include MPDU shared profits/alternative payments, condominium conversion taxes, a portion of proceeds from the sale of county land, and a portion of recordation taxes. The HIF was funded at $63.3 million in FY 2019, with $30.8 million dedicated to capital loan funds.

HIF loans are typically provided as "gap" resources, leveraging other sources of capital at ratio of $4.6 for every $1 over the last 10 years, according to DHCA. HIF borrowers generally are required to offer the County a right-of-first-refusal at point of property sale after the affordability term expires.

Over its entire history, no HIF loan has defaulted.

Assessment based on Best Practices

HIF resources are offered on a rolling basis, rather than offered at a specific point-in-time via a request for proposals/notice of funding availability process. This structure is consistent with national best practices, as it provides developers with access to capital at the point that its most needed in the development process and avoids unnecessary and costly delays in the project timeline.

For larger proposals, DHCA utilizes the state funding application. Given that many applicants are also applying for state resources, this reduces the burden of applying for multiple sources of financing. There is also a specialized, less-intensive application for smaller projects.

Practitioners interviewed consistently noted that the HIF is effectively and competently administered by knowledgeable County staff. Importantly, staff was committed to meeting various deadlines in the development process and able to adapt if circumstances shifted during the process.

Proposals are reviewed, underwritten and approved administratively. Oversight by elected official is provided at a "macro" level through the allocation of a total revenue amount at the beginning of the fiscal year and review of reporting on expenditures and outcomes. This is a "leading edge" best practice for local jurisdictions providing sizable capital investments in affordable housing, as it removes politicization from individual developments and focuses oversight on "big picture" goals and outcomes.

HIF is well coordinated with other elements of the County's "toolbox." There is a coordinated underwriting process for PILOTs and HIF loans, reducing the burden of seeking multiple funding sources. HIF funds are also often used to acquire properties/exercise ROFR. In addition, the county has offered HIF capital (in the form of subordinate/mezzanine debt) to incentivize for-profit and nonprofit developers to enter into rental agreements.

Practitioners did raise some concerns about transparency in the proposal review process, which can make it more difficult for developers to assess whether a proposal is adhering to County priorities and standards and potentially make it more difficult for newer (or smaller-scale) developers to compete for funding. For example, the most recent proposed update to HIF evaluation criteria contains fairly "high-level" standards/point allocations, without much granular detail of standards within a category (i.e., new construction or preservation).

Some practitioners expressed concerns that provisions requiring developers to provide a 10% equity contribution and defer a substantial portion of a developer fee may also put smaller developers at a disadvantage.

Moving forward, several elements of the proposed funding guidelines could make preservation somewhat less competitive compared to new construction. The proposed update to funding guidelines puts greater emphasis on new construction (up to 20 points) over preservation (15 points), other characteristics being equal. In addition, practitioners have raised concerns that state and local preferences for larger, family-sized units could make preservation less competitive.

Gaps between the cost of market rate capital and HIF resources is shrinking. Though the County provides flexibility in loan terms, interest rates are generally set at or around 3%. The lower spread between market and subsidized capital makes it more difficult for mission-driven developers to compete for properties against value-add investors.

Recommendations

- The County should maintain elements of HIF administration that are consistent with or set the standard for national best practices.
- The County should explore opportunities to expand HIF resources to better meet the needs of the preservation pipeline.
- The County can increase transparency by providing more detailed funding guidelines, as well as making public more historical information on the HIF portfolio, such as high-level information on past loan amounts, rates, and terms. This would allow developers to make informed judgments early in the process of what is feasible, while still maintaining flexibility for making context-specific underwriting decisions.
- The County should review allocation decisions moving forward to make sure that changes in HIF scoring criteria do not disadvantage preservation efforts.
- The County should consider providing additional points for preserving properties with future redevelopment potential (i.e., preserving affordability today, land banking for the future).
- The County should adjust income limit guidelines to allow for income averaging, consistent with updated regulations under the Low Income Housing Tax Credit.
- The County should consider whether lower interest rates are possible/warranted, given prevailing interest rates for market-rate capital.

