Identifying Affordable Quality Housing Components for Developing a Smart Growth Model

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ABSTRACT

Smart growth development entails retracting the city, hence attempting to house low-income residents at new affordable housing facilities within a metropolitan area. This paper introduces the Low Income Housing Tax Credit (LIHTC) as an alternative funding source for developing affordable housing projects. This paper presents affordable housing and smart growth elements from two selected tax credit programs in the United States. It compares these elements with the Malaysian commitments in Agenda 21 and recommends the Malaysian Point System that supports both affordable housing and smart growth requirements. It presents nine affordable housing and eleven smart growth elements that the proposed Malaysian LIHTC supports. The model includes four additional elements that Malaysia has committed to fulfill its Agenda 21. The proposed model can become an alternative solution for housing developers in Malaysia who cannot rely on government subsidies to develop affordable quality housing for the growing nation.

Keywords: Smart Growth Development, Affordable Quality Housing, Financing

1. INTRODUCTION

Many low-income people are trapped into paying high rental for low quality housing. It would even be farfetched for them to save enough for making down payments on a home. Malaysia needs to build 709,400 units of housing where 38.2% is for low- and low-medium units in the Ninth Malaysian Plan (9MP). The growing and shifting population is creating demands for new housing in some areas while decreasing demands for new and existing housing in another. The state of Selangor and Kuala Lumpur require 23.7% of new housing units to cater to its growing population in the 9MP. Inflation and other factors have brought about a dramatic increase in the cost of new and existing housing. In addition, th for consumer awareness is reflected in housing alternatives, improv truction method and materials. The need to provide affordable housi eople in growing metropolitan areas have long prompted the Ameri olic to develop alternative housing programs that are not degrading opulation in need. Hence, the birth of the Low Income Housing Tax section 42 (1986) of the Code in the USA. It requires each state to prep *ualified Allocation Plan* to determine housing priorities and to give pre to projects serving the lowest income tenants and projects obligated t qualified tenants for long periods (Development Authority of the N ountry, 2006).

In this article, we review two prog amely the *Washington State Housing Finance Commission* (Washin HFC) and *California Tax Credit Allocation Committee* (Californi C). Both must incorporate selection criteria, which include project lo housing need characteristics, sponsor characteristics, and tenant popu with special housing needs. With reference to the Malaysian Ninth nd Malaysian Vision 2020, we hope that any alternative Low Incom ing Tax Credit for Malaysia would also entail smart growth develop sing a local Malaysian Point System it could guide the development using policies towards improving a community's quality of life. We hat this approach could control the ratio of housing provision in t sumer basket of each family. The objectives of having a Malaysian stem are 1) providing safe, affordable shelter of high quality to those in establishing stability and opportunity in the lives of residents; and 3 ing communities that allow people from all ethnic, social and econ ckgrounds to live in harmony, with dignity and mutual respect. The p Malaysian Point System will include housing policies from Low Cost H (LCH) to Affordable Quality Housing (AQH) representing a practicab al-economic model. It will provide different opportunities for both come people and developers. By extrapolating both Washington SHFC and California TCAC programs, we initiated an analysis towards developing critical elements for supporting a smart growth LIHTC program in Malaysia.

This paper is an analytic review on how we could use the affordable housing provision to support successful smart growth policies by introducing low-income housing tax credit incentives. We compare two tax credit point systems in the United States (i.e., Washington SHFC, and California TCAC) and recommend key elements that Malaysia could benefit if incorporated. The study also compares whether the two programs are able to support the smart growth agenda for Malaysia, and recommends additional criteria to the model. With all key elements highlighted for the Malaysian Point System, we then recommend the distribution of points for all the criteria. However, details of the distribution will be published separately.

