



**Smart Growth America**  
Making Neighborhoods Great Together

# **Federal Involvement in Real Estate** A Call for Action

July 2013





## Smart Growth America

Making Neighborhoods Great Together

**Smart Growth America** is the only national organization dedicated to researching, advocating for and leading coalitions to bring better development strategies to more communities nationwide. From providing more sidewalks to ensuring more homes are built near public transportation or that productive farms remain a part of our communities, smart growth helps make sure people across the nation can live in great neighborhoods. Learn more at [smartgrowthamerica.org](http://smartgrowthamerica.org).

### Project team

Geoff Anderson, President and CEO, Smart Growth America  
Ilana Preuss, Vice President and Chief of Staff, Smart Growth America  
Christopher Coes, Managing Director, LOCUS, Smart Growth America  
Catherine Hartnett, Director of Government Affairs and Outreach, Smart Growth America  
Alex Dodds, Online Communications Manager, Smart Growth America  
Craig Chester, Press Manager, Smart Growth America  
Jay Corballis, LOCUS Associate, Smart Growth America  
Zach Smith, Program Associate, Smart Growth America

McBee Strategic

### Acknowledgments

Thank you to the members of LOCUS's Steering Committee. Additional thanks go to the following contributors:

Frank Alexander, Emory University  
Ethan Handelman, National Housing Conference  
Chris Leinberger, President, LOCUS, Smart Growth America  
Lynn Ross, Urban Land Institute

### Photo credits

Cover: Midtown Lofts in Minneapolis, MN. Image courtesy of the Lander Group.  
Page 6: Gateway Senior Apartments in Fremont, MI. Image courtesy of HRS Green.  
Page 7: Blue Plate Lofts in New Orleans, LA by HRI Properties. Image by Theodore Lee via Flickr.  
Page 10: Trinity Flats in Cincinnati, OH. Image courtesy of Cincinnati Center City Development Corporation.

# Table of Contents

<b>Executive Summary</b> .....	<b>i</b>
<b>Introduction</b> .....	<b>1</b>
Guiding principles for reform .....	1
<b>Policy Recommendations</b> .....	<b>2</b>
1. Eliminate some rate subsidies from the National Flood Insurance Program .....	2
2. Reform the Federal Housing Administration’s single-family home program .....	3
3. Better target real estate tax expenditures .....	4
4. Preserve and increase the Low Income Housing Tax Credit .....	5
5. Improve the Rehabilitation Tax Credit .....	7
6. Establish individual mortgage savings accounts .....	8
7. Create an Innovative Financing for Infrastructure Rehabilitation Program .....	9
<b>Conclusion</b> .....	<b>11</b>
<b>Endnotes</b> .....	<b>12</b>

## Executive Summary

Smart Growth America and its coalition of real estate developers and investors LOCUS, which represents private-sector development interests from across the United States, present a series of reforms to federal real estate programs. Taken together, these reforms could save the federal government an estimated \$33 billion per year while updating outdated programs to achieve better outcomes for households, communities and taxpayers.

This report builds on Smart Growth America's January 2013 report, *Federal Involvement in Real Estate: A Call for Examination*, which examined the federal government's current spending and commitment to real estate programs each year. From loan guarantees to commercial tax credits, this spending amounts to roughly \$450 billion annually and spans over 50 programs created at multiple agencies, at different times for various purposes over the past several decades.

These programs often have laudable aims: helping families purchase their first home, helping those most in need pay their rent and aiding community redevelopment. As *A Call for Examination* explained, however, there are problems with these programs both individually and as a group.

Today's programs unfairly penalize families who can't afford or choose not to buy a home, favor single-family homes over other types and provide financial incentives to purchase second homes when many families still struggle to purchase their first. In addition, the majority of funding goes to a small proportion of households, several policies are barriers to forces in today's marketplace and programs are failing to adequately support existing neighborhoods. Taken as a whole federal real estate programs have not kept pace with the evolving real estate market nor do they pursue a coherent set of policy goals.

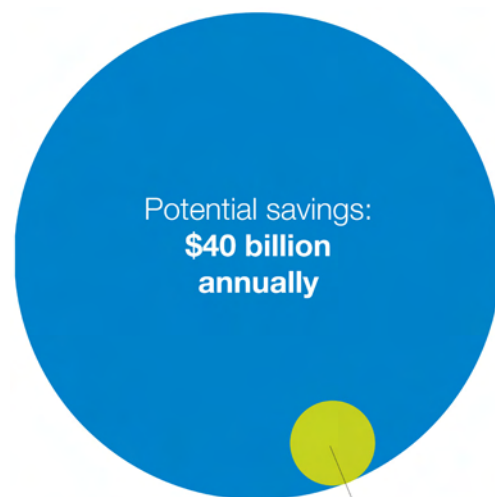
***Federal Involvement in Real Estate: A Call for Action* proposes policy changes to begin to address these problems.** We encourage Congress to improve federal real estate programs in the following ways:

1. Eliminate some rate subsidies from the National Flood Insurance Program.
2. Reform the Federal Housing Administration's single-family home program.
3. Better target real estate tax expenditures.
4. Preserve and increase the Low Income Housing Tax Credit.
5. Improve the Rehabilitation Tax Credit.
6. Establish individual mortgage savings accounts.
7. Create an Innovative Financing for Infrastructure Rehabilitation Program.

These recommendations would improve federal real estate programs to help families become more prosperous and better support economically resilient towns. The recommendations are designed to reflect the fiscal realities facing the country today, and include a potential \$40 billion in annual savings. Of that, we recommend redirecting \$7 billion to new or improved programs.

