

Government of the District of Columbia
OFFICE OF ZONING



November 4, 2005

George Rothman, President
MANNA, Inc
828 Evarts Street, N E
Washington, D C 20018

Re: Z.C. Case No. 04-33 / Inclusionary Zoning

Dear Mr Rothman

The Office of Zoning is in receipt of your letter dated October 31, 2005, regarding the above-referenced case

The Zoning Regulations are strict regarding the timeliness of submissions into case records. The record on this case was closed on September 8, 2005, therefore, your letter cannot legally be included in the above-referenced file.

Thank you for your letter. If you have any questions, please do not hesitate to me at (202) 727-0340.

Sincerely,


Sharon S. Schellin
Acting Secretary to the Zoning Commission
Office of Zoning

~~ZONING COMMISSION~~
~~District of Columbia~~
CASE NO. 04-33
EXHIBIT NO. 159

Enclosure



Rebuilding Neighborhoods Through
Affordable Homeownership

MANNA

501 (C)(3) non-profit organization.

Please designate MANNA INC -- #8847 (Metro DC)
and #7621 (Central MD) -- in the United Way
and Combined Federal Campaigns

October 31, 2005

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TO: DC Zoning Commission Members
Chairman Carol J. Mitten
Vice-Chair Anthony Hood
Commissioner Gregory N. Jeffries
Commissioner Kevin Hildebrand
✓ Commissioner John Parsons

FROM: George Rothman, President 

RE: Long Term Affordability Restrictions and Their Negative Impact on Equity for
the Low Income Homeowner

For years Manna has been the leading non-governmental organization producing affordable homeownership housing for low income residents in DC. I think we have a good idea what works and what low income people need and want.

I have already testified regarding long term affordability restrictions and our opposition to those which require re-sale to the same income/AMI category. Since my testimony, I have heard from many others who share our view, including many prospective low income homeowners, executives from LISC, Housing Counseling Services and others.

Manna has recently completed research which shows the severe negative impact of long term affordability requirements that require resale to the same AMI category on low income homeowners. It demonstrates these restrictions are unfair and discriminatory. I'm attaching that paper for your information since the vote on inclusionary zoning is near, and I think this research is very important for your decision.

Manna knows and understands affordable homeownership. We counsel prospective homeowners everyday. When they hear what's occurring, they become angry. They see it as unfair and discriminatory, and I'm not exaggerating.

I urge you not to adopt any policy regarding affordable homeownership which restricts resale to the same AMI category without thinking about the consequences. Please read the attached paper which documents how poor people will be affected.

Thank you.



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LONG TERM AFFORDABILITY RESTRICTIONS AND THEIR NEGATIVE IMPACT ON EQUITY FOR THE LOW INCOME HOMEOWNER

by

George Rothman, President

Manna, Inc.

and

Frank Demarais, VP & General Manager

Manna Mortgage Corp

October 31, 2005

In America, homeownership has always provided certain financial and emotional benefits that rental housing has not and cannot provide. Those benefits include equity buildup, or wealth creation, use of home equity loans to finance children's education, self-esteem and many others which are readily accepted by the general public. That is why homeownership is often referred to as the American Dream.

Many areas of the country have experienced rapidly rising housing prices during the past five years. With this condition has come an increasing need for affordable housing. In many areas there's an "affordable housing crisis."

Unfortunately, some government agencies and some housing advocates have been devising tools and plans which severely restrict the benefits of homeownership for low income homeowners who benefit from affordability subsidies or government loans in new developments. (This is also happening in other areas of the country, but that should not be any justification for limiting the equity build up for low-income folks. Similar mistakes are simply multiplying because of lack of thorough analysis and evaluation of consequences.)

Agencies such as the DC Department of Housing and Community Development (DHCD) and the National Capital Revitalization Corporation (NCRC) are often imposing severe long term affordability restrictions, or covenants, which limit the future resale of the home and have an extremely adverse impact on the first-time owner in the future, when compared with the advantages available for what are known as "market rate" buyers. For example, a popular limitation is to require the first-time low income buyer to sell to another buyer in the same income category, or %age AMI (Area Median Income), for a long or very long period of time, e.g. 10, 15 or 30 years. These types of restrictions are also being incorporated into one of the Inclusionary Zoning proposals.

