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Low-Income Housing Tax Credit (LIHTC) at Risk

Duty to Serve | July 2022

Risk and Impact of LIHTC Properties Exiting the Program: Examining the Risks of Expiring LIHTC Restrictions and the Outcomes of Properties that Exit

As market rents rise rapidly across the country, rental affordability has become particularly important especially in preserving affordable housing already in place. More affordable units are needed in the market, so any loss of existing units is problematic. Some market participants[1] are concerned that units supported by Low-Income Housing Tax Credits (LIHTC) may transition from having restricted, affordable rents to levels that are too expensive for low- and even moderate-income households to afford.

In this paper, we examine the LIHTC program, which has been the federal government's primary vehicle for incentivizing affordable housing development since the program's inception in 1986. We examine the factors that are correlated with properties leaving the program and examine what happens to units once they are no longer subject to LIHTC affordability restrictions. Understanding these risks can help states consider how to best use their limited LIHTC and private activity bond allocations to help preserve affordable housing. Given the intricacies of the program, disparate and incomplete data, and the inherent unpredictability of future housing market conditions, evaluating the level of risk is an inexact science. However, our goal is not to estimate the number of exiting properties but to instead paint a picture of the general risk that currently exists in the market and the potential severity of affordability loss.

A key finding from our research is that LIHTC properties that exit the program often remain more affordable than conventional market rate properties that were never subsidized, even if they are not resyndicated. Our research finds that while most properties that exited the LIHTC program have increased rents above the maximum level of allowed rent in the program, the increases are generally modest. In this way, formerly LIHTC properties commonly transition to workforce housing, remaining affordable to tenants that earn below the area median income (AMI).

Below are some of the key findings of our research:

- In our analysis, 86.8% of LIHTC properties are programmatic, meaning that they are still in the program and are still subject to rent restrictions. Given the history of the program, a growing number of properties will be able to potentially exit in the coming years.
- High opportunity areas have a relatively high share of programmatic LIHTC properties, which, given the elevated rental costs, can be particularly beneficial for these areas.
- LIHTC properties that have left the program (referred to as non-programmatic) generally have higher rents compared with LIHTC-restricted units, but lower rents compared with conventional market rate units.
- Various factors influence the propensity to leave the LIHTC program, including ownership type, resyndication history, property size, the state in which the property is located and local housing market conditions. However, the degree and direction of influence is not always clear.

[1] What Can Be Done When LIHTC Affordability Restrictions Expire? — Shelterforce and Picture of Preservation 2021 (preservationdatabase.org)

- Some non-programmatic LIHTC properties increase rents substantially above 60% area median income (AMI) affordable rents, but the majority are still affordable at this level. The most common path for a non-programmatic LIHTC unit is to remain affordable at 60% AMI, which happens roughly 61% of the time.
- For LIHTC units priced well below the 60% AMI maximum, conversion to market rate can cause a dramatic increase in rents. The conventional market is generally unable to support deeply affordable units, which is why programs like LIHTC are critical.

Explanation of Risk

Overview

Housing researchers generally agree that the U.S. suffers from a lack of affordable rental housing. The National Low Income Housing Coalition (NLIHC) estimates that for every 100 renters earning 30% of AMI there are only 36 units available.[2] Harvard's Joint Center for Housing Studies reports that the number of units renting for under $600/month declined by 3.9 million from 2011 to 2019 (inflation adjusted), decreasing that category's share of the overall rental market from 32% to 22% over this period.[3]

The LIHTC program is the federal government's primary vehicle for providing affordable housing nationwide. LIHTC units are income restricted and rent restricted based on local income levels, and generally must remain affordable for 30 years.[4] After this period, property owners are no longer required to charge rents affordable to low-income tenants, although the stipulations of the programs and the actions taken by property owners are not universal. Some units are operated at affordable levels for longer than stipulated, while some units leave the program earlier than expected. For those units that are no longer subject to rent restrictions, there is risk that the property owners may increase rents significantly and thus no longer serve the segment of the rental market in need of affordable units.

Properties financed using tax credits must remain affordable at specific income levels, generally 60% of the AMI, but can also provide affordable housing down to 30% of AMI.[5] We found, based on our LIHTC equity financing done in 2021,[6] that most units (84.5%) price units at 60% AMI, with the remaining units targeting either 30%, 40% or 50% AMI.

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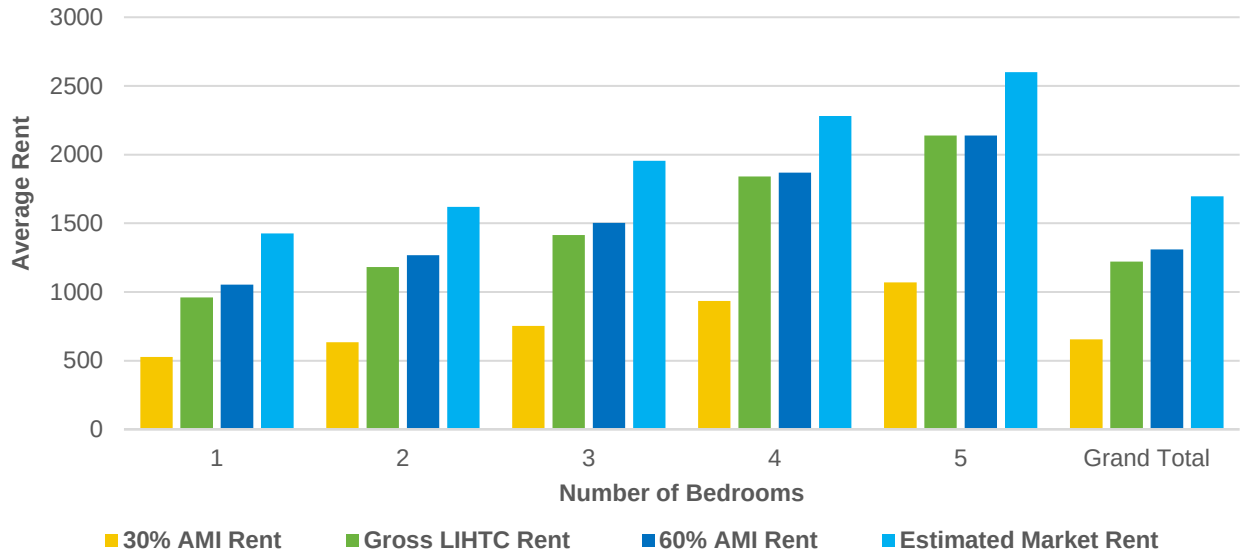
[2] https://nlihc.org/sites/default/files/gap/Gap-Report_2022.pdf
[3] https://www.jchs.harvard.edu/sites/default/files/reports/files/Harvard_JCHS_Americas_Rental_Housing_2022.pdf
[4] This time differs by state, but the restricted term is most frequently 30 years.
[5] Properties are subjected to maximum LIHTC rents at certain AMI limits (60%, 50%, 40%, 30%), however, they may not be able to charge maximum LIHTC rents given local market conditions. Units targeting lower affordability levels are more likely to obtain the maximum rent level given the low supply of deeply affordable units.
[6] Freddie Mac re-entered the LIHTC equity market in 2018 in conjunction with the start of the Duty to Serve initiative. In 2021, we provided equity financing for 37 properties, 22 of which did not have existing subsidies in place. These 22 properties comprise 3,154 rent-restricted units across 12 states and 18 MSAs, with eight properties being in rural areas.