2. BACKGROUND LITERATURE

The main objective of this study is identifying key criteria for developing the Malaysian LIHTC allocation that would motivate housing developers to build more affordable housing development, ensuring dignified inclusion of tenants to such housing programs, and encouraging authorities to protect and preserve these products. Smart growth development entails retracting the city, hence attempting to house low-income residents at new affordable housing facilities within a metropolitan area. In contrast, the dense living conditions would cause the land price to surge upward due to the scarcity of available land. In USA, when the monthly carrying cost of housing exceeds 30-35% of a household income, housing is then considered unaffordable for that household (Barclay and Batker, 2004). For homeowners, an affordable mortgage payment is defined as 25 percent of household income, which allows 5 percent of income for other costs such as taxes, insurance, utilities and maintenance (Development Authority of the North Country, 2006). The American Planning Association (APA) outlines smart growth as a new method of metropolitan development leading to more compact regions, i.e., offering an alternative to sprawl (Barclay and Batker, 2004). Given that housing comprises a major share of the built environment, policies that promote denser residential development form a key component of smart growth. Although some of these policies may require new mechanisms, it provides long-term savings by eliminating inefficiencies caused by inconsistent and uncoordinated planning. There is growing awareness, too, that poorly planned development is a hidden tax on citizens and communities alike (Danielson, et al., 1999). Danielson, et al. highlight about the different benefits that may result from housing developed at greater densities compared to subdivisions of single-family homes on large lots.

Smart growth also means investing in time, attention, and resources in restoring community and vitality to existing cities and older suburbs (Committee on Environment and Public Works, 2002). Smart growth in new developments is more towns-centered, is auto-accessible but also accommodates transit and pedestrian activity, and has a greater mix of housing, commercial and retail uses. Moreover, it preserves open space and protects sensitive areas such as wetlands (Georgetown Land Development Company, 2006). Smart growth recognizes connections between development and quality of life. Smart growth advocates argue that, if done right, building more compact regions should not conflict with economic development. Perhaps the greatest challenge smart growth faces is community resistance to new development in already built-up areas. Enacting smart growth on a regional scale means that many existing lower density neighborhoods will receive new higher density housing. Suburbanites have a long history of resisting higher density housing for fear of what it might do to property values, and who may reside in such housing (Baar and Kenneth, 1992). White suburbanites, in particular, associate higher density affordable housing with neighborhood racial succession (Danielson, et al., 1999). No matter how much current politics oppose sprawl, policies adding higher density housing to most neighborhoods remain a tough sell. The choices have always been between having higher density and going for sprawl (Danielsen, et al, 1998).

The Low-Income Housing Tax Credit (LIHTC) has been the major federal program for producing affordable rental housing since its creation as part of the Tax Reform Act of 1986 (TRA). The LIHTC represents a partnership among a variety of public and private sector actors. The basic premise of the LIHTC is to offer federal tax credits to private investors in return for them to provide equity for the development of *affordable rental housing*. The intent of the program is to provide enough incentives to ensure that there will be an adequate supply of low-income housing by granting tax credits to the owners of selected rental housing developed for occupancy by low- or moderate-income households (McClure, 2000). The program is administered by the state (or, in a few cases, the local authority) housing policy makers who set goals for the program, review projects proposed by for-profit and nonprofit developers, monitor the reasonableness of project costs, and take responsibility for ensuring that projects stay in compliance and that approved projects receive only the tax credits necessary to make the project work. The Internal Revenue Service (IRS) is responsible for monitoring compliance and state performance

(Guggenheim and Joseph, 1994). The program has been viewed as both a success and a failure. It has been a success in that it has generated many rental-housing units that are now occupied by low- and moderate-income households. Although estimates vary, the program has contributed to the rehabilitation or construction of somewhere between 500,000 and 900,000 units (Ernst and Young, 1997). This success has been attributed to the program's flexibility. Units have been built across the country, in a variety of markets and serving a broad range of housing needs (Gummings and Di Pasquale, 1998). The tax credit program appears to have been absorbed into the rental housing development process, but market rate housing developers have not adopted it. Rather, it has been adopted by either nonprofit Community Development Corporations (CDC) or by specialized developers building projects entirely dedicated to low- or moderate-income occupancy. The units are going into largely metropolitan markets containing heavy concentrations of poor, minority households but rents are being charged that make the units affordable to only those poor households with the highest incomes in these areas (McClure, 2000).

The LIHTC provides favorable tax benefits as an incentive to invest in affordable housing. In most cases, the LIHTC investors are corporations rather than individual investors, as tax law in the USA (since 1992) is more favorable to corporations than to individual investors. This is because corporations can use passive losses (i.e., the investor is not directly involved in the business, he is a passive, versus active investor) against other income while individual investors cannot (Ontario Non Profit Association, 2006). Any tax credit allocation plan must incorporate a selection criteria to qualify, which includes project location, housing need characteristics, sponsor characteristics, and tenant populations with special housing needs.

