Spotlight on Underserved Markets

Affordable Housing in High Opportunity Areas

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Examining Three Properties that Showcase the Efficacy of Providing Affordable Housing in High Opportunity Areas

The degree to which an individual is able to thrive economically is heavily dependent on their social environment. Certain areas foster greater economic success than other areas by offering residents a high level of economic opportunity and mobility. These areas are aptly referred to as high opportunity areas. While there does not exist an industrywide consensus definition for these areas, they generally have five distinguishing features: high income and low poverty, strong economic growth, high-achieving schools, well-developed public transit, and access to quality health care.

High opportunity areas are found all over the country and are home to roughly 18% of the population. Last year, we published a report[1] describing the demographic, economic and housing characteristics of high opportunity areas. We found that, although high opportunity areas provide economic and social benefits for their residents, the development of affordable housing has historically been difficult in these areas. Impediments such as high land and construction costs, lack of buildable land, and zoning restrictions all contribute to the lack of affordable housing development in high opportunity areas, and act as a barrier for lower-income families to access housing. Affordable housing in high opportunity areas is one component of residential economic diversity (RED), which aims to remove social and economic barriers that historically hindered the integration of households of varying income levels in neighborhoods across the country.

In order to better understand local efforts and successes at the property level in specific markets, we examined three case studies of affordable housing in high opportunity areas.[2] The properties discussed are located in markets that meet the criteria for high opportunity areas based on the difficult development area (DDA) criteria as outlined in the Duty to Serve regulation.[3] Studying real-life affordable multifamily properties in high opportunity areas showcases practical solutions and helps to determine which strategies can potentially be effective at addressing these barriers on a larger scale: The successes at the local level can inform broader solutions.

The three properties in our analysis are in markets where there is a pronounced shortage of affordable housing. In each case, these properties are intended to create more economically diverse areas, which will advance the opportunity of all residents, especially those of lower income. They are supported by Freddie Mac funding and received public subsidies from federal and/or local programs. These properties are:

1. Kalani Gardens in Mililani, Hawaii (Honolulu)
2. Studio 819 in Mountain View, California (San Jose, California)
3. Teale Pointe in Clark County, Washington (Portland, Oregon)

[1] https://mf.freddiemac.com/docs/Affordable_Housing_in_High_Opportunity_Areas.pdf
[2] This research project was performed in conjunction with two other case study reports: mixed-income properties in areas of concentrated poverty and affordable housing in high opportunity areas outlined in state QAPs.
[3] For more information: https://www.fhfa.gov/DataTools/Downloads/Documents/Enterprise-PUDB/DTS_Residential-Economic-Diversity-Areas/DTS-Residential-Economic-Diversity_High-Opportunity-Areas-revised.pdf

While local programs may differ, the concepts described here can be leveraged for other transactions across the country. We found from our analysis that Low-Income Housing Tax Credits (LIHTCs) and local financial support plays a vital role in the development or financing of the property to retain affordable to lower income tenants in high opportunity areas. The ability for lower-income tenants to have affordable housing in these areas provides them with economic and social benefits and advances the opportunity of all residents.

Case Study #1: Kalani Gardens

Property Overview

Buildable land is scarce in Hawaii and the high cost of development contributes to high housing costs across the state. Kalani Gardens is a 119-unit apartment in Mililani, which is just under 20 miles north of downtown Honolulu on the island of Oahu. The property operates with multiple layers of subsidy, including Low Income Housing Tax Credits (LIHTC), and the Department of Housing and Urban Development's (HUD) Section 8 and Section 236 subsidies. These subsidies allow rents at this property to be considerably lower than the surrounding area, providing much needed affordable housing to the area.

Exhibit 1: Property Characteristics

Geography	**State**	Hawaii
	MSA	Urban Honolulu, HI MSA
	County	Honolulu County
Property Details	**Style**	Walk-up
	Year Built	1970
	Number of Units	119
Ownership and Management	**Owner**	EAH Housing
	Manager	EAH Housing

Source: Freddie Mac Investment Brief

Source: Yardi

Kalani Gardens, constructed in 1970, consists of six walk-up style buildings with two or three stories, containing 88 two-bedroom units and 31 one-bedroom units. Property amenities include a business center, car wash area and off-street parking. Kalani Gardens also recently installed a solar photovoltaic (PV) system to significantly cut down on energy expenses. The PV system on Kalani Gardens has been estimated to generate $158,000 in energy benefit each year, which more than offsets the previous 12 months of electrical expense. The total cost of the system was approximately $1 million., However, after energy tax credits and deductions combined with the annual energy expense savings, the system is expected to pay for itself within two years.

Rents at Kalani Gardens are substantially lower than the prevailing market rents in the area due to a number of programs and subsidies. At the time of Freddie Mac underwriting in 2014, average rent on the property was $1,119. Per RealPage, average market rent for the area at that time was $1,836 – a difference of 64.1%. Average submarket rent was even higher at $2,060 (84.1% higher than Kalani Gardens).

RealPage tracks Kalani Gardens and shows that rents have not moved very much from the time of underwriting. In the third quarter of 2019, average rent at Kalani Gardens was $1,187, an increase of 6.1% since 2014. Meanwhile, submarket and market rents increased markedly since 2014, up 26.0% to $2,480, and 23.2% to $2,208 respectively.

The tenants of Kalani Gardens must meet certain income restrictions in order to rent at this property. For households containing three people, the income limit is $65,100 – substantially lower than the county's median family income of $99,000.[4] Based on the distribution of income in the area, we estimate that an income of $65,100 would represent the 35th percentile of income.[5]

Area's Rental Market and Affordability Concerns

Housing development faces many challenges in Hawaii, and as a result, affordable rental housing is tough to find. In a research study commissioned by the National Apartment Association and National Multifamily Housing Council,[6] Honolulu was ranked as the nation's most difficult city to create new apartment units. The lack of supply leads to expensive rental housing. Of the 151 markets that RealPage tracks, only eight metros have higher rents. Furthermore, in 2017, Hawaii had the second highest median rental burden among all states at 33.2% of renter households paying more than 30% of their income toward rent. Kalani Gardens' census tract had an even higher rate at 35.4%.

From 2013 to 2018, effective rent in Honolulu grew by 21.9%, slightly below the nation which experienced a 25.5% rent growth. However, from Exhibit 2, rent in the Outer Honolulu submarket is around 77% higher than the national average. The higher rents in the submarket compared with the lower rents offered at Kalani Gardens have resulted in a waitlist for new tenants, implying the high demand for affordable rent in the area. While vacancy rates at the submarket are volatile, Honolulu's vacancy rates in 2018 were almost identical to national trends, as seen below in Exhibit 2. Although rent growth in Honolulu came in slightly below the national growth rate, there is still a persistently wide disparity between metro rents and national rents.