As evidenced by Exhibit 1, LIHTC maximum rent of 60% AMI is typically well below the comparable market rate rent. Rents capped at 30% AMI are even lower than what could be found outside of LIHTC properties. As properties leave the LIHTC program, there is risk that rents will increase to market rate and become unaffordable to tenants making well below the AMI.

Exhibit 1: Average Rent by Unit Type and Number of Bedrooms



Source: Freddie Mac tabulations of our 2021 LIHTC equity investment data

LIHTC properties are subject to a compliance period for how long rents need to be restricted. For LIHTC properties placed in service before 1990, this period is 15 years, whereas properties placed in service in 1990 or later have an affordability period of 30 years. The first 15 years is the compliance period, where tax credits are subject to forfeiture if affordability requirements are broken, while the second 15 years is the extended use period, where credit forfeiture is no longer possible. The 30-year period is federally imposed, and some states impose longer restriction periods. For example, California has an extended use period of 55 years.[7]

Developers also can commit to more than is required by state and federal law in order to be more competitive in the credit allocation process, which is especially common for 9% tax credits since developers acquire 9% tax credits through a competitive process. Commitments can include agreeing to a longer extended use period, offering lower rents or waiving the right to a qualified contract.

Regardless of whether some property operators commit to more affordability, the fact remains that there is potentially systemic risk of LIHTC unit loss as more properties approach the 30-year mark (the end of the minimum extended use period) or even the 15-year mark.

[7] https://www.treasurer.ca.gov/ctcac/program.pdf – The 55-year extended use period is mandatory for 9% tax credit properties and highly incentivized for 4% tax credit properties.

The topic of LIHTC affordability loss has been studied before by other organizations. Prominent examples include a 2012 Department of Housing and Urban Development study of what happens to LIHTC properties at year 15, and a 2021 joint study by the NLIHC and Public and Affordable Housing Research Corporation (PAHRC) that quantifies the number of LIHTC units reaching year 30 in the near future. Our analysis complements this research and helps the industry to further understand the risks and consequences associated with LIHTC affordability loss during the existing affordability crisis across the country.

Identifying Types of Risk of Properties Exiting the LIHTC Program

Between years 1-15 of the initial compliance period for LIHTC, the risk of affordability loss is low since there is typically not a legal way to raise rents above what is stipulated at the time of credit allocation. However, at year 15 and beyond, several risks emerge that could lead to LIHTC properties leaving the program.

Through a Qualified Contract (QC)

- Beginning as early as year 14, LIHTC property owners typically may inform the applicable state Housing Finance Agency (HFA) of their intent to sell the property pursuant to the QC process.[8]
- If a buyer is not found by the HFA within one year, the owner can convert the property to market rate rents after a three-year "decontrol" period.

Expiration of Affordability Restrictions

- Depending on the year a property is placed in service, affordability restrictions will generally lapse after either 15 or 30 years. After this period, property owners can raise rents without the risk of credit recapture by the IRS or, in some cases, legal action by the HFA.
- Some states require a longer extended use period, and some property owners agree to more stringent restrictions in order to be more competitive in the allocation process. In this way, the 15- or 30-year rule is not universal.

Foreclosure

- Historically, LIHTC properties have very low delinquency and default rates. However, a LIHTC property could still suffer from financial and operational problems that give a lender the right to foreclose.
- Upon foreclosure and transfer of ownership, the Land Use Restriction Agreement that includes rent restrictions typically will terminate, permitting the new owner to convert the property to market rent after a three-year decontrol period. This can happen even before year 15.
- Some industry stakeholders have raised concerns about "planned foreclosures" where a property owner deliberately triggers a foreclosure to exit the LIHTC program.[9,10] However, the Internal Revenue Code does not allow owners to avoid enforcement of rent restrictions in these

[8] Background-on-Qualified-Contracts-under-Section-42-and-Misconceptions-Documents-April-2018.pdf (ncsha.org)
[9] Microsoft Word - IRS Comments Notice 2018 43.docx (nhlp.org)
[10] 5-05_Low-Income-Housing-Tax-Credits.pdf (nlihc.org)

circumstances, and in any event, a property leaving the LIHTC program via a foreclosure of any kind is rare.

Other Methods

- There can be other, less common ways in which LIHTC properties could exit the program, or rents could be increased subject to LIHTC restrictions. For example, some companies, known as aggregators, obtain limited partner interests in LIHTC properties with the apparent primary goal of increasing profitability (by increasing rents) rather than preserving affordability. For more information, please see the Appendix.

If LIHTC properties leave the program, the degree of affordability loss can only truly be measured on a case-by-case basis since property owners will not necessarily raise rents, especially if property or local market conditions can't support the increase. For example, two properties that exited the LIHTC program in the same metro area saw different outcomes post-LIHTC compliance. One property's rents increased to 83% of AMI, while the other property's rents remained affordable at 55% of AMI. The first property had more pricing power since the property was in very good physical condition and included amenities such as a swimming pool and fitness center. The lower priced property was much older and was of comparatively lower physical quality.

Given the complexity of the program and the diverse circumstances of property owners and local market conditions, evaluating property-level risk on a large scale does not tell the whole story. Here we examine the LIHTC market to determine potential risk factors for properties that would exit the program. In addition, we drill down to seven metro areas to match non-programmatic LIHTC properties to third-party data in order to analyze the affordability of properties after their exit.

Snapshot of Current Non-Programmatic LIHTC Properties

Overview

Our analysis primarily relies on two databases: the LIHTC property-level database compiled by HUD and LIHTC data compiled by the National Housing Preservation Database (NHPD). HUD is responsible for the data collection while NHPD consolidates HUD's data and adds some additional subsidy and property data from other sources.

We identified 40,296 multifamily properties in the entire history of the LIHTC program.[11] Of these, 34,975 properties are identified as programmatic as of the study date, which means that they currently restrict rents based on local income in accordance with LIHTC requirements. The remaining 5,321 properties are identified as non-programmatic, or properties that have exited the LIHTC program and are no longer monitored for compliance and are therefore no longer believed to have LIHTC restricted rents.

For most properties that exited the program, data that could provide a reason for why they left the program is unavailable. Most often they are simply listed as being non-programmatic without giving a reason. In a minority of cases, we can identify that they aged out of the program, and this happens most often for properties placed in service on or before 1992.

[11] Calculated using data as of April 2021

What Factors Increase or Decrease the Propensity of a Property Exiting the LIHTC Program?

While the fate of each LIHTC property depends on many factors, some of which are not available in publicly consumable data, we have identified a few broad factors and trends that are correlated with whether properties stay or leave the LIHTC program.

Ownership Type

LIHTC properties with nonprofit owners are less likely to leave the program. Just over a quarter (28.5%) of all multifamily LIHTC properties (programmatic and non-programmatic) are owned by a nonprofit entity. However, the rate of non-programmatic properties to all LIHTC properties is just 21.2%, indicating that nonprofits have a lower propensity to end LIHTC restrictions.

