

Low-Income Rental Housing and the Welfare Exemption

Introduction

Housing is significantly more expensive in California than in the nation as a whole. In fact, housing prices in California are more than double the national average, and median monthly rents are about 50 percent higher than the national average.¹

California's high housing costs have a broad range of effects on all Californians, but they have a particularly negative impact on the development of affordable housing for low-income households—more than 1.5 million of the state's lowest income households lack access to affordable housing.² The Welfare Exemption is an important element of a multi-faceted effort to mitigate the effects of California's affordable housing crisis.

Welfare Exemption

In general, the Welfare Exemption is a property tax exemption for property (1) used exclusively for religious, hospital, scientific or charitable purposes, and (2) owned or held in trust by nonprofit organizations operating for those purposes. This exemption is co-administered by the Board of Equalization (BOE) and the state's 58 county assessors. The BOE determines whether the organization is eligible to receive the exemption, and the county assessor determines whether the use of the property is eligible for exemption.

Section 214 of the Revenue and Taxation Code sets forth the many requirements and provisions of the Welfare Exemption. Section 214(g) provides exemption for certain property used exclusively for low-income rental housing by households meeting certain income limits. In most cases, these properties are restricted by a regulatory agreement or deed restriction designating that a minimum number of units must be rented to qualifying households at certain rent levels. The qualifying claimant (property owner and operator) must receive low-income housing tax

¹ "California's High Housing Costs: Causes and Consequences", Legislative Analyst's Office, March 2015
<http://lao.ca.gov/Publications/Detail/3214>

² "Update on California's Affordable Housing Crisis: The Critical Role of Housing Access and Affordability in Reducing Poverty", California Housing Partnership Corporation, April 2015
<http://www.chpc.net/dnld/2015StatewideHousingNeedReportFINAL.pdf>

credits or government financing for the particular property.³ Low-income housing properties that have some units not used for low income households are eligible for partial exemption.

Tax Credits and Government Financing as Funding Sources

Developers of market-rate housing evaluate prospective projects based on anticipated return of investment from market-level rents, tax benefits, and projected resale values. By contrast, developers of affordable low-income housing must evaluate the rents their target tenant populations can afford, and then rely on a potpourri of federal, state, and local government sources of funding to fill the "gap."

The recent elimination of redevelopment agencies in California has impacted the funding of affordable rental housing. The winding down of the last low-income housing bond issue approved by voter initiative has further impacted funding availability.

Thus, funding affordable low-income housing remains a significant challenge in California. The high costs of constructing housing in the state were documented in a report jointly released by the four state housing agencies that administer most funding sources.⁴ These agencies, discussed briefly below, still provide several sources of funding for California projects that may be eligible for the Welfare Exemption.

California Tax Credit Allocation Committee: *Low-Income Housing Tax Credits*

The Low-Income Housing Tax Credit (LIHTC) program provides federal and state tax credits to developers of affordable rental housing. The tax credits are provided during the first 10 years of a minimum 30-year compliance period during which rent and income restrictions apply. The LIHTC program was established by federal law, but allocation of credits and program administration is delegated to the states. In California, the administering agency is the California Tax Credit Allocation Committee (CTCAC), which operates as an adjunct to the State Treasurer's office.

California Debt Limit Allocation Committee: *Tax-Exempt Private Activity Bonds*

The California Debt Limit Allocation Committee (CDLAC), also an adjunct to the State Treasurer's office, administers the tax-exempt private activity bond program. Developers of projects financed under this program benefit from lower interest rates. Those savings, in turn,

³ Section 214(g)(1)(C) provides another option for exemption of low-income housing. In general, under this provision of the statute, the property may be restricted with some "other legal document" but it must be owned and operated by a qualifying nonprofit organization.

⁴ "California's High Housing Costs: Causes and Consequences", Legislative Analyst's Office, March 2015
<http://lao.ca.gov/Publications/Detail/3214>

can go toward enabling the construction of affordable rental housing for low-income households. These projects are also eligible to apply for LIHTCs.

California Department of Housing and Community Development (HCD)

HCD administers more than 20 programs that award loans and grants for affordable housing for low-income households. This funding is almost always awarded by HCD to local governments and non-profit housing developers, which may provide funds to individual end users.

HCD is also California's designated administrator of funds allocated from the National Housing Trust Fund, which is expected to provide funding for affordable low-income housing beginning in 2016.

California Housing Finance Agency (CalHFA)

CalHFA provides acquisition, rehabilitation and permanent financing to preserve, improve, maintain and increase the affordability of rental housing for very low and low-income families in California. In addition to lending, CalHFA administers funds from other governmental and third-party sources and works closely with these agencies to monitor and regulate these affordable units.

Current Legislation

Current legislation (AB 35) takes aim at the affordable housing crisis by modifying the state's administration of the LIHTC program. Among other changes, AB 35 would authorize CTCAC to allocate up to \$300 million in tax credits to developers. This amount is up from about \$75 million under current law.

As the number of projects eligible for the LIHTC program increases under AB 35, so would the number of projects eligible for the Welfare Exemption from property tax. Thus, both the BOE and county assessors must be aware of the new funding sources so that projects newly eligible for the Welfare Exemption can be approved for the exemption without delay.

Other current legislation (AB 668) requires assessors to consider the impact upon value of a home purchased with a 30-year, owner-occupied, affordable housing use restriction imposed by a nonprofit corporation. Existing law requires assessors to consider the effect upon value of any government-imposed restriction or any recorded contract involving a government agency. For nonprofit organization-imposed restrictions, the law currently provides that an easement entered into between a private land owner and a nonprofit organization for an open space, scenic, or trail easement must be considered when valuing the property. AB 668 adds another factor that must be considered that applies to affordable owner-occupied housing.

Other Concerns

State developers are actively working to nullify affordable housing ordinances in California. Recently, in *California Building Industry Association v. City of San Jose*, the California Supreme Court affirmed the city's right to enforce its inclusionary zoning ordinance. The ordinance (which is illustrative of many California city local inclusionary housing ordinances) requires new residential development projects of 20 or more units to sell at least 15 percent of the constructed for-sale homes at a price that is affordable to low or moderate income households. The measure gives developers the option of providing the requisite housing offsite through a number of available options; if they do so, however, the requisite low or moderate housing increment increases to 20 percent. The ruling sets a precedent for other California cities and counties to adopt a similar inclusionary zoning ordinance and to have "some legal assurance" that their policy would be upheld.