Exhibit 2: Multifamily Rental Market Overview

	Submarket (Outer Honolulu)	Market (Urban Honolulu)	National
2013 Rent	$1,900	$1,734	$1,063
2018 Rent	$2,367	$2,114	$1,334
5-Year Rent Growth	24.6%	21.9%	25.5%
2013 Vacancy Rate	5.6%	5.0%	5.4%
2018 Vacancy Rate	5.5%	4.7%	4.6%
5-Year Vacancy Difference	-0.1%	-0.3%	-0.8%

Source: RealPage

[4] Based on Freddie Mac tabulations of Novogradac data: https://ric.novoco.com/tenant/rentincome/calculator/z1.jsp
[5] Percentile estimation is based on Freddie Mac tabulations of data from the Internal Revenue Service
[6] https://www.naahq.org/news-publications/listing-hardest-easiest-cities-adding-apartments

State and Local Actions to Support Affordable Rental Housing

The State of Hawaii recognizes the affordable housing crisis that has been affecting its residents for decades. A 2015 study projected that the state will need 64,693 housing units to meet demand for housing by 2025. Nearly 70% (43,828) of the units will be needed for low-income households earning 80% or less of area median income (AMI).[7] In 2016, the state passed legislation establishing an affordable rental housing goal and a Special Action Team to make recommendations on actions to promote affordable rental housing. The stated goal is to develop or vest the development of at least 22,500 affordable rental housing units, ready for occupancy between January 1, 2017 and December 31, 2026. That goal is to be met through conversions (non-affordable to affordable) or new development. A July 2018 report compiled by the Special Action Team[8] estimated that 25,847 (or 40%) of the nearly 65,000 housing units needed to satisfy the demand by 2025 would be required in Oahu, which encompasses the city and county of Honolulu. The report also presented a number of findings related to existing barriers to affordable housing development and provided recommendations for the state and specific localities.

The Hula Mae Multifamily[9] program promotes the rehabilitation or new development of rental housing projects through the issuance of tax-exempt bonds by the Hawaii Housing Finance & Development Corporation. These bonds provide interim or permanent financing at rates below market interest rates and are subject to a private activity volume cap. The units must remain affordable for the longer of 15 years or the term of the bond, and projects must set aside a minimum of:

- 20% of units earning less than 50% of AMI, or
- 40% of units earning less than 60% of AMI

In Honolulu, developments where at least 20% of rental units are reserved for low-income residents for at least 15 years pursuant to a regulatory agreement are exempt from property taxes. For purposes of these requirements, low-income residents are those earning no more than 80% of AMI.[10] In addition, Ordinance 19-8, introduced early this year, would establish a temporary program to allow for the construction of affordable rental housing by relaxing certain zoning and building code standards, and offering certain financial incentives.[11]

Property Financing

Hawaii has some unique obstacles to housing development that may be more severe than in other parts of the nation. These include extremely high construction costs, high land costs and a lack of infrastructure; the severity of these challenges is largely due to the island geography. The area also faces similar hurdles to the rest of the country, including lack of economic feasibility, NIMBYism, zoning and government delays and fees, along with environmental impacts and concerns.

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[7] The State Department of Business, Economic Development and Tourism, Measuring Housing Demand in Hawai‘i, 2015- 2025 study (Department of Business, Economic Development & Tourism, 2015)
[8] http://files.hawaii.gov/dbedt/op/spb/AffordableRentalHousingReport_10YearPlan.pdf
[9] https://dbedt.hawaii.gov/hhfdc/developers/hmmf_html/
[10] Revised Ordinances of Honolulu, Chapter 8-10.20 (Exemption- Low-income rental housing)
[11] Ordinance 19-8, Bill 7(2019), CD2,FD1 *available at* http://www4.honolulu.gov/docushare/dsweb/Get/Document-237616/DOC%20(27).pdf (current as of 11/8/2019)

In areas like Honolulu County, the extremely high costs to build and maintain units make constructing and running an affordable project economically infeasible with the limited cash flows generated. Some form of subsidy is necessary to make the project feasible.

Kalani Gardens has several layers of different subsidies to keep rents affordable, along with a permanent real estate tax abatement as long as the property maintains 20% of units affordable at 80% AMI. All the units at Kalani Gardens are restricted to tenants earning 30%, 50% and 60% of AMI due to a LIHTC regulatory agreement. The property also has a restriction from a Department of Housing and Urban Development (HUD) 236 loan for the remaining useful life of the property (but not less than 50 years) where 82 units are affordable at 50% of AMI, 13 units greater than 50% and up to 80% of AMI, and 22 units greater than 80% and up to 95% of AMI, with rent restricted to 25% of income. Furthermore, 24 units have project-based Section 8 restrictions through a Housing Assistance Payments (HAP) contract through 2044. A bond regulatory agreement requires 40% of units be rented to tenants at or below 60% AMI. The agreement lasts 15 years after 50% occupancy is achieved, until the bonds are no longer outstanding, or the HAP contract expires. At the time of financing the property was also planned to be renovated using 4% LIHTC. Among all the subsidies at different affordability levels, the property is required to meet the most restrictive rent levels of the subsidies.

In 2014, Kalani Gardens was purchased by EAH Housing's new tax credit partnership. EAH Housing is a non-profit corporation which develops, manages, and operates affordable housing for low-income families in California and Hawaii. The EAH partnership utilized a permanent loan as the primary funding source. The property value was estimated at $8,850,000, while the loan amount was for $6,548,000, which equated to a loan-to-value (LTV) ratio of 74.0%. Per unit, the loan amount was $55,025 and the price per unit was $74,370. The unit-level pricing of Kalani Garden was significantly below market rate transactions. In 2014 the median price per unit in Honolulu County was over $308,000 – more than four times higher than value of units at Kalani Gardens.

The significant price per unit difference between Kalani Gardens and market rate transactions is not surprising due to the rent restrictions on the property. A market rate property is free to set rents at whatever level the market will bear, while Kalani Gardens has restrictions on the rent increases based on Fair Market Rents set by HUD. These restrictions depress the unit price. The value of these units, however, is greater than the amount of rent they can generate based on their rent restrictions.

High Opportunity Characteristics of the Surrounding Area

The lack of affordable housing is a problem in many parts of the country but creating and maintaining the affordable rental housing stock in high-cost areas is particularly challenging. Typically, one of the key advantages of these high-cost areas is that they provide economic opportunity and mobility to their residents. The area around Kalani Gardens is no exception in terms of opportunity, but high housing costs limit the families that can take advantage of the opportunity. Kalani Gardens is a critical source of housing for families that would otherwise struggle to live in an area with high opportunity and economic mobility; without developments like Kalani Gardens, these families would have little opportunity to improve their economic standing.

According to GreatSchools.org[12], the Kalani Gardens school district is excellent. Kipapa Elementary school is located across the street from the development and scores an eight out of ten; the middle

[12] https://www.greatschools.org/

school also scores an eight out of ten. Mililani High School is rated a ten out of ten. Access to this school district gives the young residents of the apartment community an excellent chance to improve their economic situation later in life.

Kalani Gardens is located about 20 miles northwest of Honolulu in a valley that divides the island. The closest large-scale retail is the Town Center of Mililani, located within a mile of Kalani Gardens. It features a grocery store, Walmart, PetSmart, a drug store and several eateries. The area features many golf courses, hiking trails and parks, and a myriad of water sports are all within easy access to area residents. The development is 1 mile southwest of Highway H-2, providing easy access to Honolulu (20 miles) to the southeast, where most of the island's largest employers are located. Historic Pearl Harbor and the associated joint military base are located about 12 miles to the south of Kalani Gardens. Joint Base Pearl Harbor-Hickam has more than 19,000 active duty personnel and employs more than 10,000 civilians.[13] The Pearl Harbor Naval Shipyard is Hawaii's largest industrial employer with over 5,000 workers.[14]

Kalani Gardens is in a wealthy section of Hawaii. Income in Honolulu County is above the state average and considerably higher than the national average. Poverty is low, at only 9.1% (as seen in Exhibit 3) in the county and even lower at the census tract at 8.4%. Renter and owner income in Kalani Gardens' census tract are low compared with the surrounding county and the state but high compared with the national average.