The effect of ownership type varies across geography, but the general trend of high programmatic rates among nonprofits is consistent. In rural and high opportunity areas[12], for example, LIHTC properties are more likely to be owned by nonprofits, but the relative disparity between programmatic and non-programmatic among nonprofits remains roughly the same in these areas.

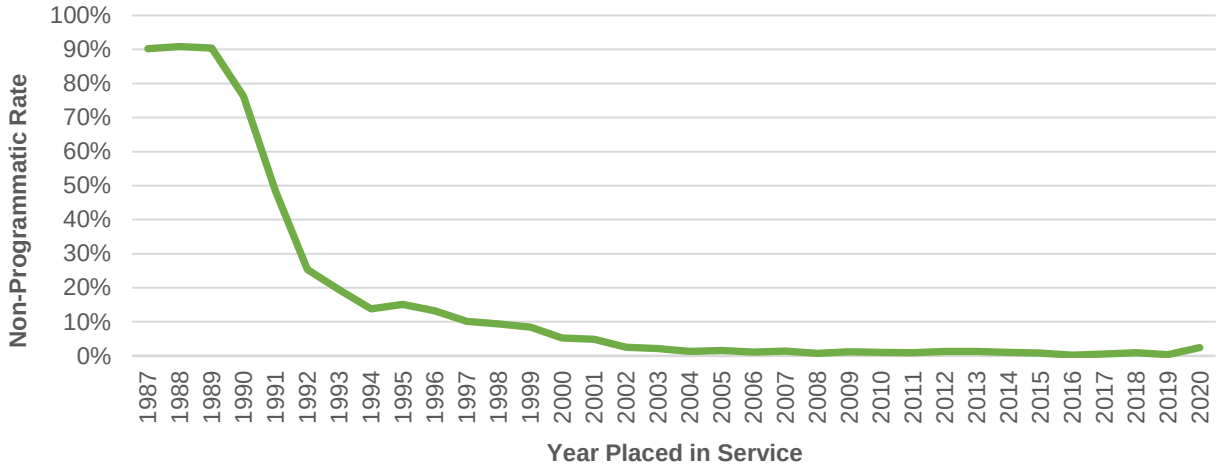
Year Placed in Service

Older LIHTC properties are substantially more likely to exit the program. Over 90% of properties placed in service prior to 1990 are believed to be non-programmatic. In 1990, the program length switched from 15 years to 30 years, at which point we see the rate of non-programmatic properties begin to steeply drop until leveling out at around 1% starting in the early 2000s. Even though very few properties have hit the end of their 30 years of rent restrictions, some have exited through other methods, such as through a QC or a foreclosure. This explains why there are still cases of properties exiting in the past several years.

Properties placed in service in the early 1990s are reaching year 30 now unless they are subject to lengthened affordability restrictions. We have very limited data on this population of properties coming to the 30-year expiration. We learned from discussions with state HFAs that some properties are starting to roll out of the program given the end of the 30-year period and this is a concern for the market as more properties hit this milestone. As properties from the early 1990s reach 30 years, the industry will start to learn more about what happens to properties reaching the end of their extended use period.

[12] Per Duty to Serve, a high opportunity area can be designated in two ways: by a state's Qualified Allocation Plan (QAP) or by HUD's Difficult Development Area (DDA) designation. In general, high opportunity areas have high income and low poverty, and typically have good access to transportation, health care and education.

Exhibit 2: Non-Programmatic Rate vs. Year Placed in Service



Source: Freddie Mac tabulations of HUD and NHPD data

Exhibit 2 captures a steep decline in the rate of non-programmatic properties after the earliest years of the program. As properties reach the 30-year mark, the high non-programmatic rate observed in properties from the late 1980s could extend to properties placed in service in the early 1990s. From 1986-1989, 2,339 properties were placed in service and 90.6% are now non-programmatic. In 1990-1994, 5,553 properties were placed in service, and 36.3% are now non-programmatic. From 1995-1999, the current non-programmatic rate is 11.2%; however, if properties in this time frame were to mirror the trend from the prior five-year period, the number of non-programmatic properties would increase from 742 to 2,402. If the trend from 1986-1989 were to be repeated and 90.6% of the 1995-1999 properties become non-programmatic, this would increase the non-programmatic rate in this cohort from 742 to 5,984 (an increase of 5,242 properties).

These figures are not our baseline forecast, but simply show the potential effect of expiring restrictions. Very few properties have reached 30 years, so no one can predict with any certainty how long most of these properties will remain in the program. Our analysis here simply quantifies the degree of property loss if historical patterns are repeated.

Property Size

Among LIHTC properties placed in service prior to 1990, smaller properties are more likely to have exited the program. The average property size of a non-programmatic property that was placed in service prior to 1990 is 43 units, compared with 73 units for programmatic properties. The trend changes for properties in service after 1990, where programmatic properties tend to be smaller than non-programmatic properties.

These findings are consistent with our discussions with some state HFAs — older properties that have left the program tend to be smaller, and often exit the program because of regulatory burdens that are relatively heavy for small operators. However, those units generally remain affordable even after leaving.

Resyndication History

Resyndication refers to the allocation of tax credits for a property that has already received credits in the past. This is typically done with the intent to preserve the affordability of the property and finance rehabilitation or upgrades.[13] Since new tax credits are allocated, the property's rent restrictions start over and the property must remain affordable through the extended use period.

We have data for 678 cases of tax credit resyndication among programmatic and non-programmatic properties, but the actual number of resyndicated properties may be higher than this. Some states indicated that resyndication is quite common, while other states said it occurs less frequently but is starting to be incentivized more.

The rate for resyndicated programmatic properties is high — 96.2% of properties that have resyndicated remain programmatic. Properties that receive a new set of tax credits restart the rent-restriction clock, pushing the expiration date further. It would rarely be the case that a resyndicated property would have had the chance to exercise a QC given the relative recency of the program.

Resyndication is often done with the express intention of keeping a property affordable, made possible through securing funds necessary for rehabilitation. Because of this, resyndication and near-term LIHTC exit risk are strongly negatively correlated.

State

The LIHTC program is largely decentralized. While funding comes from the purchase by investors of federal tax credits allocated to LIHTC projects, state governments decide how to allocate credits according to their Qualified Allocation Plan (QAP), which also contains stipulations for property owners who are awarded the tax credits.

Some states will mandate or incentivize extended use periods longer than the 15-year federal minimum. NHPD has identified 11 states for which this is true, with extended use periods ranging from 18 years to 99 years.[14] These increased restrictions appear to decrease the rate of non-programmatic properties. Controlling for average year placed in service, nine of the 11 states have a disproportionately low rate of non-programmatic properties, as seen in Exhibit 3. Therefore, LIHTC properties in states with longer extended use periods will generally correlate with lower risk of near-term exit.