The purpose of the restrictions is to maintain affordable housing units for the long term, but it appears that some of the agencies and proponents of these restrictions do not consider what may happen in the future to the low income buyers. As affordable homeownership housing producers, Manna deals with these issues on a regular basis, and there appears to be little thought given as to what happens when the low income owner needs or wants to sell.

One of the misconceptions related to the impact of restrictions is based on assumptions about where buyers fit into certain income categories, e.g. 50% AMI. Often, assumptions are made which show buyers making the highest income permitted in a category, but that is unrealistic because that doesn't happen often. That assumption exaggerates what the original owner will receive in the future when restricted to selling to a new buyer in that income category. Categories are broad, and there's no guarantee that one could find a subsequent buyer at the same or higher income in a particular category at a particular time. And, if that is the case, the situation becomes even worse for the low income homeowner. Even though it's unrealistic to assume new buyers will be at the maximum allowed for an income category, we use it here in our examples to portray the best possible outcomes. Therefore, **our examples are optimistic and still show very poor results for low income buyers.**

In our opinion, the results of these restrictions make certain that low income homeowners will remain second class citizens and do not offer them a vehicle to rise out of low wealth status. It is simply unfair and discriminatory, though legal, to impose such restrictions. **In effect, low-income homeowners become glorified renters.**

People often move because of job changes, because they want to marry and/or have a family, or because of illness or disability. In other words, there are good reasons for moving before affordability periods expire. Affordability restrictions can substantially limit equity build-up during the control/affordability period, even though general home values would have increased significantly, causing any seller to incur dramatic increases in housing costs with very little equity take-out to cushion the increase. Why should low-income homeowners be penalized in an unreasonable manner for needing to move?

Low income people also buy because they want to be able to leave a valuable asset to their children or grandchildren. Severe affordability restrictions can also adversely affect this valid reason for homeownership and prevent wealth transfer among generations which is common among the middle and upper classes.

For many years, the ability to accumulate equity in a home has been the major factor in helping people move up the economic ladder. That ability is now being severely taken away—especially in Washington, DC.

Here's how:

If all mortgage affordability decision criteria remained *constant*, then affordable housing resales would re-sell during affordability periods at below market prices equal to the original sales prices times the percentage income increases. FOR EXAMPLE If 80% AMI for one person increased at 2% a year for 10 years, from \$50,000 to \$61,000 (22% increase), a \$175,000 home affordable to an 80% AMI person in 2005 when interest rates are 6% would be affordable to another person in the 80% AMI category in 10 years at a price of \$221,000 (22% increase) **if interest rates remained the same.** The seller at that time would realize about \$58,000 due to amortization and after sales commission.

However, mortgage affordability criteria, such as (1) interest rates, (2) tax and insurance costs, (3) mortgage debt ratio tolerances *don't stay constant*. Income increases for very low and low income persons have historically tracked to 2-3% annually, while home prices have increased annually at approximately 5%. A lower income buyer of a restricted affordable home could face small or negative

equity increases in the future based on the limitation of income of his/her future buyer. Therefore, the *following example illustrates what really happens* when the above variables are factored into the projections

Example - Assumptions

Income increases at 2% per year

Taxes and insurance/condo fee increase at 3% a year

Interest rates increase to 7 ½ %.