Capital Financing | Multifamily Mortgage Financing Program

Description

In addition to its role as a public housing authority, the Montgomery County Housing Opportunities Commission (HOC) also serves as a housing finance agency. This enables it to provide low interest mortgage financing to private developers, both for-profit and non-profit, by issuing tax-exempt revenue bonds. A portion of units financed by HOC capital must be set aside for rent to low- and moderate-income households. HOC financing supports both rental and homeownership opportunities.

Over the past decade, HOC has focused its activities on recapitalizing and ensuring the long-term viability and quality of its public housing portfolio, in part through the HUD Rental Assistance Demonstration.

Assessment Based on Best Practices

The research team did not have access to sufficient data to conduct a detailed assessment of HOC's Multifamily Mortgage Financing activities.

At a high-level, there has been a nationwide deterioration of the public housing stock, in part due to inadequate federal funding. Public housing is critical to meeting the needs of some of the County's lowest-income and most vulnerable tenants. As such, recapitalizing public housing properties (whether under the Rental Assistance Demonstration or other sources) for long-term viability is critical to a comprehensive preservation effort.

Recommendations

Nationwide, several HFAs have used capital tools and/or the proceeds from lending activities to facilitate preservation. Examples include:

- Investments in targeted acquisition funds (Colorado Housing Finance Agency – Denver Regional TOD Fund)
- Low cost first mortgages for preservation (Minnesota Housing Finance Agency – Preservation Affordable Rental Investment Fund)
- Providing flexible capital/gap resources for high-priority projects (Virginia Housing Development Authority – REACH Virginia)

If there is additional capacity beyond public housing recapitalization and other existing priorities, HOC should explore whether these or similarly innovative HFA investment models are replicable in Montgomery County.

Benchmarking Resources:

- Enterprise Community Partners. "Denver Regional TOD Fund." https://www.enterprisecommunity.org/financing-and-development/community-loan-fund/denver-regional-tod-fund
- Minnesota Housing. "Preservation Affordable Rental Investment Fund Program Guide." http://www.mnhousing.gov/sites/Satellite?blobcol=urldata&blobheadername1=Content-Type&blobheadername2=Content-Disposition&blobheadername3=MDT-Type&blobheadervalue1=application%2Fpdf&blobheadervalue2=attachment%3B+filename%3DMHFA_006876.pdf&blobheadervalue3=abinary%3B+charset%3DUTF-8&blobkey=id&blobtable=MungoBlobs&blobwhere=1533150921680&ssbinary=true
- Virginia Housing Development Authority. "Community Outreach – REACH." https://www.vhda.com/BusinessPartners/GovandNon-Profits/CommunityOutreach/Pages/Community-Outreach.aspx

Capital Financing | Additional resources from third-party entities

Resource	Description	Local Applicability	Opportunities
Low-Income Housing Tax Credit **(LIHTC)** and **Maryland Department of Housing** and Community Development multifamily financing programs	LIHTC (equity) and DHCD capital (debt) are essential funding sources for affordable rental housing production Both 9% and 4% credits can be used for interventions to support preservation, with 4% credits (associated with a less generous subsidy) often used as part of recapitalization/rehabilitation efforts. As part of its allocation procedures, the state establishes preservation as one among several priorities.	LIHTC and DHCD capital are critical, with HIF funding often used to provide gap resources. There is a sense among practitioners that the state's priority for family-sized units puts preservation transactions at a disadvantage, given the number of older market-rate properties with higher proportions of one-bedroom apartments.	Though local funding is important, a lack of LIHTC equity is often the "binding constraint" that limits affordable rental production. Given the limited allocation of 9% LIHTC, the County could explore whether there are opportunities to increase local subsidies that would make more 4% LIHTC transactions feasible.
HUD Rental Assistance Demonstration	The Rental Assistance Demonstration provides resources, regulatory flexibility, and access to capital for the long-term redevelopment/recapitalization of federally assisted affordable rental properties. Though commonly associated with the recapitalization of public housing, certain other federally assisted properties are also eligible.	Montgomery County HOC is utilizing RAD to recapitalize its multifamily and clustered public housing sites. As of September 2019, it has invested $254 million in total development costs in its existing housing stock, preserving over 1000 units in 14 communities and increasing the number of affordable units by more than 400.	The County should advocate for the continuation and potential expansion of Rental Assistance Demonstration resources at the federal level.
Maryland DHCD National Capital Strategic Economic Development Fund (**NED**)	NED provides grant resources to support commercial and residential predevelopment activities in areas targeted for revitalization, focusing on parts of Prince Georges and Montgomery Counties inside the Capital Beltway. Funding can be used for site acquisition, land assembly, site development, and construction-level architectural and engineering design.	DHCD awarded $4 million in state fiscal year 2020. However, only one award fell withing the boundaries of Montgomery County ($100,000 for the New Hampshire Avenue Façade Program within the City of Takoma Park).	County practitioners (government and private) should explore whether these resources can be better utilized in Montgomery County. The County can play a convening role. If these resources are less effective for "standard" preservation efforts than more typical tools, the County can explore whether these funds can play a role in meeting more targeted preservation needs, such as preserving smaller properties that are inefficient to finance through LIHTC.