[13] Extra Credit: Considering Resyndication; Brian Carnahan and Jon Welty; June 1, 2014 (novoco.com)
[14] https://preservationdatabase.org/wp-content/uploads/2022/01/Data-Notes.pdf

Exhibit 3: States with Extended Use Periods Higher than the Federal Minimum

State	Extended Use Period (Federal is 15 Years)	Pertinent Years (by Credit Allocation Year)	Higher or Lower Rate of Non-Programmatic vs. Predicted
Alabama	20 Years	2020+	Lower (-4.7%)
California	40 Years	2001+	Lower (-2.8%)
Connecticut	25 Years	2011+, 9% Credits Only	Lower (-5.2%)
Hawaii	30 Years	2016+, 4% Credits Only	Lower (-4.6%)
Kentucky	18 Years	2005-2018	Lower (-8.5%)
Maine	75 Years 30 Years	2004-2012 2013+	Higher (7.6%)
New Hampshire	84 Years 84 Years 45 Years	2004-2018 2019, 9% Credits Only 2020+, 9% Credits Only	Lower (-1.2%)
Oregon	45 Years	2011+, 9% Credits Only	Lower (-3.8%)
Pennsylvania	20 Years 25 Years	2017-2020 2021+	Higher (7.8%)
Utah	35 Years 84 Years 35 Years	2000-2007 2008-2012 2013+	Lower (-3.0%)
Vermont	84 Years	2001+, 9% Credits Only	Lower (-1.5%)

Source: NHPD

Local Housing Market

There is the concern of an increased risk of losing LIHTC restricted properties that may be able to receive a premium due to local housing conditions. The conventional multifamily market has seen tremendous rent growth over the past several years, which has continued to compound the affordability crisis as rents have typically outpaced income growth, especially in highly sought-after neighborhoods. As land and building costs continue to increase, there is a growing concern that properties leaving the LIHTC program may be targeted to be renovated into higher rent properties if they are in an area that experienced or is experiencing strong growth.

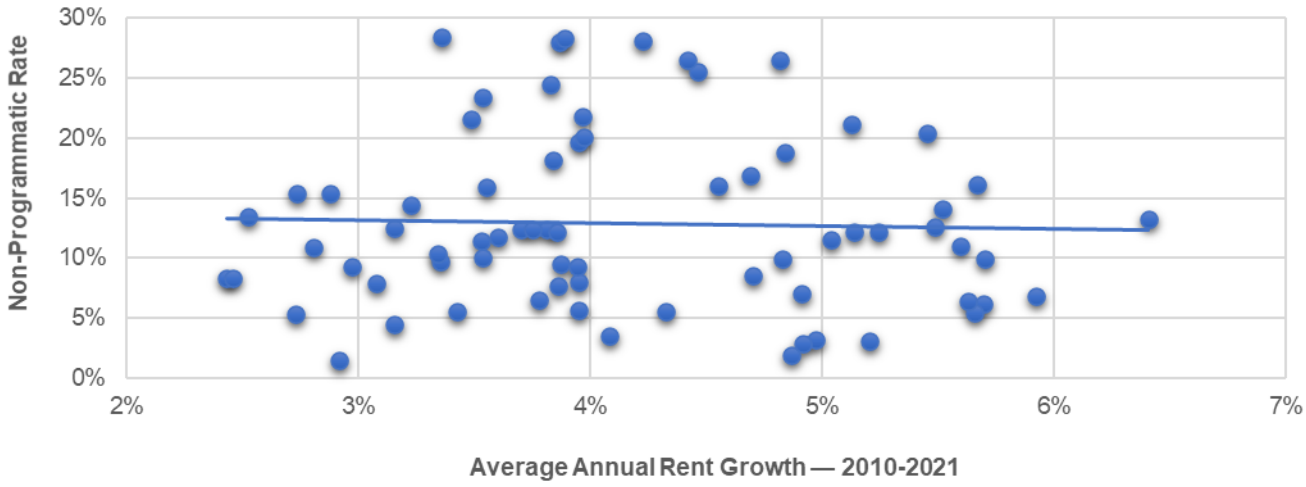
We find that programmatic LIHTC properties are in census tracts with an average poverty rate of 21.4% while the rate for non-programmatic properties was slightly higher at 23.0%.[15] Average income across census tracts was 11.7% lower among non-programmatic properties, indicating on average, non-programmatic properties are in lower-income areas compared with programmatic properties. In high opportunity areas, 10.3% of LIHTC properties are non-programmatic compared with 13.4% outside of

[15] Prior research from HUD noted that LIHTC properties were repositioned as market rate after 15 years tended to be in low-poverty areas. Of course, our studies are not directly comparable — HUD's study was conducted 10 years ago and focused specifically on properties leaving the program after 15 years, whereas our approach is broader, focusing on all non-programmatic.

these areas. Given the elevated rental costs, high opportunity areas especially benefit from affordable housing, so it's encouraging that an outsized portion of LIHTC units are still in the program.

We leveraged Reis's rental data to calculate the average rent across the nation's top 71 major markets from 2010-2021. We found that rent growth and the non-programmatic rate are largely independent of each other, as seen in Exhibit 4. There is a slight negative trend, but the result is not conclusive. This shows that there is little to no correlation between the rate of LIHTC properties leaving the program and metro area rent growth over the past 11 years. Intuitively, areas that have seen much higher rent growth may be at higher risk of losing LIHTC properties since there is more of an economic incentive to move units to market rent levels. However, our results are not too surprising given the dynamics within metro areas differ significantly from submarket to submarket, and more localized data could be more informative.

Exhibit 4: Non-Programmatic Rate vs. Average Historical Rent Growth by MSA



Source: Freddie Mac tabulations of HUD, NHPD and Reis data

Exhibit 4 includes properties that left the LIHTC program for any reason. If we narrow our scope to properties that leave via a QC provision, then we do find some correlation. QCs are the primary way in which a property leaves the program before maturity of LIHTC restrictions and is a deliberate action taken by the property owner to no longer be subject to rent restrictions. Our known population of properties that have exercised a QC is very limited (86 properties), but the average annual rent growth from 2010-2021 is 5.5%, compared with 4.1% for other non-programmatic properties. This suggests that there is a potential trend that QCs tend to be used in areas of higher rent growth.

Our analysis of rent growth and the non-programmatic rate is a simple correlation computation that does not capture regulatory constraints or property owner objectives. Areas of high rent growth are more likely to be in states with stricter LIHTC requirements, partially due to these states having less affordable rental housing. For example, California, a state known for high housing costs, is also known for having LIHTC stipulations that make it more difficult for properties to leave the program. In addition, mission-driven LIHTC owners in higher-cost areas may be more incentivized to keep properties in the program because tenants in these properties have few affordable options outside of LIHTC.

Rent Level, Market vs. Max LIHTC

As market rate rents increased, fewer conventional market rate properties remain affordable at 60% of AMI and below, creating a gap between maximum restricted LIHTC rents and conventional rents. If market rent is substantially higher than maximum LIHTC rent, this could entice property owners to reposition a LIHTC property as market rate either at expiration of affordability restrictions or before expiration via a QC.

Using rent data from Reis and income data from the Federal Housing Finance Agency (FHFA)[16], we compute a market rent to 60% AMI income ratio for the top 71 markets across three time periods: 2000, 2010 and 2021. We then take the average of these three periods to determine a long-run market rent to 60% AMI ratio. For the nation, the average rate is 110% but this is skewed by larger, more expensive metros. The simple average across the 71 metro areas is 89%.

Comparing the average rent to 60% AMI rate to the rate of non-programmatic properties shows they are negatively correlated, meaning that the higher the market rent is compared with 60% AMI rent, the less likely LIHTC properties are to leave the program. This implies that there was no evidence of more properties leaving the LIHTC program in areas where market rents are substantially higher than the maximum LIHTC rent allowed.