Exhibit 3: Demographic Characteristics

	Tract	County	State	Nation
Population Density	8,249.1	1,648.5	221.4	90.9
Median Income	$69,338	$80,078	$74,923	$57,652
Median Income - Owner	$93,214	$104,759	$94,123	$73,252
Median Income - Renter	$45,313	$57,016	$54,216	$36,653
Poverty Rate	8.4%	9.1%	10.3%	14.6%
Renter Rate	39.7%	44.4%	41.9%	36.2%
Cost-Burdened Renter %	59.9%	58.0%	56.1%	50.6%
Unemployment Rate	4.9%	4.5%	4.9%	6.6%

Source: Freddie Mac Tabulations of 2017 5-Year American Community Survey

Per Moody's Analytics employment growth in Honolulu has been nearly flat over the past five years, growing by just 0.9%, well behind the national rate of 7.4%. Growth in the county since the financial crisis has been more impressive at 7.9% but still trailed the national average of 12.3%.

[13] https://www.cnic.navy.mil/regions/cnrh/installations/jb_pearl_harbor_hickam/about.html
[14] https://www.navsea.navy.mil/Home/Shipyards/PHNS-IMF/Careers/Pay-Benefits/

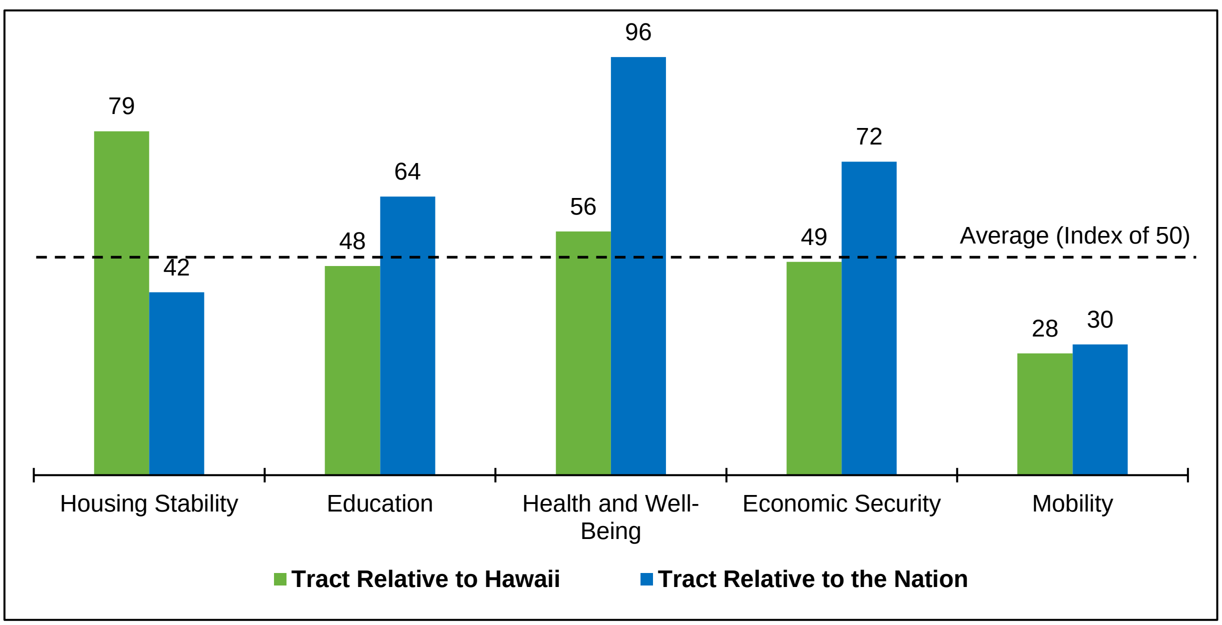
In addition to high income levels and a stable employment market, there are many other factors that determine high opportunity. Enterprise Community Partners (Enterprise), an organization that advocates and builds affordable housing for lower-income households, created Opportunity360 to assess areas of opportunity. Opportunity360 includes a tool that measures opportunity in census tracts across the country.

The tract that contains Kalani Gardens generally ranks high, especially in comparison to the nation. Exhibit 5 shows the scores of this tract in the five categories that Opportunity360 measures: housing stability, education, health and well-being, economic security, and mobility.

Exhibit 4: Map of the Area Surrounding Kalani Gardens

Source: Google Maps

Exhibit 5: Opportunity Indices for Kalani Gardens Census Tract



Source: Opportunity360

As seen in Exhibit 5, education, health and well-being, and economic security for the Kalani Gardens' tract are in line with the average for the State of Hawaii, while housing stability is well above the state average, and mobility is well below the average. The tract compares favorably with the nation in education, health and well-being, and economic security, while slightly lagging the national average for housing stability and well below for mobility. The low mobility numbers can be attributable to only 4% of commuters using public transportation, while 11% of commuters travel more than an hour each way to work.

Impact of Supporting Affordable Housing

Hawaii generally, and Honolulu County specifically, recognize that rents in the area are extremely high, due to high demand and limited supply, and subsequently low vacancy. Because of the high development costs in the area, developing unsubsidized affordable housing is rare, so conscious attempts to provide it are needed. Kalani Gardens was initially constructed utilizing a HUD 236 loan and LIHTC funding, along with an indefinite tax abatement as long as affordability restrictions are met. Due to the many subsidies in place at Kalani Gardens, which allows the property to operate at below-market rate rents, the tenants have access to safe, decent, affordable housing in an area that provides opportunity for economic advancement that most likely would not have been otherwise available.

Case Study #2: Studio 819 Apartments

Property Overview

Mountain View, California, in the heart of Silicon Valley, is at the center of the affordable housing crisis. Rents are high, and although incomes are generally high as well, those making lower incomes who work in the community have a hard time finding available housing that is affordable to them. Studio 819 is a new development that seeks to address this need.

Exhibit 6: Property Characteristics

Geography	**State**	California
	MSA	San Jose-Sunnyvale-Santa Clara, CA
	County	Santa Clara
Property Details	**Style**	Mid-rise
	Year Built	2015
	Number of Units	49
Ownership and Management	**Owner**	Eden Housing
	Manager	Eden Housing

Source: Freddie Mac Investment Brief

Mountain View sits between Palo Alto and Santa Clara in Silicon Valley, which is part of the San Jose metro area. Studio 819 is a 49-unit mid-rise apartment with a modern design built in 2015. The property was funded with a LIHTC subsidy and a soft debt loan from the city of Mountain View.

Studio 819 was developed by Eden Housing – one of California's oldest and most well-known nonprofit affordable housing developers. As the property's name suggests, every unit in the building is a studio except for one 1-bedroom unit that is occupied by the building manager. Each studio is 405 square feet, which is 22.9% smaller than the submarket studio average of 525 square feet (Reis). The property has an on-site laundry facility, a community room, a computer room and a bicycle storage area. The top floor contains a roof deck.