Capital Financing | Additional resources from third-party entities

Resource	Description	Local Applicability	Opportunities
Mission-driven capital/acquisition funds	Non-governmental entities (such as Community Development Financial Institutions and other mission-driven entities) may invest resources to acquire existing units and add/extend affordability restrictions. These funding sources may have shorter terms and/or return expectations than traditional subsidized capital and require additional intervention (redevelopment incentives, additional recapitalization funding) to preserve longer-term (or deeper) affordability.	There are several CDFIs active in the DC metropolitan region (including but not limited to Enterprise Community Partners and LISC) that offer financing resources of varying types. In addition, in the last decade equity funds (such as the Washington Housing Initiative and Housing Partnership Equity Trust) have been established that focus on the acquisition and continued affordability of naturally-occurring affordable housing.	Some mission-driven resources are intended to contribute as part of a typical LIHTC funding package. Developers tend to be well-aware of these resources. The specific time horizons (generally 10 years or less), terms, and return expectations of some acquisition capital may make longer-term preservation difficult. These products do provide short-term affordability and are effective at extending the window of opportunity for the County to assemble additional resources and/or adopt appropriate land use incentives for redevelopment that would constitute a more durable intervention.
Minor rehabilitation capital	Low-cost resources for minor rehabilitation or property improvement (including increased energy efficiency) can improve housing quality and potentially be used to incentivize property owners to maintain affordability. Examples that could serve this role locally if adapted include: The Weatherization Assistance Program provides no-cost assistance for energy efficiency improvements in both single-family and multifamily settings. The County also offers a Property Tax Credit for Energy and Environmental Design to offset property tax obligations if a building meets specific standards.	The County's Weatherization Assistance Program has not been fully operational in recent years. This primary source of funding for this program is "pass through" funds from federal/state sources., and funding amounts are relatively small. The research team was unable to obtain data on utilization of the Property Tax Credit for Energy and Environmental Design in multifamily and/or affordable properties.	Based on a review of available information, neither resource has been proactively put forward as a tool for preservation. Though the funding amounts are relatively small, the County could explore whether the programs can be more effectively marketed or amended to better meet affordable housing needs. These could be additional sources of capital for properties that are inefficient to finance through LIHTC.

Policy Gap: There are insufficient resources for capital intensive acquisition efforts.