Alternatively, we can calculate the change in the ratio from 2010 to 2021 to see which markets experienced a shrinking or expanding gap between market rent and 60% AMI rent. Correlating this rate with the non-programmatic rate, we continue to find no relationship between the propensity for a property to leave the LIHTC program and difference in market rents and maximum LIHTC rents.

Summation of Factors Influencing LIHTC Exit

The decision of whether to exit the LIHTC program ultimately depends on the interests of property owners and on regulatory considerations. However, there are multiple factors that are correlated with propensity to exit the program. We find that nonprofit ownership is associated with lower exit risk. Credit allocation year is also a major factor, with properties that have recently received tax credits being far less likely to leave the program. Properties that resyndicate are also less likely to leave the program. Furthermore, states with strict regulations concerning LIHTC restrictions generally lose fewer LIHTC units.

Other factors have a less straightforward influence. Property size plays a role, but the trend is inconsistent throughout time. Local housing market conditions can impact the decision to exit, but we were unable to draw definitive links between market conditions and the rate of non-programmatic LIHTC.

However, data analysis does not always paint a complete picture. Our analysis is based on metro-level trends and does not consider submarkets within metro areas or rural areas. In discussions with HFAs, we learned that the loss of LIHTC units is most acutely felt in metro areas generally, particularly metro areas

[16] We use FHFA's data because it's the official income data used by Freddie Mac. FHFA's income figures are based on HUD's estimates and are the exact same for most metro areas. There are some cases where they deviate, but this is uncommon, and deviations are small (average of 2.4% difference).

with high rents or fast-growing rents. These exits are typically via a QC, which we have very limited data on but indicate some trends for risk in higher-growth metro areas. Meanwhile, properties in rural areas are unlikely to experience the same level of rent increases and, therefore, are potentially at less risk of exiting the program.

What Happens to LIHTC Properties that Become Market Rate?

Once a LIHTC property exits the program, rents at the property are no longer subject to restrictions, provided the property does not receive other subsidies and is not subject to other restrictive covenants. The lack of restrictions raises the possibility of units being repositioned at higher, market rate rent and consequently falling out of the affordable stock.

Building a Database of Properties

Our population of non-programmatic loans comes from NHPD and HUD, but neither dataset contains observed rents on the specific properties. To determine what happens to LIHTC properties when they leave the program, we merged our non-programmatic file with Yardi Matrix's database.

To best match properties, we also narrowed down our search to seven metro areas: Dallas, Indianapolis, Los Angeles, Orlando, Phoenix, Seattle and Washington, D.C. These locations were chosen because they are geographically and culturally diverse and had relatively large non-programmatic populations. We also filtered out non-programmatic properties with fewer than 50 units since Yardi only tracks properties with at least 50 units. After standardizing and manually matching addresses, we matched 181 properties.[17] This labor-intensive detailed work represents just 3.4% of the non-programmatic population, but we feel it is informative.

Property Quality and Location

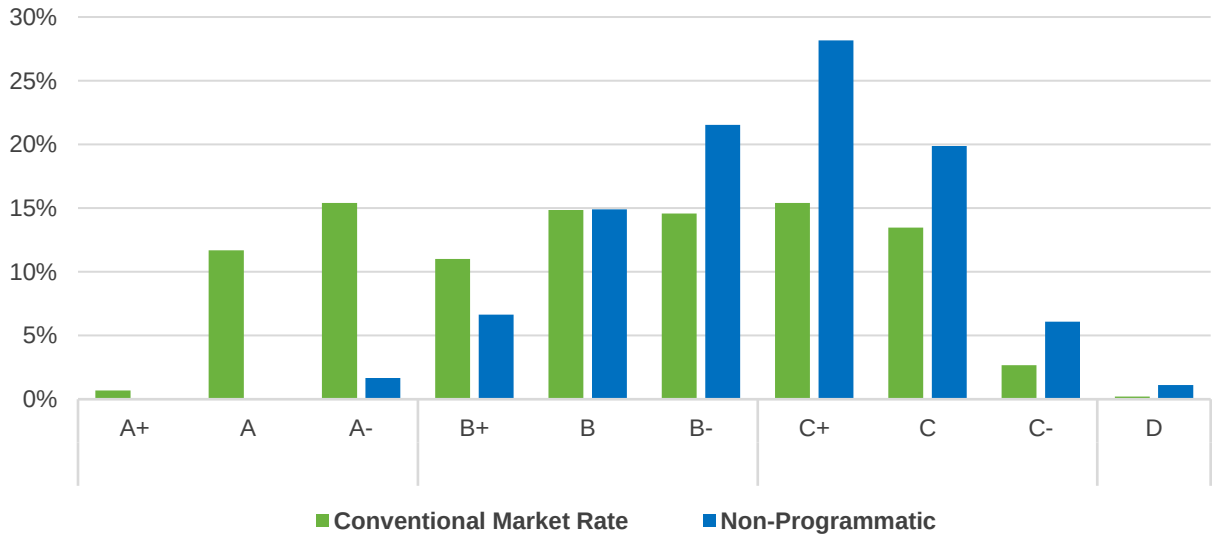
Non-programmatic LIHTC properties are considerably older than other market-rate properties. The completion year for former LIHTC properties across the seven metro areas is 1982, with values ranging from 1973 (Dallas) and 1994 (Orlando). The average completion year for all properties, including market rate, across these seven metro areas is 1992.

[17] Not all non-programmatic LIHTC properties lose affordability restrictions. In our sample of 181 properties, 127 transitioned to market rate, while the remaining 54 properties remained fully or partially affordable, according to Yardi Matrix's classifications. Most of the properties that remain affordable are likely supported by a non-LIHTC subsidy, although some may still be LIHTC but not captured appropriately due to data collection and timing inconsistency. Roughly 70% of non-programmatic LIHTC properties converted to market-driven apartments while the remaining 30% may still be subsidized. For our analysis, and without knowing the potential non-LIHTC subsidies, we will still consider all 181 properties to be non-programmatic LIHTC.

Non-programmatic LIHTC properties generally have lower property ratings and lower location ratings compared with conventional market rate properties, as seen in Exhibits 5 and 6.[18] Yardi measures property and location quality using an A-D scale, with A indicating higher quality, D indicating lower quality and the average rating of B across all properties. However, for non-programmatic LIHTC, the average is only a C+ for both metrics. It is encouraging that when matching current improvement rating to these non-programmatic properties, we do not see that they have moved up to A ratings. This suggests that the properties are not being repositioned to the top of the market, which would completely squeeze out all low-income households.

Given that LIHTC properties are typically older and have, on average, a lower property quality rating, LIHTC properties will most likely need rehab, and without new credits to help fund those rehab costs, the property may have to rehab outside the program. Acquisition and rehabilitation accounts for about 4 in 10 LIHTC transactions, with the remaining being new construction.[19] Without additional credits or preservation of affordable units, renovation costs could be passed on to the tenant in the form of higher rents.