Source: Rent.com

Every studio unit on the property is restricted for occupancy by extremely low- and very low-income households. Occupancy is restricted based on a regulatory agreement recorded in 2013. The same agreement requires rents to be affordable to the following income brackets:

- Restricted to those earning 30% of AMI or below: 13 units
- Restricted to those earning 40% of AMI or below: 10 units
- Restricted to those earning 45% of AMI or below: 25 units

Studio 819 allows for small households to live in an expensive area for relatively little cost. In 2019, rent at Studio 819 ranged from $768 to $1,153.[15] During the same time, market rate rent for a studio in this submarket was $2,419.[16]

The tenants of Studio 819 must meet certain income restrictions in order to rent at this property. For households containing one person, the income limit ranges from $30,750 to $46,125 – substantially lower than the county's median family income of $131,400.[17] Based on the distribution of income in the area, we estimate that an income of $30,750 and $46,125 would represent the 16th and 23rd percentile of income, respectively.[18]

Area's Rental Market and Affordability Concerns

The property sits in the middle of Silicon Valley, an area known around the world as a center for technological innovation. The area is also known for having exorbitantly high housing costs.[19,20] Because of the high-cost nature, constructing and operating affordable housing in this region is tougher than in most parts of the country. When Studio 819 was developed, it cost roughly $360,000 per unit.[21] A potential 2019 development being considered in the same area is estimated to cost nearly double that amount.[22] The primary reason is that land prices in Santa Clara have increased tremendously; from 2012 to 2017, land values grew by 98.4%. An acre of residential land in Santa Clara was valued at about $5.2 million in 2017. This puts Santa Clara in the top 1% of all counties in terms of land prices.[23]

In a report released in April 2018, the California Housing Partnership Corporation, citing work from the National Low Income Housing Council, found that Santa Clara's lowest-income renters spend 62% of their income on rent payments. The report also concluded that Santa Clara needs to build more than 58,000 affordable rental units for supply to meet demand.[24]

The San Jose metro area has seen tremendous rent growth in the past five years, as seen in Exhibit 7. From 2013 to 2018, rents grew from $2,078 to $2,803 – a change of 34.9%. The submarket that contains

[15] Based on Freddie Mac tabulations of Novogradac data: https://ric.novoco.com/tenant/rentincome/calculator/z1.jsp
[16] Reis
[17] Based on Freddie Mac tabulations of Novogradac data: https://ric.novoco.com/tenant/rentincome/calculator/z1.jsp
[18] Percentile estimation is based on Freddie Mac tabulations of data from the Internal Revenue Service
[19] https://www.mercurynews.com/2018/09/06/san-jose-tops-list-for-least-affordable-housing-in-u-s/
[20] https://mf.freddiemac.com/docs/rental_burden_by_metro.pdf
[21] Based on Studio 819's Sources and Uses documentation
[22] https://www.mv-voice.com/news/2019/05/02/the-high-price-of-affordable-housing
[23] From tabulations of FHFA data: https://www.fhfa.gov/PolicyProgramsResearch/Research/Pages/wp1901.aspx
[24] https://1p08d91kd0c03rlxhmhtydpr-wpengine.netdna-ssl.com/wp-content/uploads/2018/04/Santa-Clara-2018-HNR.pdf

Studio 819 grew by 33.1%, from $2,495 to $3,321. To put this in perspective, the national average rent growth over this period was only 25.5%.

In 2016, the residents of Mountain View responded to the high rent growth by voting to adopt the Community Stabilization and Fair Rent Act, which regulates permissible rent increases and requires cause for eviction of a tenant. For apartments built between 1995 and 2017, the rent regulation does not apply; however, new developments are subject to both requirements. Interestingly, the findings of the Act reflect that just the consideration of rent regulation led to increases in rents, as landlords anticipated future restriction.[25] Recently, the State of California enacted legislation that would similarly restrict rent growth and require cause for eviction, which may offset the local impact on Mountain View of its earlier regulation.[26]

Exhibit 7: Multifamily Rental Market Overview

	Submarket (Mountain View - Palo Alto)	Market (San Jose - Sunnyvale - Santa Clara)	National
2013 Rent	$2,495	$2,078	$1,063
2018 Rent	$3,321	$2,803	$1,334
5-Year Rent Growth	33.1%	34.9%	25.5%
2013 Vacancy Rate	4.1%	3.8%	5.4%
2018 Vacancy Rate	4.6%	3.8%	4.6%
5-Year Vacancy Difference	0.5%	0.0%	-0.8%

Source: RealPage

The area's economic opportunities are a driver behind the above-average rent performance. Wages in Santa Clara are roughly 85% higher than elsewhere in the country and they are growing faster too. From 2009 through 2017 (the most recent year of ACS 5-year income data), wages in the United States grew by 12.1%. Meanwhile, wages in Santa Clara grew by 24.8%.

State and Local Actions to Support Affordable Rental Housing

Even though incomes are growing quickly, Exhibit 7 shows that rents are growing faster, resulting in rental affordability worsening over time. Mountain View acknowledges the affordability issues that many households in the area face and has taken steps to combat the problem. Increasing affordable housing has been a stated major goal and priority of the City Council since 2015.[27]

25 https://library.municode.com/ca/mountain_view/codes/code_of_ordinances?nodeId=PTITHCH_ARTXVIICOSTFAREAC_S1701FI

26 https://www.gov.ca.gov/2019/10/08/on-statewide-rent-housing-tour-governor-gavin-newsom-signs-nations-strongest-statewide-renter-protection-legislation/

27 https://www.mountainview.gov/council/goals.asp

There are two primary ways that the city provides affordable housing: subsidies and the Below Market Rent (BMR) program. The city, along with other investors, provides funding to subsidize the rents, making them affordable to extremely low-income and very low-income households. As of 2019, there are 13 subsidized properties supporting about 1,200 apartment units, including Studio 819, and all of them have a closed waitlist (as of January 2019).[28]

The second way of providing affordable housing is through the BMR program. Under this program, at least 15% of units in new, market rate properties are set aside as BMR units or a fee is paid by the developer in lieu of the set aside at a rate greater than the cost of developing the BMR units.[29] BMR units must be affordable in perpetuity to a minimum of two income levels ranging from 50% to 120% of AMI and must average to no more than 65% of AMI.[30] The set aside rate used to be 10% but was increased to the current rate of 15% as part of a two-phase initiative begun in late 2017. The desire to increase this rate and recency of these changes highlight the city's ongoing struggle to keep up with demand for affordable housing.

Property Financing

Studio 819 had two primary funding sources when it was originally constructed in 2015. The first was $9 million in soft debt funding from the city of Mountain View. The second was tax credit equity from federal and state sources, which covered $8.2 million of the development cost. At the time of development, the LIHTC program requires that properties set aside either 40% of units to be affordable at 60% AMI or 20% of units to be affordable at 50% AMI. Property operators will often set aside a higher percentage of units, and at lower AMI levels, to be more competitive in obtaining municipal or state funding, or because they are mission-focused. As mentioned earlier, Studio 819 sets aside all their studio apartments at or below 45% of AMI.

Wells Fargo provided a $6.2 million construction loan that was converted into a permanent loan of $475,000 in 2017 by the California Community Reinvestment Corporation (CCRC), a leading Community Development Financial Institution (CDFI). CCRC plays an important role in providing permanent debt for affordable housing projects across California. Since their inception in 1989, they have approved over $1.5 billion in loans for affordable housing, financing more than 42,000 rental homes for individuals and families earning 60% or less of AMI. Providing this access to capital allows individuals to live, work and raise their families in communities throughout California, creating a more economically diverse and stable statewide economy.

The $475,000 permanent loan was crucial for the operation of Studio 819. However, finding a traditional lender to support such a small loan amount is often difficult. Instead of a traditional lender, Eden Housing relied on CCRC for the loan's origination. CCRC has a unique business model among CDFIs of providing small, permanent take-out loans to affordable multifamily properties and recycling capital through securitizations. The permanent loan on Studio 819 is important because it requires only a small monthly debt service payment, which enables rents to remain low and the deal to work economically. CCRC's involvement in Studio 819 exemplifies the crucial role that CDFIs play in the development of affordable housing across the country in cases where nontraditional financing is needed.