3. RESEARCH METHODOLOGY

In our study, we compared two units for analysis in a case study research. They are the California TCAC "point system application LIHTC 2007 form" and Washington SHFC "point system application LIHTC 2007 form". We propose that there are favorable criteria that Malaysia could benefit for inclusion in the Malaysian Point System that would support affordable housing and smart growth elements. We extracted the affordable housing and smart growth elements, which are embedded within the "Point System" for ranking and scoring of the Malaysian LIHTC. We then compare the affordable housing and smart growth elements in both programs before recommending key elements for smart growth principles within affordable housing requirements to be applied in the Malaysian context. Then, we report the summary of the scoring and ranking as the proposed criteria for a Malaysian Point System.

4. LIHTC POINT SYSTEM FOR SCORING AND RANKING

When the United States' housing authorities receive far more applications for tax credit than it could award, it started to implement a point system for ranking applications in 1999. A housing development applicant is responsible for demonstrating that his project qualifies for all selected *Allocation Criteria* and ensuring that all appropriate attachments are submitted. The state's tax credit program administrator will determine if a *project* qualifies to receive *Allocation Criteria Points*. Although it is somewhat complicated by the overlay of statutory set-asides and geographical apportionments, the basic point structure supports applications that show evidence of leveraging public and some private funds, whose owner and management company have previous affordable housing experience, have location amenities (for example, being located by a public transit stop), offering tenants various service amenities (for example, after school computer classes), serving the lowest income tenants, are "mixed income" projects that have a non-tax credit component of renters, ready to proceed with construction, attain energy efficiencies, and contribute to neighborhood revitalization. The point system is not a competition between developers, but rather for projects to excel by earning all maximum scores of point system. We outline the point system details in Table 1 below.

Table 1: Inclusion and Score Distribution of Affordable Housing and Smart Growth Elements in the Washington State Financing Committee (2007), California Tax Credit Allocation Committee (2007) and the proposed Malaysian Point System

	Elements/Principles/Commitments (Constructs)	Washington SHFC		California TCAC		Proposed Malaysian Point System	
		Location	Weight	Location	Weight	Location	Weight
Affordable Housing Elements (Adapted from Metropolitan Tenant Organizer (2007))	Focused on families with minimum wage	1, 2, 7, 8, 9 & 10	*51.9%	5	41%	6	22.35%
	Based on sliding scale	LIHTC	X%	LIHTC	X%	LIHTC	X%
	Medical expenses should be deducted from housing cost	-	-	-	-	-	-
	Housing size needs to be based on family need	6	3.9%	2	8%	2	4.06%
	Choice about location	*LIHTC	X%	LIHTC	X%	LIHTC	X%
	Needs to be stable in rent	LIHTC	X%	LIHTC	X%	LIHTC	X%
	Must meet stringent housing quality standards	-	-	4	8%	5	4.06%
	Based on the income	LIHTC	X%	LIHTC	X%	LIHTC	X%
	Should have the same rights, & responsibilities	Management System	X%	Management System	X%	Management System	X%
	No additional fees	-	-	3(B)	10%	LIHTC& 4	X%
Smart Growth Principles (Adapted from APA (2002))	Preserve open space	-	-	-	-	12	8.13%
	Conservation of natural resources	-	-	4	8%	5	4.06%
	Developing infill sites	-	-	-	-	10	4.87%
	Pedestrian-friendly architecture	-	-	3(A) & 3(B)	Z	3, 4, 11 & 12	28.45%
	Include citizens in land use decision-making ventures	-	-	-	-	1	2.43%
	Provision for creating widespread affordable housing	LIHTC	-	LIHTC	-	LIHTC	X%
	Encourage regional governing solutions to urban/suburban sprawl	-	-	-	--	11	6.1%
	Reduce automobile dependence	-	-	3(A)	12%	3, 4, 11 & 12	28.45%
	Promote compact, high-density or mixed-use development	-	-	3(A) & 3(B)	Y	11	6.1%
	Encourage cooperation from local/regional governments and planning organizations	4, 17 & 18	7.9%	-	--	1	2.43%
	Impose the social costs of new development onto real estate developers	-	-	3(B)	10%	3 & 4	14.22%

	Elements/Principles/Commitments (Constructs)	Washington SHFC		California TCAC		Proposed Malaysian Point System	
		Location	Weight	Location	Weight	Location	Weight
Additional Malaysian Commitments to Agenda 21	Physical and social infrastructure	-	-	-	-	8	8.13%
	Female-headed as a target group	-	-	-	-	13	6.1%
	Attention to mix income housing	-	-	-	-	14	4.87%
	Concentrate on building for disadvantaged and the poor in urban area	-	-	-	-	8 & 11	14.22%

NOTE:
* = The percentage is an approximate total of common elements in a program.
*LIHTC = Some elements are involved in LIHTC aims and management system.
X% = Unaccountable.
Y = Although developers would pay the costs for improving site and services amenities, they may not directly involve pedestrian-friendly architecture.
Z = Applicable to mix-development projects only.