Exhibit 5: Improvement Rating by Property Type

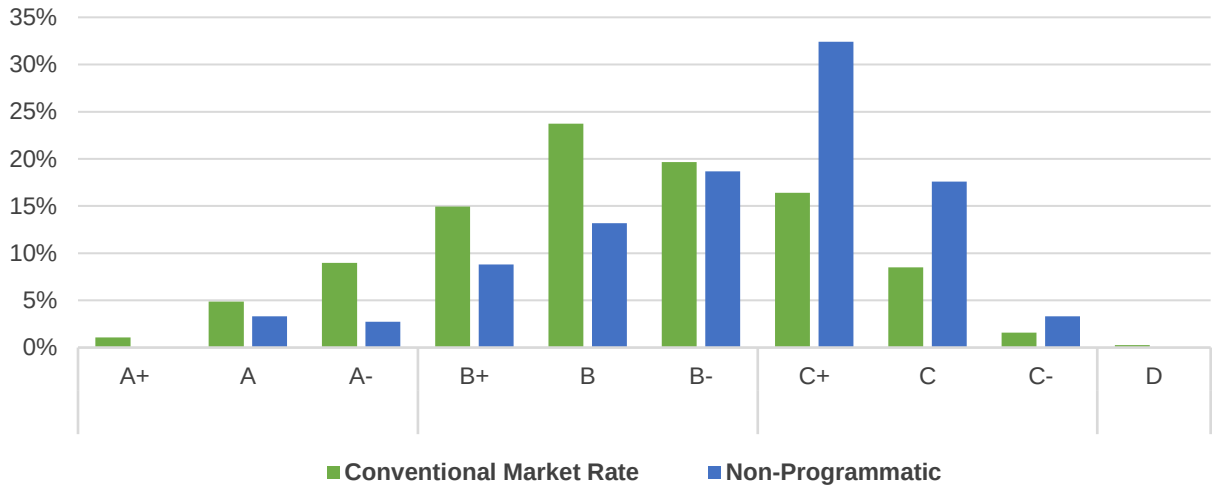


Source: Freddie Mac tabulations of HUD, NHPD and Yardi Matrix data

[18] Yardi Matrix's rating classifications attempt to capture the property and location level characteristics that influence rent levels. For more information, please see https://www.yardimatrix.com/About-Us/Our-Methods/How-We-Define-The-Apartment-Supply/Property-Ratings.

[19] Yardi Matrix reports on the earliest completion year, so it can happen that a property's first phase occurs before 1986 and is not supported by LIHTC, whereas the second phase is supported by LIHTC, but the completion year is not updated.

Exhibit 6: Location Rating by Property Type



Source: Freddie Mac tabulations of HUD, NHPD and Yardi Matrix data

Rent Comparison

Of the 181 non-programmatic properties in our study, Yardi reports on the current rent data of 134 of these properties.[20] Rents in non-programmatic LIHTC properties tend to be lower than market-rate units that were never in the LIHTC program. This is true for all seven metro areas studied, shown in Exhibit 7 below. The largest rent gap was in Dallas, where non-programmatic LIHTC rents are 26.5% lower than market rate, while the smallest gap was in Phoenix, where non-programmatic rents are only 3.0% lower.

While LIHTC properties leaving the program pose a risk in the form of rents no longer being restricted, our analysis shows that non-programmatic LIHTC rents are still materially below the rest of the market. Of course, part of the reason why rents are lower is because non-programmatic LIHTC properties tend to be older properties, with lower improvement ratings and in areas with a lower location rating per Yardi's classification. We can account for this by comparing non-programmatic properties with market-rate units that have the same improvement and location rating. This control allows for a fairer comparison of like properties by quality and location.

The results after controlling for property and location condition are mixed. Non-programmatic rents are higher in four of the seven metro areas. Rents are lower than conventional market rate in Dallas, Los Angeles and Orlando. The simple average across all metro areas is 1.2%.

[20] This includes 127 purely market-rate properties and seven partially affordable properties (no fully affordable properties provide rent data in Yardi Matrix) and one of the market-rate properties does not have current rent data. We compared our finalized list of 134 properties with the broader rental population in these seven metros, which includes a total of 11,019 properties tracked by Yardi.

Exhibit 7: Non-Programmatic LIHTC Rent by Market

Market	Properties (with Rent Data)		Average Rent (December 2021)				
	Non-Programmatic	Market Rate	Non-Programmatic (% AMI)	Market Rate	% Difference Between Non-Prog. and Market	Market Rate (Controlled)*	% Difference Between Non-Prog. and Market (Controlled)
Dallas	51	2,997	$1,065 (49%)	$1,449	-26.5%	$1,114	-4.4%
Indianapolis	24	683	$953 (47%)	$1,104	-13.7%	$949	0.4%
Los Angeles	16	1,678	$2,160 (86%)	$2,537	-14.9%	$2,380	-9.3%
Orlando, FL	12	739	$1,542 (86%)	$1,705	-9.5%	$1,586	-2.7%
Phoenix	12	1,382	$1,596 (78%)	$1,646	-3.0%	$1,391	14.8%
The District	11	1,644	$1,788 (57%)	$1,992	-3.5%	$1,783	9.3%
Seattle	8	1,763	$1,934 (64%)	$2,004	-10.2%	$1,769	0.3%
Combined	133	10,886			-11.6%		1.2%

Source: Freddie Mac tabulations of HUD, NHPD and Yardi Matrix data. The "Market Rate (Controlled)" column adjusts the comparison population to mirror the improvement and location rating of non-programmatic properties, as described in the paragraphs preceding this table.

The column "% Difference Between Non-Prog and Market" shows that non-programmatic rents tend to be lower. This finding is symptomatic of filtering, which is the process by which units become more affordable as they age. Many of the non-programmatic properties were new construction or were substantially rehabilitated under the LIHTC program, but as they aged, they moved into the affordable stock.