[28] https://www.mountainview.gov/civicax/filebank/blobdload.aspx?BlobID=26650
[29] https://www.mountainview.gov/documents/BMR%20Phase%202%20Guidelines%20-%20FINAL%20CLEAN%20COPY.pdf.
[30] http://laserfiche.mountainview.gov/WebLink/0/doc/228170/Page1.aspx

In 2019, Freddie Mac securitized CCRC's loan on Studio 819 along with 86 other loans as part of a Q-Deal. The Q-Deal program allowed CCRC to access Freddie Mac securities and the capital markets network. More specifically, CCRC exchanged a pool of loans, which included Studio 819, for Freddie Mac guaranteed Class A certificates and unguaranteed Class B certificates. The Class A certificates were sold into the market by Wells Fargo, and the cash proceeds of the sale were returned to CCRC. The Q-Deal execution with Freddie Mac allowed CCRC to recycle capital and continue its lending to create and preserve more affordable housing.

High Opportunity Characteristics of the Surrounding Area

Mountain View is considered a very desirable area to live. Part of the reason for this is the tremendous job opportunities that the area offers. However, while the influx of new businesses and high-paying jobs have been a boon for the local economy, it has also led to housing struggles. The affordable rent levels of Studio 819 allow for lower-income workers to live within their means in Mountain View despite the high housing costs that are typical of this area.

The economic and social advantages of living in Mountain View are of great value to all residents and without properties like Studio 819, many lower-income renters could potentially find job opportunities in Mountain View but live elsewhere to avoid high housing costs, losing out on the local area advantages. In addition, living in more distant, more affordable towns with less opportunity would entail very long commute times in an area that is known for traffic congestion. Properties like Studio 819 allow for renters to live comfortably in an area with close access to employment centers and great public amenities.

The area surrounding Studio 819 exemplifies a high opportunity area. Santa Clara is one of the highest earning counties in the entire country. The median household income of $106,761 ranks 11th in the nation and first in California. The county's renter income of $77,588 is more than double the national renter median and is even higher than owner income nationally (renter income is normally about half as much as owner income).

Households in Studio 819's tract earn even more than the county average, as seen in Exhibit 8. Median income exceeds the nation by about $65,000. Renter income exceeds $100,000 which is very rare, occurring in fewer than 3% of tracts nationwide.

Exhibit 8: Demographic Characteristics

	Tract	County	State	Nation
Population Density	5,744.3	1,481.3	250.2	90.9
Median Income	$122,679	$106,761	$67,169	$57,652
Median Income - Owner	$142,019	$135,113	$90,735	$73,252
Median Income - Renter	$101,667	$77,588	$46,062	$36,653
Poverty Rate	5.1%	8.6%	15.1%	14.6%
Renter Rate	56.4%	43.1%	45.5%	36.2%
Cost-Burdened Renter %	46.1%	47.7%	56.0%	50.6%
Unemployment Rate	2.2%	5.7%	7.7%	6.6%

Source: Freddie Mac Tabulations of 2017 5-Year American Community Survey

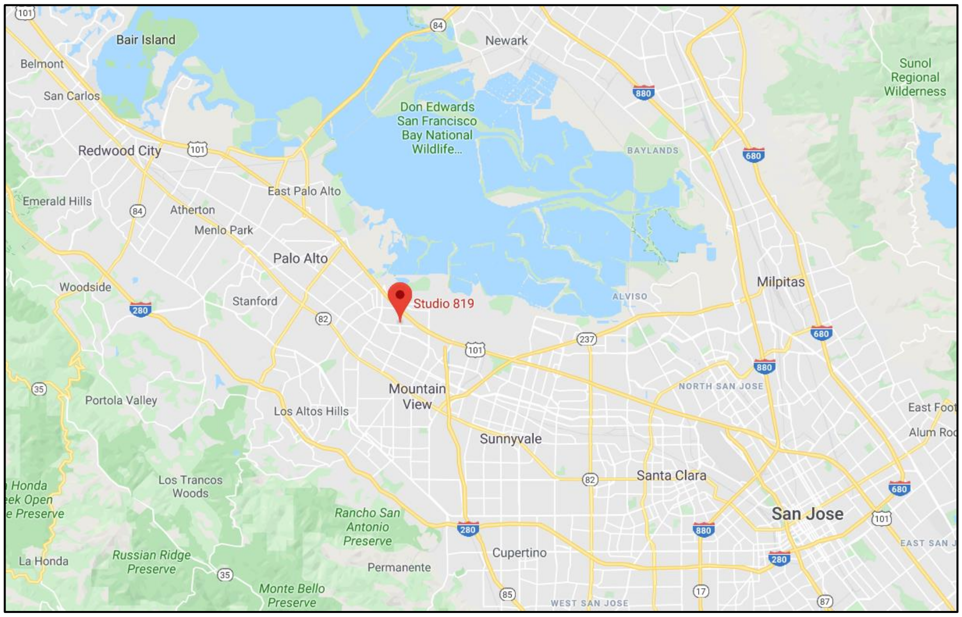
Although the wages are very high in this area, especially for renters, rents are also very high, which still makes housing a burden for a large percentage of the population. Per RealPage, the average rent in 2017 in the Mountain View–Palo Alto submarket was $3,184. Using the renter income in Studio 819's tract, the monthly income-derived rent amount is $2,542, assuming 30% of income is spent on housing. This suggests, a household making the median renter income still faces high housing costs. At the county level, renter incomes are far less than Studio 819's tract so most renters in the area would be even more rent burdened. In addition, the occupants of Studio 819 will have an income that is less than half of the tract median.

High income is driven by the vast number of high-quality employment opportunity that exist in the area. Nearly a fifth of all employed people in the city work for Google,[31] which is headquartered in Mountain View only a few blocks away from Studio 819. Other large employers include Symantec, Microsoft and LinkedIn. Prominent employers outside of the city limits include Apple, Stanford University and the county of Santa Clara.

The employment base in the county of Santa Clara grew by 10.1% in the past five years, which beat the national rate of 7.4%. Growth in Santa Clara since the financial crisis (2009) has been much more impressive at 32.1%, compared with 12.3% for the nation.