Potential Intervention	Description	Examples and Precedents
Capital for light-to-moderate rehabilitation	Medium-to-long term capital can be used to recapitalize existing affordable properties currently under mission-driven control outside of the LIHTC pipeline, with the purpose of focusing deeper subsidies on properties with more significant capital needs and/or higher acquisition costs. Properties would need to be in relatively decent condition, and certain requirements that are triggered by state/local funding (such as more ambitious environmental requirements that do not generate utility savings) may need to be deferred.	The Massachusetts Housing Partnership offers an FHA Risk Share product that offers a low-interest 40-year amortizing loan with capitalized reserves at an amount sufficient to ensure the long-term physical and financial viability of the property.
Targeted acquisition funding	Purpose-specific acquisition funds can provide capital to mission-driven entities to acquire and preserve affordability of at-risk properties. These funds often include a streamlined underwriting process to allow for rapid response when opportunities arise, though the County ROFR obviates some of that need. Acquisition funds often use a relatively small amount of public resources as "top-loss" funds to leverage larger amounts of public (including housing finance agency), philanthropic and private capital. The most recent County budget included a request to establish the Affordable Housing Opportunity Fund which would fulfill this purpose. The program has yet to be funded.	Targeted acquisition funds have been adopted in a wide range of cities and regions. Locally the District of Columbia's established a Housing Preservation Fund. Other notable example have been established in Denver, the San Francisco Bay Area, the Twin Cities, and Boston, among several others. These efforts are often in response to and/or coordinated with catalytic investments (such as new transit lines) that are anticipated to contribute to property value appreciation and potential displacement of lower-income residents.
Value Capture Methods, including Tax Increment Financing (TIF)/Special Assessment Districts (SA Districts)	Value capture methods are generally utilized to "recapture" some of the private value created from catalytic public investment (or other market contexts where property values are rapidly appreciating). With TIF, a portion of rising property tax revenues can be used to provide funding for a public purpose such as affordable housing development/preservation through a TIF arrangement. Similarly, SA Districts capture value by levying an additional tax on top of the baseline rate within a given geographic boundary. These increment revenues can either be used to seed a specific housing budget item (such as a trust fund) in a "pay-as-you-go" manner or be bonded against to provide upfront revenue.	Value capture can be a powerful tool when utilized effectively, though there can be risks to jurisdictional financial sustainability if the policy is poorly designed or if the tool is utilized too broadly. Examples of the use of value capture for the purpose of preservation and/or creation of affordable housing can be found in the cities of Chicago and Portland, and statewide authorization language has been developed in states as politically diverse as Utah, Texas, Minnesota, and Maine.

Policy Gap: Addressing challenges posed by small properties

Potential Intervention	Description	Examples and Precedents
Dedicated capital for small scale acquisition	Small scale properties are often more difficult to preserve and manage, given the lack of economies of scale and (in some cases) significant amounts of deferred maintenance. However, small scale properties often add unique value, particularly a source of economic integration in lower-density neighborhoods. Some local practitioners interviewed as part of this research expressed concern that proposed changes to HIF guidelines may make smaller properties more difficult to finance moving forward. If the County determines that preserving smaller scale properties is a high-priority, one approach is to create or enhance dedicated resources (or set asides) for that purpose.	The City of San Francisco's Small Sites Program provides soft debt for 5-25 unit properties in which two-thirds of existing tenants have incomes at or below 80% AMI. The program also provides capacity grants to community sponsors, who take ownership of the properties and maintain them as permanently affordable housing.

Jurisdictions can offer incentives and resources that make it financially feasible for landlords/owners to offer reduced rents to lower-income tenants.

Property owners, whether market-rate or mission-driven, may be better able to offer affordable rents (or deeper targeting) if they are able to reduce operating costs and maintain net operating income.

A successful strategy:

- Provides an opportunity to preserve affordability in properties that cannot be brought under mission-driven ownership or long-term affordability restrictions.
- Includes multiple types of support to reflect the varying interests of property owners and needs of different property types.

Montgomery County provides multiple tools that facilitate lower rents in both deed-restricted and market rate properties. These tools have significantly contributed to preservation, from larger-scale, permanent extensions of affordability to shorter-term extensions for a portion of units within a transitioning property. **There could be opportunities to expand these tools to provide an operating subsidy in exchange for extending lower rents.**

Description

Rental Agreements are voluntary agreement between the property owner or purchaser and DHCA that provide for the retention of affordable units with specific terms and conditions. A critical component of some Rental Agreements is a Rental Assistance Payment, a direct allocation of DHCA resources that bridges the gap between the agreed-upon affordable rents and what the market could otherwise command.

Other associated incentives included as part of the Rental Agreement can include Payments-in-Lieu-of-Taxes, and technical/staff support in extending HUD contracts.

Assessment Based on Best Practices

Rental Agreements and Rental Assistance Payments are effective tools for preserving affordability in a variety of contexts. Whereas in other jurisdictions preservation is often binary proposition, based on the ability to bring a property under mission-driven ownership, these agreements provide another path to maintaining affordability. Though the extended affordability period may be shorter in some cases, the overall costs is also generally lower.

While Rental Assistance Payments may be lower-cost, they do not "revolve" back into the HIF via loan repayments, unlike other forms of County assistance.