4.1 California Tax Credit Allocation Committee (California TCAC)

The point system in the LIHTC 2007 application form under the California TCAC program has 6 articles with total possible points of 124 (California Tax Credit Allocation Committee, 2007). We list the 6 articles below in reference to Table 1 on the allocation criteria:

1. **General Partner/Management Company Characteristics** (maximum 9 points)
   (A) General Partner experience
   (B) Management Company experience
2. **Housing Needs** (maximum 10 points)
   Large Family Projects or Single Room Occupancy Projects or Special Needs Projects or Seniors Projects or At-Risk Projects
3. **Amenities (A-Site)** (maximum 15 points)
   Amenities (B-Service) (maximum 10 points)
4. **Sustainable building methods** (maximum 10 points)
5. **Lowest Income** (maximum 52 points)
6. **Readiness to Proceed** (maximum 20 points)

4.2 Washington State Housing Finance Commission (Washington SHFC)

The point system in the LIHTC 2007 application form under the Washington SHFC program has 20 articles that a developer can earn a maximum 277 points (Washington State Housing Finance Commission, 2007). We list the 20 articles below in reference to Table 1 on the allocation criteria:

1. **Additional low-income housing set-aside**. Points will be awarded to Projects based on the Applicant's Commitment to provide selected percentages of the Total Low Income Units for occupancy by households at or below selected Area Median Gross Income levels (Maximum 50 points).
2. **Additional low-income housing use period.** (Maximum 44 points).
3. **Housing needs.** Points will be awarded based on the county in which the project is located. (Maximum 10 points).
4. **Nonprofit sponsor.** (Maximum 5 points).
5. **Farm worker housing.** (Maximum 25 points).
6. **Housing for large households.** (Maximum 10 points).
7. **Housing for persons who are elderly**. (Maximum 10 points).
8. **Housing for persons with disabilities.** (Maximum 10 points)..
9. **Housing for the homeless.** (Maximum 20 points).

10. **Preservation of federal assisted low-income housing**. (Maximum 10 points).
11. **Maximize use of credit**. Projects that request the "4%" credit and that agree to limit the credit reservation and/or allocation to $4,050 or less per low-income housing unit or projects that request the "9%" credit and that agree to limit the credit reservation and/or allocation to $7,940 or less per low-income housing unit (Maximum 10 points).
12. **Rehabilitation projects.** Points will be awarded to projects consisting of one or more buildings, which will be rehabilitated and returned to, or converted to, residential use (Maximum 12 points).
13. **Project size**. Points will be awarded based on the greater (Maximum 10 points).
14. **Developer fees.** (Maximum 10 points).
15. **Historic property.** Percentage of housing units in building(s) designated as historic property (Maximum 5 points).
16. **Targeted areas**. A Difficult to Develop Area (DDA) or a Qualified Census Tract (QCT), additional points * may be scored if the entire project is located in a QCT and the Project's development contribute to a Community Revitalization Plan (Maximum 7 points).
17. **Leveraging of public resources.** (Maximum 10 points).
18. **Donation in support of local housing needs.** (Maximum 5 points).
19. **Eventual tenant ownership.** (Maximum 2 points).
20. **Project readiness** (Maximum 12 points).

Notice the differences between both programs from Washington and California states in the United States. We categorize all the affordable housing elements and the smart growth principles in two original groups and try to show which element has come in which point system. Both Washington and California's point systems give special attention to the first affordable housing element, i.e., focused on families with minimum wage. However, they defer on one of the smart growth principles, which is reducing automobile dependence. We found that the California point system includes this element while Washington did not. Another contrary item is that the Washington point system focuses on encouraging cooperation from local/regional governments and planning organizations, which California does not. As the reader would note, the ratings differ for each element between both states since both have differing number of articles and points for consideration. For instance, California focuses on the quality of life while Washington emphasizes on the human factors such as the elderly, farmers and homeless.