[31] https://www.mountainview.gov/civicax/filebank/blobdload.aspx?BlobID=27959

Exhibit 9: Map of the Area Surrounding Studio 819



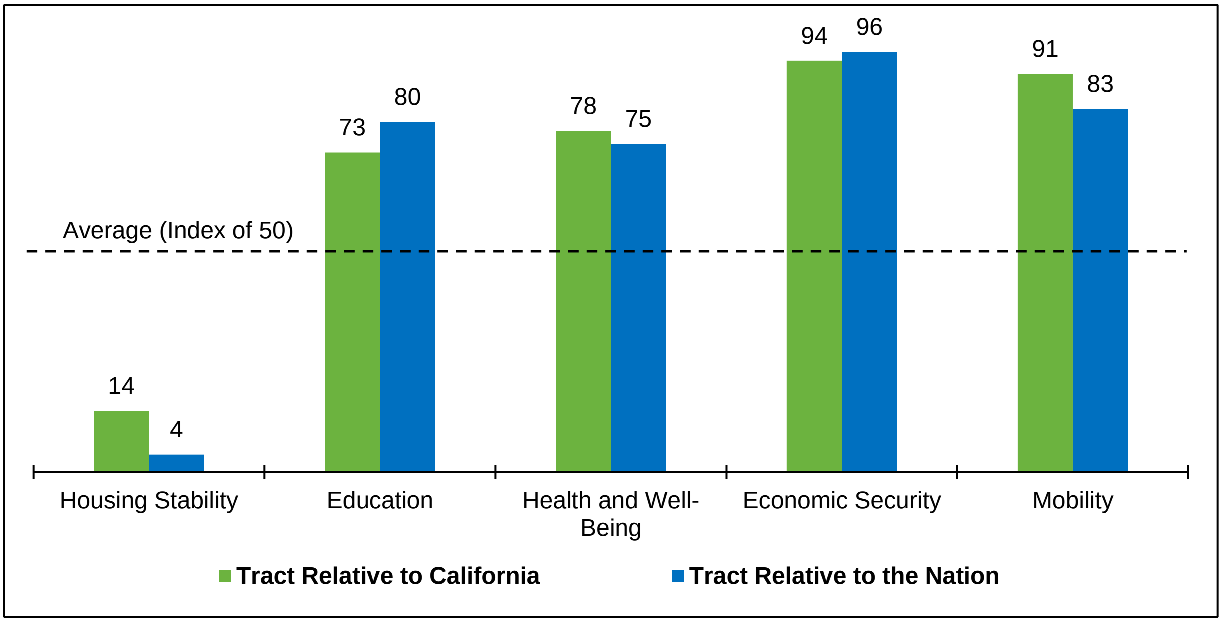
Source: Google Maps

Studio 819 is just over a 2 mile car ride to the nearest Caltrain station, a commuter rail running from the north end of San Francisco to the southern part of Santa Clara.[32] In addition, Studio 819 is two blocks away from the Mountain View Community Shuttle, a free service that provides transportation around Mountain View.[33] There is also another nearby shuttle service, the MVgo, which serves a similar purpose.[34]

In addition to the employment market and transit system, there are many other factors that determine high opportunity. Using Enterprise's Opportunity360 tool, we find that the tract that contains Studio 819 generally ranks very high. Exhibit 10 shows the scores of this tract in the five categories that Opportunity360 measures: housing stability, education, health and well-being, economic security, and mobility.

[32] http://www.caltrain.com/stations/systemmap.html
[33] https://mvcs.tripshot.com/g/tmsSystemMap/TMSSystemMap.html
[34] https://www.mvgo.org/all-routes.html

Exhibit 10: Opportunity Indices for Studio 819's Census Tract



Source: Opportunity360

As seen in Exhibit 10, four of the five categories are well above the state and national average. Noticeably, housing stability ranks very low. The area surrounding Studio 819 has low homeownership, extremely high home values and rents that are more than double the national average. In addition, 8.1% of occupied units are either crowded or overcrowded, which compares with 3.4% for the nation and only 0.1% for the metro.[35]

The root cause of low housing stability is typically an undersupply of housing. On the rental side, increased supply, especially in the affordable segment of the market, will lower rent levels and help to alleviate housing burden for renters in the area. The tract's low marks for housing stability simply indicate that more housing support is needed, and Studio 819 is helping to fill the void.

Impact of Supporting Affordable Housing

California is well-known for having a severe shortage of affordable housing and in areas like Mountain View the issue is more pronounced. Mountain View and the surrounding area is a very desirable place to live due to its strong employment base, relatively low crime rate and socially active community. However, due to the high development costs in the area, developing affordable housing without subsidies is very difficult, so deliberate steps to provide it are often necessary. Studio 819 required funding from many sources for the construction and sustained operation of the property, including federal tax credits, soft debt from the city of Mountain View and a loan from a CDFI. As a result, many of the property's tenants have access to affordable housing that they may not have otherwise had.

[35] https://www.policymap.com/report_widget?pid=184039&type=op&area=predefined&sid=2010

Case Study #3: Teal Pointe

Property Overview

The area in and around Portland, Oregon is well-known for its natural beauty and unique culture. However, the area is also known for an increasing shortage of affordable units needed to serve its population. In a recent study[36] that we conducted on rising unaffordability in metro areas across the country, we found that the percentage of multifamily rental units in Portland that are affordable to very low-income households dropped by 46.8 percentage points from 2010 to 2017– the largest drop among the nation's Top 50 metros areas. The construction and preservation of affordable housing is becoming increasingly important in this region and where properties like Teal Pointe are instrumental in alleviating the affordability crisis.

Teal Pointe is a 120-unit garden style apartment in Clark County, Washington, located 14 miles north of downtown Portland. The property operates with a LIHTC subsidy and has the distinction of being the first Targeted Affordable Housing property to receive mezzanine financing from Freddie Mac.

Exhibit 11: Property Characteristics

Geography	**State**	Washington
	MSA	Portland-Vancouver-Hillsboro, OR-WA
	County	Clark County
Property Details	**Style**	Garden
	Year Built/Reno.	1985/2003
	Number of Units	120
Ownership and Management	**Owner**	Wishrock & Ray
	Manager	Guardian Real Estate Services LLC

Source: Freddie Mac Investment Brief

Teal Pointe consists of eight, two-story apartment buildings that contain an almost equal mix of one-bedroom and two-bedroom units. The complex was built in 1985 and was renovated in 2003 at a cost of nearly $1.5 million. The community includes many amenities, including a fitness center, a pool and a dog park.

Every unit on the property has restricted rents; per the LIHTC restriction, rents are affordable to households making 60% of the AMI. At the time of underwriting in late 2018, the average rent on the property was $873, which is 29.7% less than the submarket average of $1,242, per RealPage.

The tenants of Teal Pointe must meet certain income restrictions in order to rent at this property. For households containing three people, the income limit is $47,520 – substantially lower than the county's median family income of $87,900.[37] Based on the distribution of income in the area, we

Source: ApartmentFinder.com

[36] https://mf.freddiemac.com/docs/diminishing_affordability_inescapable.pdf
[37] Based on Freddie Mac tabulations of Novogradac data: https://ric.novoco.com/tenant/rentincome/calculator/z1.jsp

estimate that an income of $47,520 would represent the 30th percentile of income.[38]

Wishrock & Ray acquired Teal Pointe in part because it was coming to the end of its LIHTC compliance period and could have been at risk of conversion to market rate had the qualified contract process been pursued. They also appreciated that the property itself was well-maintained, which allowed them to focus their efforts on providing social services via The Opportunity Council, a Washington-based nonprofit, to the tenants at the property – services that were not previously available.

Area's Rental Market and Affordability Concerns

Teal Pointe is a critical source of affordable housing for lower-income tenants since Clark County has very little affordable rental stock. While the median percentage of income that is spent on rent in Clark County does not differ significantly from the nation (29.6% vs. 30.3%), the tract-level rent burden is eight percentage points higher than the national average at 38.3%. In total, 61.9% of households in Teal Pointe's tract spend at least 30% of their income on rent.

The area has seen tremendous rent growth in the past five years. In the Vancouver, Washington submarket, which contains Clark County, effective rent in 2013 was $854; by 2018, this jumped all the way to $1,242 – a change of 45.4%. To put this in perspective, the national average rent growth over this period was only 25.5%. During the same period, the vacancy rate in Vancouver remained essentially flat but was well below the national average in both 2013 and 2018. RealPage reports that in 2018, only 3.4% units in the submarket were vacant, which is much lower than the national average of 4.6%. Persistently low vacancy leads to faster rent growth and has resulted in a shortfall of affordable housing units in this area. Low vacancy and high rent growth are also indicative of a desirable area that provides opportunity and a higher standard of living for its residents.