Recommendations

The County should continue to use Rental Agreements and Rental Assistance Payments to preserve and expand affordability in private- and nonprofit-owned properties.

As previously recommended, the County should continue to track and evaluate expenditures and outcomes by preservation approach to determine the appropriate balance for resource allocation.

Operating Subsidy | Payments-in-lieu-of taxes (PILOTs)

Description

Payments-in-Lieu-of-Taxes (PILOTs) provide for a negotiated payment that lowers the cost of real property and special area taxes in return for a property owners' commitment to provide affordable housing. Specific exemptions are negotiated by the DHCA and approved by the Department of Finance, subject to legal, budgetary and procedural restrictions. To be eligible, the property must receive other federal, state, or local financing.

The total amount of tax revenue foregone through pilots is capped ($18M in FY 2020). HOC properties qualify for a 100% abatement but do not count against this cap. Based on recent data, the County has opportunities to increase utilization without reaching this cap. According to Tax Expenditure Report released in October 2019; there were 3,205 tax accounts (associated with parcels, not properties or units) receiving $19M in exemptions. The HOC exemption constituted approximately $9.6 million of this total.

There have been recent changes to the allocation of PILOTs. The amount abated in prior iterations of the program varied by property type and the amount of rent foregone, or the amount that was necessary to acquire a property. The most recent proposal establishes abatements for properties with Rental Agreements at the amount of loss due to keeping rents low. For all other non-HOC properties, taxes will be reduced by an amount equal to the percentage of income-restricted units (i.e., a property with 20% affordability receives a 20% abatement). HOC will continue to receive a 100% abatement.

Assessment based on Best Practices

The County's provision of PILOTs is consistent with national best practices, is regarded by practitioners as an important component of the local affordable housing financing stack, and along with HIF constitutes an important complementary tool for Right-of-First-Refusal acquisitions and/or Rental Agreements.

Recommendations

Given the County is not at the PILOT cap, the County could consider opportunities to expand utilization of Rental Agreements, if such expansion could be accomplished without overly restricting availability for high-priority acquisitions/Rental Agreements in future years.

Operating Subsidy | Additional resources from third-party entities

Resource	Description	Local Applicability	Opportunities
Project-Based Rental Assistance	Applying project-based rental assistance to redeveloped or rehabilitated units can achieve the same goal of maintaining net operating income for the property owner.	The Montgomery County HOC manages the HUD Section 8 Project-Based Rental Contract program. These contracts provide assistance directly to private- or nonprofit property owners to rent at reduced rates to income-eligible households, which pay 30 percent of their income on rent.	The availability and utilization of HUD Project-Based Rental contracts is limited by federal regulations appropriations; as such opportunities to expand or enhance this program are minimal at this juncture.

Operating Subsidy | Potential New Interventions

Policy Gap: Express-purpose preservation plans

Potential Intervention	Description	Examples and Precedents
Property tax credits	The County could offer a property tax credit to owners or managers that voluntarily offer reduced rents to income-qualified tenants. Program specifics could vary, but potential structures could include: • Offering a fixed amount to owners of naturally-occurring affordable rental units that demonstrate adherence to voluntary rent guidelines and lease to income-qualified tenants. • Providing a tax credit equal to the amount rent is reduced (or a fraction thereof) compared to a market-based standard.	Previously, Montgomery County offered a Property Tax Credit for Reduced Rent for Elderly or Disabled Tenants. The County created a tax incentive for landlords to discount rent for elderly (defined as 65 and older) and disabled tenants that meet income and asset eligibility criteria. Landlords who leased to tenants that met eligibility restrictions and reduced rents by at least 15 percent below the market rate are eligible to apply for a tax credit equal to 50 percent of the rent reduction. The program was set to sunset and lapsed on June 30, 2018, **without any utilization.**

Operating Subsidy | Potential New Interventions

Policy Gap: Limited federal resources for Project Based Rental Contracts

Potential Intervention	Description	Examples and Precedents
Locally-funded master leasing	Mission-driven and/or public entities can lease a specified number of units in private, market-rate properties to preserve affordability while still providing the owner with a market-rate return. Such policies can be targeted toward gentrifying neighborhoods and/or larger-scale properties.	Master leasing is commonly found in the social services context, in which local jurisdictions and/or nonprofits provide resources to lease a portion of units in larger rental properties for use by vulnerable households. While master leasing may be optimal in certain contexts (service-enriched housing opportunities, the leasing of full properties, etc.). The County's current approach to Rental Assistance Payments has a similar impact at lower risk to the County.