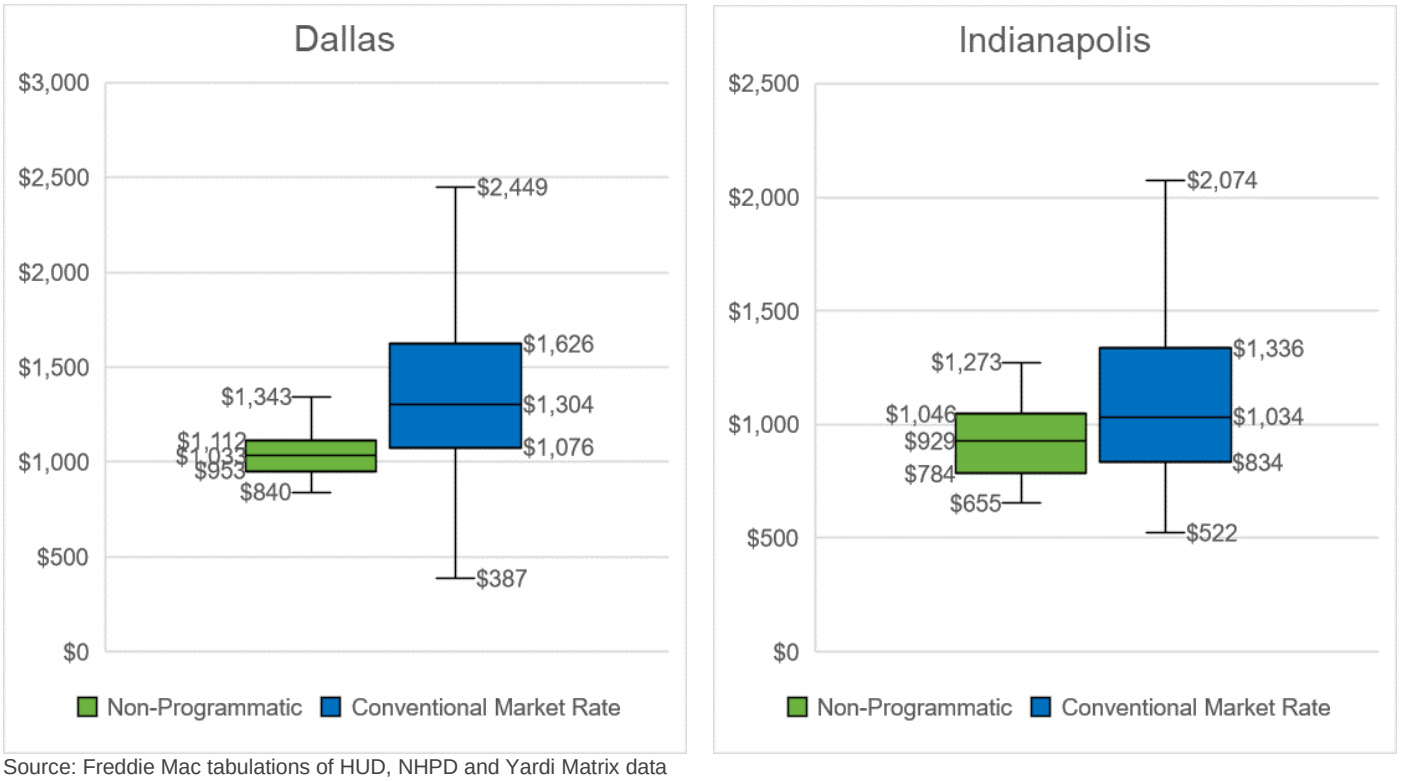
The last column, which controls for property type, shows that similar units do not rent for substantially different amounts regardless of former LIHTC status, which signals that non-programmatic units are priced based on market forces. There are some large disparities on the metro level even when controlling for improvement and location quality, such as in Phoenix, the district and Los Angeles. For the first two metro areas, unit sizes of non-programmatic LIHTC properties are between 30% to 40% larger which helps to explain the gap. In Los Angeles, however, this same phenomenon is present, but rents are still materially lower. This suggests that non-programmatic LIHTC properties in Los Angeles are more affordable than their conventional market rate counterparts, even when controlling for pertinent variables.

In general, many non-programmatic LIHTC properties continue to provide affordable housing. Rent levels across these metro areas for non-programmatic properties are affordable, on average, to tenants making 61% of AMI. This provides housing for lower-income tenants who may not be eligible for subsidized housing or who are eligible but not able to utilize it due to long waiting lists.

Exhibit 8 further illustrates the average rent differences between market rate and non-programmatic LIHTC in the two metro areas for which we have the greatest number of observations: Dallas and Indianapolis. In Dallas, median rent for non-programmatic LIHTC is lower than the 25th percentile of its

market-rate counterpart. Indianapolis's non-programmatic distribution deviates from its conventional market-rate counterpart less but is still noticeably lower.

Exhibit 8: Rent Distribution in Dallas and Indianapolis



Source: Freddie Mac tabulations of HUD, NHPD and Yardi Matrix data

Our sample size of 134 non-programmatic properties is small but robust. The variation as measured by the coefficient of variation (standard deviation divided by mean) for the non-programmatic sample is smaller than that of conventional market-rate properties for all seven metro areas. This means that even though the sample size is small, the rents are less spread out for the non-programmatic sample. Although coefficient of variation is not a direct way of measuring sample robustness, the tight spread of the non-programmatic data signals that the data does not have a high share of outliers.

Comparison of Non-Programmatic Rent with Market Rate Submarket Rent

We studied the intra-metro trends of conventional market rate and non-programmatic rents in Dallas and Indianapolis, specifically looking at property distribution at the submarket level. We found that non-programmatic properties are more likely to be in low-rent submarkets, per Yardi Matrix's submarket classification. Of the 75 non-programmatic properties for which we have data, only eight (10.7%) are in submarkets with an average rent level more than 5% above the metro average. This rate of 10.7% is considerably lower than the conventional market rate of 36.5%.

LIHTC properties are less prevalent in high-rent areas generally, but the absence of non-programmatic units in high-rent areas corroborates our findings that owners typically are not removing properties from the LIHTC program to drastically raise rents. Comparable rents do not greatly exceed LIHTC maximum

rents, so hiking rates substantially is often not feasible. As a result, conversions to market rate are not as dramatic as they might be if the properties were in areas with higher-rent levels and the rent was adjusted fully to market rate. However, this is not the case for deeply discounted LIHTC units, such as units affordable at 30% AMI, since these units can still see large increases even in lower-rent areas.

Opportunity for Workforce Housing

Non-programmatic LIHTC represents a loss of the strictly affordable stock, which is the segment of the market with the most need, but it benefits another market segment: workforce housing, where there is also a need. Market-rate units in the seven metro areas of our non-programmatic study are roughly evenly spilt across Yardi's four market positions: Discretionary, High Mid-Range, Low Mid-Range and Workforce. Non-programmatic units are heavily concentrated in Low Mid-Range and Workforce, with these two combined making up nearly 90% of units, as seen in Exhibit 9. It is encouraging that no units move to Discretionary, which would indicate that properties are repositioned to the top of the market.

Exhibit 9: Market Position by Property Type

Market Position	Unit Count		Rate	
	Conventional	Non-Programmatic	Conventional	Non-Programmatic
Discretionary	490,999	0	17.8%	0.0%
High Mid-Range	817,727	3,737	29.6%	11.3%
Low Mid-Range	837,124	14,919	30.3%	45.2%
Workforce	613,877	14,334	22.2%	43.4%

Source: Freddie Mac tabulations of HUD, NHPD and Yardi Matrix data

Additionally, a high percentage of non-programmatic LIHTC units are still affordable at LIHTC maximum rent levels. Exhibit 10 breaks out conventional market rate and non-programmatic units by AMI affordability. Roughly 61% of non-programmatic units are affordable at 60% AMI, which is nearly twice the rate of market-rate units (31.5%).

Exhibit 10: AMI Breakout by Property Type

Affordable At…	Unit Count			Rate		
	Conventional	Non-Programmatic	Programmatic	Conventional	Non-Programmatic	Programmatic
50% AMI	332,716	11,321	824	14.1%	42.1%	26.1%
60% AMI	409,225	5,155	2,330	17.4%	19.2%	73.9%
70% AMI	387,908	3,795	0	16.5%	14.1%	0%
80% AMI	404,504	1,250	0	17.2%	4.6%	0%
100% AMI	485,744	3,782	0	20.6%	14.1%	0%
>100% AMI	332,836	1,581	0	14.1%	5.9%	0%
Average AMI	**76%**	**61%**	**55%**			

Source: Freddie Mac tabulations of HUD, NHPD and Yardi Matrix data. The programmatic population comes from Freddie Mac's 2021 equity portfolio.