Exhibit 12: Multifamily Rental Market Overview

	Submarket (Vancouver)	Market (Portland - Vancouver - Hillsboro)	National
2013 Rent	$854	$966	$1,063
2018 Rent	$1,242	$1,344	$1,334
5-Year Rent Growth	45.4%	39.1%	25.5%
2013 Vacancy Rate	3.5%	3.8%	5.4%
2018 Vacancy Rate	3.4%	4.4%	4.6%
5-Year Vacancy Difference	-0.1%	0.5%	-0.8%

Source: RealPage

[38] Percentile estimation is based on Freddie Mac tabulations of data from the Internal Revenue Service

State and Local Actions to Support Affordable Rental Housing

The massive increase in rents prompts the need for community action to address the growing unaffordability issues. The Vancouver Housing Authority (VHA) is the chief provider of affordable housing in Clark County. The organization has provided subsidized housing for roughly 6,800 people through subsidized rental properties and HUD Section 8 vouchers. The VHA also provides more than 1,600 unsubsidized apartment units to families earning below 80% of AMI. These rental units are meant for lower-income families that either do not qualify for subsidized housing or are waiting for a subsidized unit to become available. The organization has been nationally recognized as an innovator in affordable housing.[39]

The VHA is not the only organization that provides housing assistance in Clark County – the City of Vancouver has its own affordable housing initiatives. However, despite having a Vancouver address, Teal Pointe is actually outside of the city limits of Vancouver and therefore would not be eligible for any type of funding provided by the City of Vancouver. Studying the local policy initiatives of Vancouver, the nearest city to Teal Pointe, is helpful in understanding community actions aimed at addressing the shortage of affordable housing throughout the region.

The City of Vancouver acknowledges the shortage of affordable units in the area and has taken steps to address the need for affordable housing. In 2015, the City of Vancouver convened a 21-member Affordable Housing Task Force in response to Vancouver's extremely low vacancy rate, rapidly increasing rents and recent mass housing displacement events. The task force recommended to expand the supply of housing in Vancouver, particularly income-based affordable housing. In 2016, Vancouver voters approved a ballot initiative creating a $42 million Affordable Housing Fund to serve households making 50% of AMI. So far, this fund has helped hundreds of low-income households find housing within their budget. The funds are used for preserving or constructing long-term affordable housing, sheltering the homeless and providing rental assistance to help households avoid eviction.[40,41]

Other funding sources and incentives for the development of affordable housing include sources of soft debt, namely Federal HOME Investment Partnerships and Community Development Block Grants (CDBG). These two federal grant programs provide funding that is allocated according to state and local program priorities. The City of Vancouver's current CDBG priorities include: revitalizing eligible neighborhoods, providing services to low- to moderate-income persons, upgrading public facilities to provide Americans with Disability Act (ADA) compliance, and providing affordable housing to low- and moderate- income citizens. Tax exemptions are also available for multifamily developments that provide housing to low-income households in specific, high-need areas of the city: the Vancouver City Center and the Fourth Plain corridor. In addition, a portion of park and traffic impact fees may be waived for properties that provide units that are affordable to households making at or below 80% AMI.[42]

[39] https://vhausa.org/about-vha/about-vha
[40] https://www.cityofvancouver.us/ced/page/affordable-housing-task-force
[41] https://www.cityofvancouver.us/citycouncil/page/ordinances-protecting-vulnerable-renters#Rent
[42] https://www.cityofvancouver.us/ced/page/affordable-housing

Property Financing

Teal Pointe received LIHTC funding about 15 years ago. The rent restrictions are now under an extended use agreement that goes until 2042, meaning that the units must stay within the affordability limits set by the program until that time.

In 2018, Teal Pointe was acquired by Wishrock & Ray LLC, who used a 12-year, first lien loan as the primary funding source. In addition to this loan, Teal Pointe also received $1,082,500 in mezzanine funding from Freddie Mac, closing a gap that would have typically been filled by local public subsidy if such a subsidy were available. The mezzanine loan included Freddie Mac's Preservation of Affordable Rents Covenant, which in this case, where rents were already restricted,[43] acted to (1) ensure that the borrower would not submit a qualified contract request which could result in the early termination of the LIHTC restrictions, and to (2) encourage continued compliance by the borrower with such restrictions through the imposition of monetary penalties for non-compliance. This combination of funds enabled the borrower to plan for a new tax credit syndication at the end of the loan term that would extend affordability further into the future.

The first lien loan amount was $8,046,000 and the property value was estimated at $10,825,000, which equates to a loan-to-value (LTV) of 74.3%. Based on the property value from 2018, the price per unit is $90,208. In comparison, the median price per unit in the Portland area was $179,012 – 98.4% higher than the price per unit for Teal Pointe.

Similar with the other two case studies, the unit-level pricing of Teal Pointe is dramatically below prevailing market rates but is not surprising given the property's rent restrictions. The maximum rent that Teal Pointe can charge is established by HUD, based on incomes and not market rents.

As stated earlier, Teal Pointe was acquired by Wishrock & Ray LLC when it was nearing the end of its LIHTC compliance period. Through the use of a qualified contract, the property could have been converted to market rate, which could have caused rents to increase dramatically and then property valuation would have increased in tandem. The increase in rents would have displaced some of the lower-income tenants or forced them to pay more toward rent while sacrificing other necessities. However, despite the lucrative alternative of converting to market rate, the LIHTC restriction remained in place, thus ensuring that the affordability of the units was preserved. Mezzanine debt from Freddie Mac offered the borrower favorable financing which partially mitigated the lower net operating income from the below market rate rents. Otherwise, with higher financing costs, rental income may not be able to cover operating and financing expenses and could result in higher rents.

High Opportunity Characteristics of the Surrounding Area

The area surrounding Teal Pointe is relatively wealthy. Clark County has income levels that are comparable to the state average and considerably higher than the national average. Poverty is low at only 10.3% (as seen in Exhibit 13) compared with the national rate of 14.6%. In the past five years (2014-2019), total employment in Clark County grew by 15.7%, well above the national rate of 7.5%.

[43] The property is subject to two regulatory agreements: one that relates to an award of LIHTCs by the Washington State Housing Finance Committee and one from the Housing Authority of the City of Vancouver (which is not more restrictive than the LIHTC agreement).

Interestingly, the census tract where Teal Pointe is located has comparatively high poverty and low income. Exhibit 13 shows that the poverty rate in this tract is 21.6%, which is atypical of a high opportunity area since low poverty is typically one of the defining characteristics of high opportunity. Owner households earn considerably more than the national average, but renter income and overall income fall short of the national average.

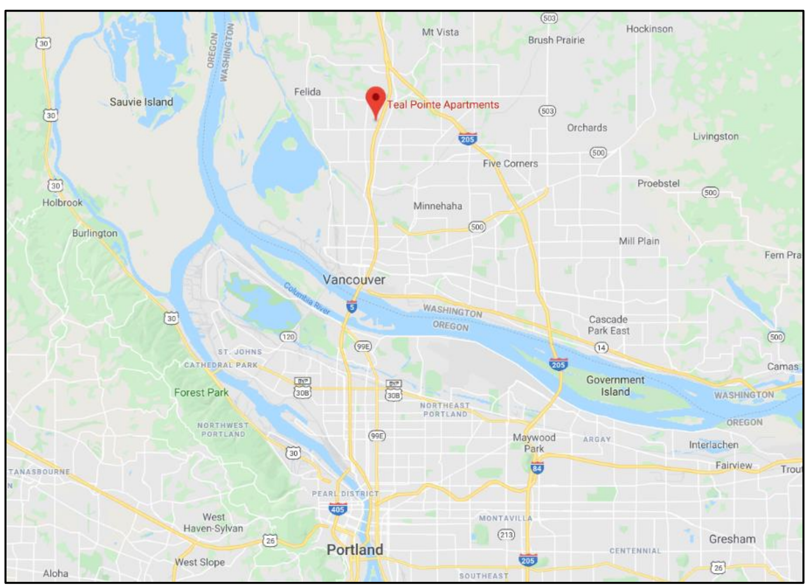
Exhibit 13: Demographic Characteristics

	Tract	County	State	Nation
Population Density	4,075.5	727.3	107.9	90.9
Median Income	$52,160	$67,832	$66,174	$57,652
Median Income - Owner	$85,153	$83,278	$83,343	$73,252
Median Income - Renter	$25,845	$43,485	$43,114	$36,653
Poverty Rate	21.6%	10.3%	12.2%	14.6%
Renter Rate	42.0%	34.2%	37.3%	36.2%
Cost-Burdened Renter %	61.9%	48.9%	48.9%	50.6%
Unemployment Rate	7.8%	6.2%	6.0%	6.6%