Many jurisdictions manage resources, policies, and tools that can be used to preserve affordable housing. The likelihood of success in stemming the loss of affordable units is contingent on a consolidated strategy that combines all these interventions.

A successful strategy:

1. Comprehensively analyzes preservation needs, risks, and opportunities, in the context of other housing priorities;
2. Intentionally develops, coordinates (often across agencies and sectors) and administers interventions to meet the specific needs and goals of the jurisdiction; and
3. Communicates and proactively engages with private and nonprofit sector stakeholders to implement and promote utilization of available tools and resources.

Montgomery County is actively involved in advancing each of these three steps. In particular, practitioners interviewed as part of this evaluation spoke positively of the availability, compatibility, and coordination of the various tools/resources directly administered by the county. There could be opportunities to enhance the County's overall strategy through a more intentional focus on preservation pipeline "triage" and better linking private owners to County tools.

Description

Research assessment and strategy development is a broad category that captures a jurisdiction's efforts to analyze preservation needs and opportunities and develop an overall strategy and suite of interventions tailored to the local context. Though each specific intervention will be assessed individually, it is also important to examine the effectiveness and complementarity of the overall "toolbox."

Montgomery County has undertaken several preservation-related analyses over the last twenty years, beginning with a 2001 Preservation Strategy report commissioned by DHCA that focused on federally subsidized properties at high risk of loss. More recently, in 2017 the Planning Department commissioned a broader rental housing study, which also addressed preservation needs and tools. This study builds on these and other research and analysis efforts, both internal and public-facing.

Though the County has not published an up-to-date, formal "preservation strategy," DHCA has been intentional in developing and deploying several "sets" of complementary tools that support different preservation approaches. County budget and appropriations documents establish Multifamily Program Performance Measures (see next slide) which disaggregate production figures by preservation and new construction.

Assessment based on Best Practices

- The County has strong overall pipeline monitoring/management practices, which is critical for prioritizing resources as preservation opportunities emerge.
- The County provides a substantial amount of resources to preservation, both in terms of capital financing and overall multifamily efforts (see following slides).
- The County has demonstrated success in coordinating various tools for different preservation approaches and deploying these tools in a systematic manner. Rental Agreements (slide TBD) are a notable example, as is the coordination of Payments-in-Lieu-of-Taxes (slide TBD) with Housing Initiative Fund capital (slide TBD).

Recommendations

- The County should maintain, update, and analyze a comprehensive inventory of at-risk properties by type, location, and risk profile.
- County investment information should be contextualized with the number of years the affordability period is extended to weigh the cost-effectiveness of intensive vs. light-touch approaches.
- The County should improve coordination between the suite of tools offered by DHCA and the various land use and planning tools to better facilitate preservation through redevelopment. This could enhance "triage" opportunities by allowing near-term, less costly approaches to serve as a bridge to later, more comprehensive preservation efforts.

Benchmarking Resources:

Inventories, analysis, and dashboards:

- Fairfax County Redevelopment and Housing Authority. "Fairfax County Affordable Housing Dashboard." https://www.e-ffordable.org/affordable-housing-dashboard.
- Arlington County Department of Housing and Community Development. "Annual Reports." https://housing.arlingtonva.us/plans-reports/annual-reports/

Rehabilitation takes up nearly half of all capital expenditures and more than half of all production over the last twelve fiscal years.

	Total Units	Affordable Units	% Affordable	% of Total	% of Affordable Units	County Funding	% of Total
Foreclosure Homeownership Assistance	33	33	100%	< 1%	0.45%	$5,900,000	2%
Special Needs	515	486	94%	4%	6.55%	$46,020,040	12%
Homeownership	110	103	94%	1%	1.39%	$7,743,000	2%
New Construction	2,005	629	31%	17%	8.48%	$46,648,597	13%
MPDUs Purchased by Non-Profits	56	53	95%	<1%	0.71%	$3,186,590	1%
Senior Housing	2,273	1,863	82%	20%	25.12%	$93,139,457	25%
Multifamily Acquisition and/or Rehab (nonprofit)	4,672	3,290	70%	40%	44.37%	$127,798,548	35%
Multifamily Acquisition and/or Rehab (for-profit)	1,982	955	48%	17%	12.88%	$39,748,274	11%
Single Family Rehab	3	3	100%	< 1%	0.04%	$11,975	<1%
Total	**11,649**	**7,415**	**64%**	**100%**	**100.00%**	**$370,196,481**	**100%**
Total Rehabilitation Efforts	*6,654*	*4,245*				*$167,546,822*	