Original sales price in 2005 is \$175,000 condominium to a buyer at 80%AMI

Resale is restricted to a subsequent buyer earning 80% of AMI

- **After 5 years** the seller could expect a sales price, net of real estate sales costs, of about 13% below original purchase price, or \$152,000. Amortization of 7% would reduce the loss to 6% above original price. This happens because resale is restricted to a buyer in the same income category, and even when the income has increased over the 5 years by more than 10%, a higher interest rate (7.5% vs original 6.0%) and higher taxes and insurance/condo fees reduce the amount of loan that such a person can afford to below original sales price. Sales commission and taxes eat up another 7.1%. Amortization of 7% leaves net equity still at a loss.
- **After 10 years** the seller could expect a sales price, net of real estate sales costs, of about 6% below original purchase price, or \$167,000. Amortization of 16% would create net proceeds of about 10%, or \$17,500 on a \$175,000 original price. With that amount, and the 2% increases in income over ten years, the owner could then afford only a property which costs about \$189,000, if condo, or \$220,000 if single family (affordable loan plus \$10,000 proceeds after 3% closing costs). This is below most market rate DC properties today (2005). This happens because resale is restricted to a buyer in the same income category, and even when the income has increased over the 10 years by 22%, a higher interest rate (7.5% vs original 6.0%) and higher taxes and insurance/condo fees reduce the amount of loan that such a person can afford to about 1% above original sales price. Sales commission and taxes eat up 7.1% of the sales price. Equity from amortization of 16% then leaves only about 10% of original price to the seller.
- **After 15 years**, the seller could expect a sales price, net of real estate sales costs, of about 6% of original price. Amortization of 29% would create net proceeds of about \$58,000 on a \$175,000 original price. With that amount, the owner could then only afford a property which costs \$230,000 if condo or \$287,000 if single family (affordable loan plus \$52,000 proceeds after 3% closing costs). This is below most market rate DC properties today (2005).

These proceeds also need to be considered relative to remaining a renter. If rents were \$200 less than mortgage payment, the renter saving the \$200 a month in a bank account earning 3% would have about \$28,000 versus the \$17,500 gain over 10 years in the example, and about \$45,000 versus the \$58,000 gain over 15 years.

NOTE ON THE CALCULATIONS BELOW: THE EQUITY BUILDUP SHOWN USES THE “AFFORDABLE SALES PRICE” AS THE BASE FROM WHICH PRICE INCREASES ARE CALCULATED—NOT THE MARKET PRICE—AND, THEREFORE, INTENTIONALLY UNDERSTATES THE ACTUAL DIFFERENCE, I.E. DISADVANTAGE SUFFERED BY LOW INCOME BUYERS. THIS WAS DONE BECAUSE THE ASSUMPTION OF ANY PARTICULAR MARKET PRICE WAS TOO SPECULATIVE AND COULD SUBJECT THE CALCULATIONS

TO ACCUSATIONS OF MANIPULATION. THE AUTHORS ERRED ON THE SIDE OF CONSERVATISM.

THESE CALCULATIONS ARE EXCLUSIVE OF ANY RECAPTURE OF PUBLIC SUBSIDY, WHICH WE SUPPORT AND WHICH CAN BE ACCOMPLISHED THROUGH A VARIETY OF STRUCTURES THAT ENCOURAGE LONG TERM OCCUPANCY AND COMMUNITY COMMITMENT.

**WHAT CAN 50% AND 80% AMI HOUSEHOLDS AFFORD
TO PAY IN THE FUTURE?**

**Examples of equity buildup limitations with restrictions limiting
resales to the same income category (Base Year – 2005)**

Assumptions for the charts which follow

6% initial interest rate, 30-year, fixed rate loan

38% debt-to-income ratio

\$150 month debt payment (conservative estimate)

2% AMI increase per year 3% tax & insurance/condo fee costs increase per year

- "With Restrictions" assumes amortization plus equity if sold to buyer limited by same AMI %
- "Without Restrictions" assumes amortization plus equity if sold at price increasing 5% per year - *true market based equity increase*. (This assumes original purchase price was either at market or had a subordinate lien for the amount between original purchase price and market value at that time. Therefore, no equity built in at the time of purchase.)