Source: Freddie Mac Tabulations of 2017 5-Year American Community Survey

However, upon further analysis we find that this tract is surrounded by areas that have much higher incomes. The four census tracts that surround the property have an average income of $78,706 – 36.5% higher than the national average. In addition, the average poverty rate of these tracts is 5.1%, which is more than four times lower than the property's census tract and almost three times lower than the national average. This suggests that this tract is an anomaly and is not representative of the opportunity that exists in this area.

Exhibit 14: Map of the Area Surrounding Teal Pointe



Source: Google Maps

Teal Pointe is located right next to Interstate 5 and is only minutes away from several shopping centers. The property is also only a few miles from the historic Vancouver Waterfront area, a mixed-use development that has recently received a significant amount of funding for further development. The area contains residential, office, retail spaces and fine dining in a 32-acre public space.[44] It is also near the Vancouver Waterfront Park, which is a 7.3-acre community park containing walking paths, a playground and open lawn areas.[45] Development activity on the Waterfront is expected to continue for at least the next few years.[46]

Clark County has a well-developed public transportation system. C-Tran operates buses throughout the county, and the I-5 Express bus line is only a few minutes' walk from Teal Pointe and brings travelers to downtown Portland.

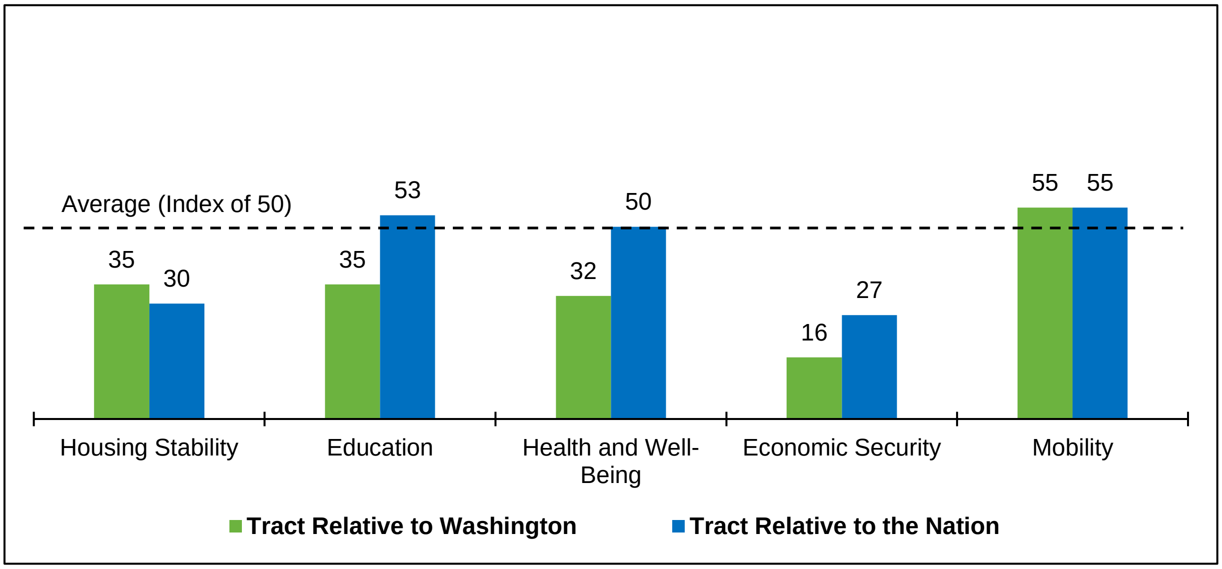
The economy of the Portland metro area is very robust. The employment mix is very diverse, the workforce is highly educated, and population growth has been strong in recent years. The metro area has a higher than average growth in gross metro product, which has translated into high household income growth. Part of its recent economic success stems from its high concentration of technology companies, which has earned the area the nickname of "Silicon Forest." The broader Portland area is very active in tech and business services.[47] Some of the largest employers in the metro include Intel, Nike and Boeing.

In nearby Vancouver, education and health care are two of the largest industries; of the Top five employers in the city, two are school districts and two are in the health care industry. The largest employer in the area is PeaceHealth Southwest Medical Center, which employed nearly 4,500 people in 2017.[48]

Exhibit 15 shows the scores of Teal Pointe's tract in the five categories that Enterprise's Opportunity360 measures: housing stability, education, health and well-being, economic security, and mobility. The scores are quite low, which is unusual for a high opportunity area.

[44] https://thewaterfrontvancouverusa.com/
[45] https://www.cityofvancouver.us/parksrec/page/vancouver-waterfront-park
[46] https://thewaterfrontvancouverusa.com/TheWaterfront-Vancouver-USA-Book.pdf
[47] Information came from metro reports compiled and produced by RealPage
[48] https://www.cityofvancouver.us/sites/default/files/fileattachments/financial_and_management_services/page/1060/2017_cafr_for_cov_web_page.pdf

Exhibit 15: Opportunity Indices for Teal Pointe's Census Tract



Source: Opportunity360

Although Teal Pointe's census tract may not appear to embody the traits of a high opportunity area by the mediocre scores shown in Exhibit 15, this is based only on the criteria used by Opportunity360. The concept of "high opportunity" is difficult to define. The Opportunity360 and Duty to Serve classifications rely on different criteria, which can result in inconsistent measurements of opportunity. Notably, in the case of Teal Pointe, the four bordering tracts have significantly higher scores according to Opportunity360. For example, their average economic security score relative to the nation is 70 – more than two and a half times greater than that of Teal Pointe's tract. Accordingly, both Duty to Serve measures and the Opportunity360 tool recognize that the general area is one of opportunity.

Impact of Supporting Affordable Housing

Rents in Clark County are abnormally high, driven by high demand and subsequent low vacancy. Teal Pointe was financed using LIHTC and low-cost permanent debt. Due to the high development costs in the area, developing affordable housing without subsidies is very difficult so deliberate attempts to provide it are often necessary. In the case of Teal Pointe, LIHTC equity and below market-rate mezzanine debt were necessary for the construction and sustained operation of the property, and as a result, many of the property's tenants have access to affordable housing that they may not have otherwise had. The ability to finance Teal Pointe without city subsidy enabled Clark County to deploy its subsidy dollars toward additional affordable housing development, resulting in more support for low-income families.

Conclusion

We set out to investigate how affordable properties in high opportunity areas attempt to create more economic diversity that will advance the opportunity of all residents. The three properties highlighted here provide affordable housing in areas that are classified as difficult to develop and were made possible with the use of a variety of subsidies as well as debt provided by Freddie Mac. The subsidies discussed here included soft funds, public subsidies, and state and local support, which provided necessary funding for the properties to operate at below-market rent levels. Our three case studies in this paper are replicable financing approaches with concepts that can be used across the country in other transactions in similar high opportunity areas.