Source: DHCA data on Affordable Housing Loans provided through the HIF or Housing Capital Investment Plan for Fiscal Years 2008-2019. This data does not include resources utilized for rental assistance.

According to County performance data, the County consistently preserves substantially more rental housing than it produces, at a much lower cost-per-unit.

Category	Actual FY 2017	Actual FY 2018	Estimated FY 2019	Target FY 2020	Target FY 2021
Total affordable housing units preserved (includes rental assistance)	2,951	4,390	4,900	4,750	4,950
Total affordable housing units produced	1,724	1,525	1,616	1,538	1,277
Cost per unit of affordable housing produced	$24K	$34K	$34K	$28K	$25K
Cost per unit of affordable housing preserved	$4.2K	$5K	$14K	$7K	$7K

The relative cost-effectiveness of preservation is well-established in affordable housing cost study literature. In the Montgomery County context, the magnitude of this difference as illustrated in this table may be overstated, given the inclusion of rental assistance in the preservation metric. While rental assistance is a critical part of the preservation toolbox, the number of years of affordability that such assistance provides may be substantially shorter than an upfront capital investment in preservation (via acquisition by mission-driven ownership) or new construction of affordable units. Disaggregating data by intervention type and number of years affordability is extended could allow for more thorough analyses of cost-effectiveness.

Source: Montgomery County Department of Housing and Community Affairs, FY 2020 Appropriations Report

Description

Proactive outreach and assistance to landlords can inform them of resources that are available for improving properties (such as rehab loans) and/or reducing rents (rental assistance or property tax incentives). These outreach efforts can address the capacity gaps of smaller-scale private landlords that are interested in continuing to serve their existing tenant base or willing to sell to a mission-driven entity.

Montgomery County provides resources to the Montgomery Housing Partnership to administer the Apartment Assistance Program as part of its *Neighborhoods to Call Home* initiative. The program was originally established to support lower-capacity owners/landlords in conjunction with an increasing County focus on housing quality and code enforcement. Today, issues covered by program activities include code compliance, fire and life safety, rodent and trash issues, leasing legal requirements (including fair housing compliance), and reasonable accommodations/modifications for persons with disabilities. Forums for engagement include workshops, one-on-one assistance, and a building trade expo. Through these engagements, owners/landlords are also provided with information on county resources to improve/rehabilitate housing (including a small set-aside in the HIF for smaller apartments).

Outside of this program, the County has also worked with private owners to retain affordability. For example, the County has committed to providing technical assistance to owners engaging with HUD in the sometimes-complicated process of extending Housing Assistance Payment (HAP) contracts.

Assessment Based on Best Practices

In funding the Apartment Assistance Program, Montgomery County provides a proactive service to small owners/landlords that is sometimes absent in other comparable jurisdictions, at a relatively low cost.

The County's core focus is on housing quality and stewardship, as compared to similar programs in other jurisdictions (such as the New York City Landlord Ambassador Pilot) that prioritize linking owners with resources and building a preservation pipeline.

The County is aware of – and proactively guards against – the use of the capital promoted by the Apartment Assistance Program to drive up rents or "gentrify" a property.