5. PROPOSED MALAYSIAN POINT SYSTEM FOR LOW INCOME HOUSING

In this section, we describe the motivation for the Malaysian Point System for low income housing in Malaysia. Housing has been heavily promoted in the 7th Malaysian Plan (7MP) and the 8th Malaysian Plan (8MP). The 9MP is expected to see the government's continuous effort to ensure that Malaysians of all income levels will have access to adequate, quality and affordable homes, particularly for those under the low-income group. In this regard, the private sector is expected to support the government's initiative to build more low- and low-medium-cost houses in their mixed-development projects while the public sector will concentrate on building low-cost houses as well as houses for public sector employees, the disadvantaged and the poor in urban and rural areas. To enhance the quality of life of the urban population, the provision of more systematic and well organized urban services programs will emphasis on sustainable development, promoting greater community participation and social integration of the population (Malaysian 9th Plan). As a participant at the 25th special session of the general assembly for an overall review and appraisal of the implementation of the outcome of the United Nations Conference on Human Settlements (Habitat II) in New York in 2001, Malaysia has made a commitment to implement Agenda 21. We extracted the key elements in these documents and list them below:

1. Median income group beside the low income group (Seventh Malaysian Plan)
2. Quality of life (Ninth Malaysian Plan)
3. Development projects with the public sector (Ninth Malaysian Plan)
4. Houses for public sector employees (Ninth Malaysian Plan)
5. **Concentrate on building for disadvantaged and the poor in urban and rural areas (Ninth Malaysian Plan)**
6. More systematic and well organized urban services programs (Ninth Malaysian Plan)
7. Emphasize on sustainable development (Ninth Malaysian Plan)
8. Promoting greater community participation (Ninth Malaysian Plan)
9. **Physical and social infrastructure (Malaysian statement at Habitat II)**
10. Soft housing loan for target group (Malaysian statement at Habitat II)
11. **Female-headed as a target group (Malaysian statement at Habitat II)**
12. **Attention to mix development and mix income housing (Malaysian Vision 2020)**

We found four items (as highlighted above) missing from the combined affordable housing and smart growth elements requirements. Hence, we extended Table 1 to include the four Malaysian smart growth requirements. Additionally, we would like to support the introduction of three smart growth elements that are missing in both tax credit programs. They are preserving open space, developing infill sites, and encouraging regional governing solutions to urban/suburban sprawl. In this table, we include the weight distribution amongst the proposed elements for the Malaysian Point System. The biggest weight is located at pedestrian-friendly architecture (28.45%), reducing automobile dependence (28.45%), families with minimum wage (22.35%), impose the social costs of new development onto real estate developers (14.22%), and concentrate on building for disadvantaged and the poor in urban area (14.22%). More details on how we break down the elements will be published in a separate article. In view of the varied distributed points over the proposed 24 elements, the study would like to propose the need to form an administrative commission overseeing the qualified allocation plans.

6. CONCLUSION

In this paper, we attempt to develop articles for a low-income housing tax credit program for Malaysia that includes smart growth elements while supporting the development of affordable housing units in Malaysia. The proposed Malaysian Point System supports nine affordable housing elements including focusing on family with minimum wage, points based on a sliding scale, housing sizes are based on family needs, choice of location, needs to be stable in rent, must meet stringent housing quality standards, based on the income, should have the same rights and responsibilities, and no additional fees. It also supports eleven smart growth elements including preservation of open space, conservation of natural resources, developing in-fill sites, pedestrian-friendly architecture, inclusion of citizens in land use decision-making ventures, provision for creating widespread affordable housing, encouragement for regional solutions to urban/suburban sprawl, reduction on automobile dependence, promotion of compact high density or mixed-used development, encourage for participation of corporation from local/regional governments and planning organizations, and imposition of the social costs of new development onto real estate developers. We are proposing the inclusion of four elements that Malaysia committed in Agenda 21 including physical and social infrastructure, female-headed as a target group, attention to mixed-income housing, and concentrate on building for disadvantaged and the poor in the urban area. The proposed Malaysian Point System is expected to shift low-income housing policies from a low-cost housing paradigm to affordable quality housing provision. With an authorized commission to oversee its implementation, the Malaysian Point System can become a social- economy model for Malaysian authorities that would encourage private developers to support affordable quality housing projects.

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