Workforce housing typically serves renters who make below the median income for the area but are not eligible for subsidy. In this way, workforce housing has one distinct advantage over rent-restricted units; the latter is affordable but not always available to all renters. The downside is that whereas LIHTC units only permit lower-income renters, workforce housing is unrestricted, meaning that lower-income renters may face competition from higher-income earners. In addition, there is still a risk that since non-programmatic properties are not rent restricted, they can move rents higher at a substantially faster pace than LIHTC units. Although empirically this appears to be rare, it may still occur.

Overall, programmatic LIHTC units are generally the most affordable and guarantee they will remain affordable, followed by non-programmatic LIHTC. A LIHTC property ending restrictions and converting to market rate generally causes a rise in rents over time but may not necessarily lead to a substantial increase; it simply means that rent pricing will be market-driven instead of policy-driven.

Loss of Deeply Affordable Units

The creation of workforce housing units stemming from the loss of LIHTC units is a silver lining of the LIHTC exit process, but the loss of affordable LIHTC units can still be very problematic. This is especially true for deeply affordable units at 30% AMI. The median non-programmatic LIHTC unit is affordable at 60% AMI, but there are no units in our non-programmatic dataset that are affordable at 30% AMI, while only 0.1% of conventional market-rate units are affordable at this level. Since market rents can almost never support rents at this level, the conversion of a LIHTC property to market rate typically means the loss of deeply affordable units at 30% AMI. Of course, as demonstrated earlier, this is not a major issue for higher AMI units. For example, units priced at 60% AMI are unlikely to experience an increase on par with a 30% AMI unit converting to market rate.

Conclusion

Rent and income restrictions for LIHTC properties generally persist for at least 30 years, but as the program ages and more properties near the end of their compliance periods, the risk of affordability loss increases. Certain factors are correlated with the risk of ending LIHTC rent restrictions such as ownership type, property characteristics and local housing market. The decision to convert properties to market rate, however, ultimately lies with the property owner who is motivated by a variety of factors.

Fortunately, the propensity for LIHTC properties to move to a rent level on par with market rate is low. Although rent for units among non-programmatic LIHTC properties is typically higher than programmatic LIHTC rents, they are still materially below conventional market-rate rent levels. In this way, LIHTC properties leaving the program play a role in a community's overall rental housing strategy by adding to the workforce housing stock, thus increasing affordable access to households that may not qualify for subsidized housing.

However, several risks remain, particularly around the loss of deeply affordable units and the risk of rents increasing due to market conditions or rehabilitation to the property. Available public subsidies can best benefit those properties that provide deeply affordable housing as well as affordable housing in areas without a lot of access to similar priced housing. Understanding the risks associated with the loss of affordable units from LIHTC properties can help inform what may happen as more properties exit the program and provide strategies to help preserve affordable housing to help those tenants most at risk of losing affordable housing.

Appendix

Data Quality

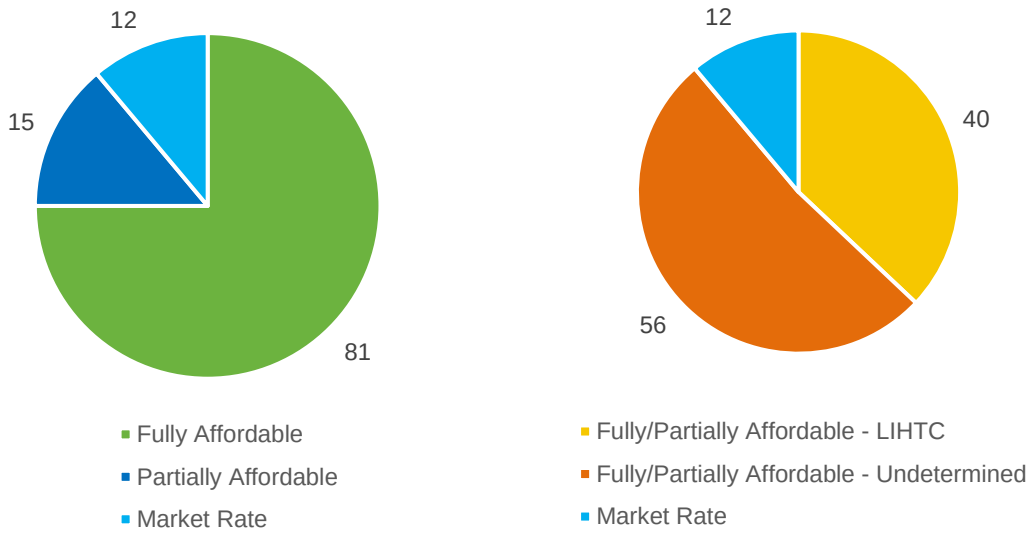
HUD possesses the industry's most comprehensive LIHTC dataset. Once each year, HUD asks each state for updated property-level LIHTC data, but the format and contents of the data sent back by each state varies.

As noted above, state governments are in charge of administering the tax credits. Therefore, there is no centralized database that is updated in an automated and consistent fashion. While HUD tries to ensure high data quality, there are inevitably shortcomings.

Yardi Matrix is a leading real estate market intelligence firm and provider of commercial real estate data. Yardi tracks market-rate apartments and affordable properties, and the latter gives us a benchmark for our tabulation of HUD and NHPD data. We do find that our designation and Yardi's designation typically agree.

We sampled a subset of our properties classified as programmatic and lined them up with Yardi's database to see how they are currently classified. Our random sample consists of 108 properties, and of these properties, Yardi classifies 12 of them as market rate, while 15 are partially affordable and 81 are fully affordable. Within this fully and partially affordable universe, 40 were confirmed to be programmatic LIHTC. The remaining 56 properties do not specify subsidy so we cannot confirm that they are LIHTC. Some of these properties have non-LIHTC subsidies on them so it's possible that the fully affordable flag is referring to another subsidy. If this were the case for a property, then that property should be designated as non-programmatic.

Exhibit 11: Composition of Programmatic Properties



Similarly, as noted previously in our analysis, our population of 181 non-programmatic properties is mostly composed of market-rate units but there are some affordable properties as well. Some are likely subsidized by other programs aside from LIHTC, but 6.5% are LIHTC properties according to Yardi.

From this analysis, we acknowledge that our list of programmatic and non-programmatic properties is subject to a larger degree of error than we're accustomed to. There are several sources of error for any discrepancy between the datasets beyond data collection errors and methodology differences. For example, there are timing differences between the datasets, since Yardi designations are as of the first quarter of 2022 while HUD's data lags by a few years. It's also possible that a property will exit the program but receive more tax credits at a later date.

Despite the uncertainty, we believe that the data is robust enough to draw meaningful conclusions. HUD produces the most comprehensive view of the LIHTC market, and this is the source that we primarily rely on. Yardi's data acts as a benchmark, which shows some inconsistences but generally agrees with HUD data. In addition, Yardi's data supplements HUD's data in that it allows for us to track the rents of non-programmatic properties. For the rent and AMI analysis in this section, we only include properties that are non-programmatic per both HUD and Yardi, so the data quality is very high.

Aggregators

There is not much data regarding aggregators which we could digest and analyze for purposes of this paper. Aggregators have only increased in prominence in the past 5-7 years, the sale of equity interests in LIHTC transactions are private sales, and the companies do not act consistently in all deals. They might act as a typical equity investor or syndicator in most deals and only take a more aggressive investment posture with a small number of LIHTC properties.

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