CHART #1 – Net Equity Buildup Upon Resale in 5 Years (rounded to nearest \$100)

	<u>Amount w/ Restrictions</u>	<u>Without Restrictions</u>	<u>Difference</u>
1 person household, 50% AMI	Loss of \$4,500	Gain of \$19,300	\$23,800
3 person household, 50% AMI	Loss of \$6,800	Gain of \$31,400	\$38,200
1 person household, 80% AMI	Loss of \$9,400	Gain of \$44,700	\$54,100
3 person household, 80% AMI	Loss of \$13,200	Gain of \$64,100	\$77,300

CHART #2 – Net Equity Buildup Upon Resale in 10 Years

	<u>Amount w/ Restrictions</u>	<u>Without Restrictions</u>	<u>Difference</u>
1 person household, 50% AMI	Gain of \$19,800	Gain of \$50,800	\$31,000
3 person household, 50% AMI	Gain of \$33,800	Gain of \$ 82,800	\$49,000
1 person household, 80% AMI	Gain of \$49,200	Gain of \$118,000	\$68,800
3 person household, 80% AMI	Gain of \$71,600	Gain of \$169,100	\$97,500

CHART #3 – Net Equity Buildup Upon Resale in 15 Years

	<u>Amount w/ Restrictions</u>	<u>Without Restrictions</u>	<u>Difference</u>
1 person household, 50% AMI	Gain of \$ 35,600	Gain of \$ 91,800	\$56,200
3 person household, 50% AMI	Gain of \$ 61,400	Gain of \$149,500	\$88,100
1 person household, 80% AMI	Gain of \$ 89,500	Gain of \$212,900	\$123,400
3 person household, 80% AMI	Gain of \$130,400	Gain of \$305,300	\$174,900

Charts 4-6 below estimate opportunities for the first-time homebuyer to purchase a second home based on the loan amount available at their income and a 6% interest rate, plus the proceeds from the sale of the original Affordable Home, estimated With and Without Restrictions as defined above. Proceeds from sale assume additions for equity buildup/loan amortization and deductions for real estate sales commissions and transfer taxes and average DC closing costs.

CHART #4 – Maximum New Home Purchase Amount Affordable Upon Resale in 5 Years

	<u>Amount w/ Restrictions</u>	<u>Without Restrictions</u>	<u>Difference</u>
1 person household, 50% AMI	\$ 66,500	\$105,400	\$ 38,900
3 person household, 50% AMI	\$108,000	\$189,200	\$ 81,200
1 person household, 80% AMI	\$155,500	\$266,800	\$113,000
3 person household, 80% AMI	\$222,200	\$372,500	\$150,300

CHART #5 – Maximum New Home Purchase Amount Affordable Upon Resale in 10 Years

	<u>Amount w/ Restrictions</u>	<u>Without Restrictions</u>	<u>Difference</u>
1 person household, 50% AMI	\$108,600	\$173,000	\$ 64,400
3 person household, 50% AMI	\$180,000	\$281,800	\$101,800
1 person household, 80% AMI	\$258,700	\$401,400	\$142,700
3 person household, 80% AMI	\$373,000	\$575,500	\$202,500

CHART #6 – Maximum New Home Purchase Amount Affordable Upon Resale in 15 Years

	<u>Amount w/ Restrictions</u>	<u>Without Restrictions</u>	<u>Difference</u>
1 person household, 50% AMI	\$131,600	\$247,600	\$116,000
3 person household, 50% AMI	\$220,500	\$403,500	\$183,000
1 person household, 80% AMI	\$318,500	\$574,800	\$256,300
3 person household, 80% AMI	\$461,000	\$824,000	\$363,000

In summary, the above examples, using relatively conservative assumptions, show how and how much low income buyers must forfeit if “same income AMI” re-sale rules are used and how little house they can afford during various control periods. First time owners can easily become renters if they must move for legitimate reasons--because they will not be able to afford to buy in the future.

Long term affordability is a laudatory goal, but its burden shouldn't be placed on the shoulders of low income folks. Individual homeownership must continue to be used to enhance community and individual stability, to catalyze neighborhood revitalization, and to promote wealth creation. For the majority of Americans who are fortunate enough to be homeowners, their homes represent their most significant asset. Stripping the financial gains from the low income homeowners is unfair and, in a sense, discriminatory. There are other existing legal structures available to provide long term affordability, e g rentals, limited equity coops, and community land trusts. There are recapture mechanisms which can be used to recycle subsidies back into affordable housing. These can and should be used by governments and housing producers to accomplish long term affordability goals. But don't saddle the low income homeowners with this responsibility.