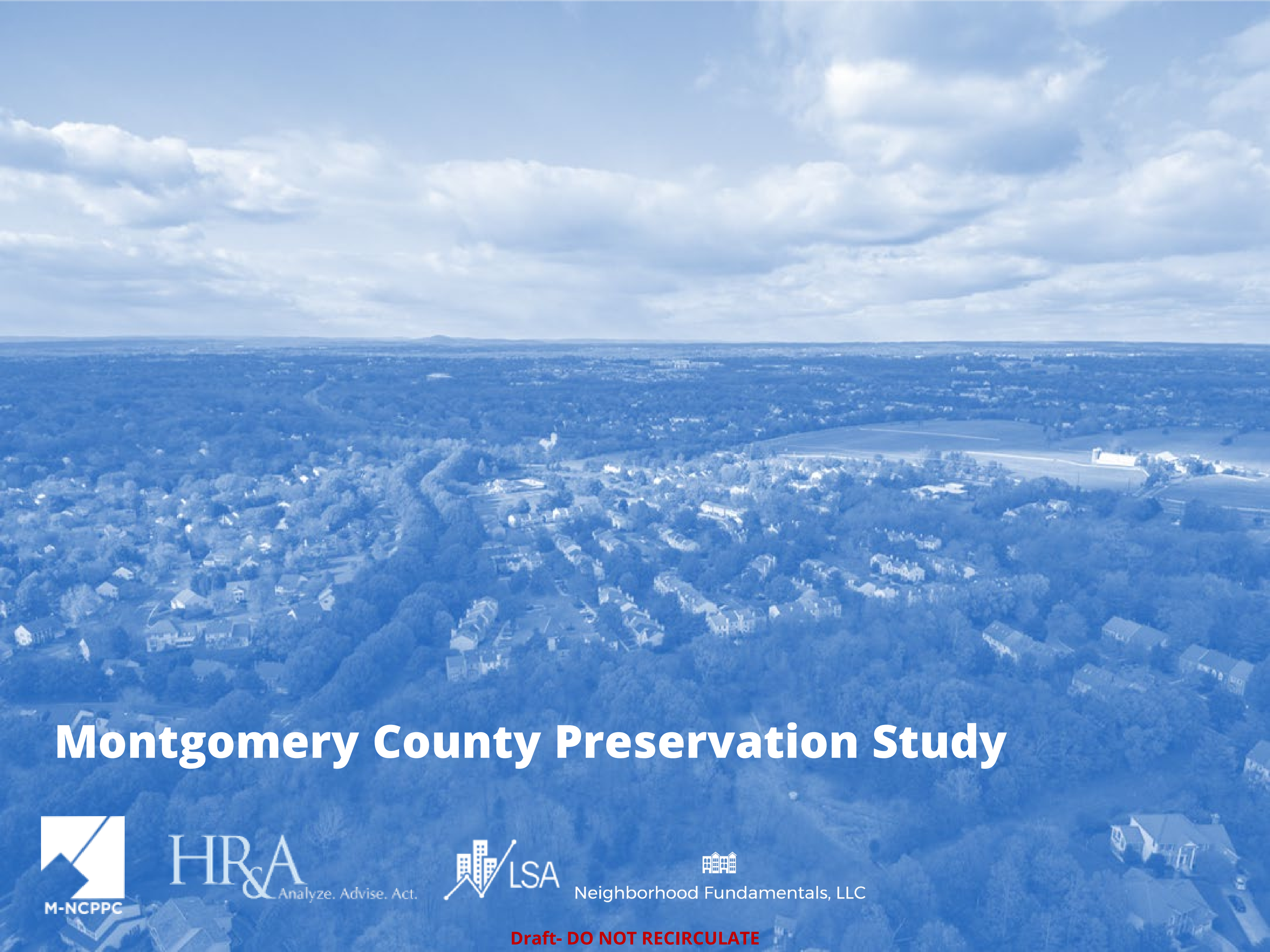
Exogenous factors, especially the low interest rate environment for market-rate rehabilitation capital limits, limit the attractiveness of County resources to profit-driven small owners/landlords.

Recommendations

If the County decides that preservation of the smaller multifamily stock is a critical priority, the Apartment Assistance Program could be refocused (or a complementary program developed) with pipeline development as a core focus.

Coordination between the Apartment Assistance Program, code enforcement, and Landlord-Tenant Mediation could be enhanced to identify the most challenging properties for more intensive focus (and potential prioritization if the property is marketed for sale).

Providing additional services, such as centralized income certification and waitlist management, could decrease the bureaucratic burden and increase the attractiveness of County resources that carry income restrictions.



Montgomery County Preservation Study

M-NCPPC

HR&A Analyze. Advise. Act.

LSA

Neighborhood Fundamentals, LLC

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