Together these changes would help federal real estate programs better achieve their goals and better reflect current market, budget and economic realities. With Congress and the administration taking a fresh look at how the nation spends taxpayer money, now is the time for policymakers to strengthen federal real estate programs.

Taken together, these reforms could save the federal government an estimated \$33 billion per year



## Introduction

Federal real estate programs could be more efficient and could provide better value for American families, communities and taxpayers.

That was the finding of *Federal Involvement in Real Estate: A Call for Examination*, released by Smart Growth America in January 2013.<sup>1</sup> The report examined the federal government's spending and commitment to real estate programs each year: \$450 billion annually across 50 programs at half a dozen federal agencies. This examination did not include the Government Sponsored Enterprises, nor did it include non-real estate spending that greatly influences development such as investments in transportation, other infrastructure and federally owned real estate.

From loan guarantees to commercial tax credits, federal real estate programs help families purchase their first home, help those most in need pay their rent and aid community redevelopment, along with many other things. Taken as a whole these expenditures influence where and how homes, businesses and even whole neighborhoods are built in the United States.

As *A Call for Examination* explained, there are problems with current federal real estate programs. Today's programs unfairly penalize families who can't afford or choose not to buy a home, favor single-family homes over other types, and provide financial incentives to purchase second homes when many families still struggle to purchase their first. In addition, the majority of funding goes to a small proportion of households, several policies are barriers to forces in today's marketplace and programs are failing to adequately support existing neighborhoods.

These shortcomings mean today's programs are creating an inefficient real estate market. It means federal programs are not helping families move up the economic ladder as well as they could, and it means programs are missing an opportunity to support America's economic recovery through reinvestment in neighborhoods and downtowns.

## Guiding principles for reform

There are currently no overarching goals or guiding principles that drive the federal government's involvement in the real estate market. Without a clear set of goals it is hard to judge the rationale or effectiveness of the government's current investments, or to evaluate them for areas to improve.

Therefore, in our previous report we sought to make federal goals explicit and to use these as a guide to reform.

- **Support balanced housing choices in suburbs, cities and rural communities.**

The federal government's involvement in the market should not steer homebuyers or renters toward a particular housing product. This is especially relevant in today's marketplace, when demand for multifamily homes is growing more quickly than for single-family ones. A majority of Americans today would prefer to live in neighborhoods with a mix of housing types and transportation choices near a grocery store, jobs and schools; demand for homes in walkable neighborhoods could exceed 140 percent of the current supply over the next 10 years.<sup>2,3</sup> The federal government should be efficient with federal resources and modernize investments to reflect today's demand for a variety of housing choices in all communities.

- **Reinvest in America's existing communities and neighborhoods.**

The federal government should support stability in communities where the public and private sectors have already made substantial investments. Failing to do this can lead to precipitous declines in neighborhood value, causing deep losses in household wealth, defaults and economic dislocation. Federal programs should protect past public and private investments, including property values and infrastructure. This would also benefit local governments, which can reduce costs and increase revenue by focusing development investments.<sup>4</sup>

- **Provide a safety net for American families.**

The federal government has long invested in a variety of programs that provide a safety net for families and individuals who would otherwise not be able to meet their basic need for shelter. Shelter is a basic building block that enables individuals to participate in the economy, and from practical and policy perspectives providing this creates a host of public goods and avoids public harm. Despite being one of the most fundamental functions of government, this goal currently receives some of the lowest levels of federal support. Federal programs should continue to provide a safety net and increase the level of support provided.

- **Help more Americans reach the middle class.**

Federal real estate programs should help all Americans—whether homeowners or renters in rural, suburban and urban communities alike—reach the middle class. A broad and thriving middle class has been a driver of America’s prosperity in the last century and a symbol of each citizen’s opportunity to achieve the American Dream. Federal intervention in real estate has long been justified as a means to support citizens as they seek to gain middle class lifestyles. Federal real estate programs can and should serve this purpose but to do so requires reforming programs that were designed decades ago and no longer meet market and economic realities.

The reforms proposed in the following pages are designed to help federal real estate programs achieve these four goals. They are a set of interdependent proposals that both save money and improve how these programs work. By reforming select federal programs, taxpayers can get more out of these investments while also supporting neighborhoods and providing better opportunities for families across the country.

## Policy Recommendations

To improve federal real estate programs for American families, communities and taxpayers, we recommend seven specific changes.

These recommendations include a potential \$40 billion in annual savings. Of that, we recommend redirecting \$7 billion to new or improved programs. The remaining \$33 billion can be used for deficit reduction, to facilitate broader tax reform or both.

### 1. Eliminate some rate subsidies from the National Flood Insurance Program.

In 1968, Congress created the National Flood Insurance Program (NFIP) to provide property owners a way to financially protect themselves from flood damage. Administered by the Federal Emergency Management Agency, the NFIP works closely with nearly 90 private insurance companies to offer flood insurance to homeowners, renters and business owners.<sup>5</sup>

#### Why take action?

Many property owners and renters covered by the NFIP pay highly subsidized rates that do not reflect the true risk of flooding or the costs associated with it. These subsidies have contributed to increased development in flood hazard areas, putting more people and property at risk. And this has come at a high cost to taxpayers: The program is currently almost \$24 billion in debt to the Department of Treasury.<sup>6</sup>

Insurance subsidies mask risk, so property owners may not understand the true likelihood or cost of flood damage. The subsidized rates also eliminate the financial incentive for homeowners to reduce their exposure to flood hazard areas. If left undeveloped, flood hazard areas also have the potential to act as natural buffers during storms and reduce costs due to flood damage, but developing these areas eliminates this potential.

Recognizing the high costs of the program and the way in which it incentivizes new development in flood-prone areas, Congress passed legislation in 2012 that took steps to reduce subsidies for some structures included in the NFIP, thus reducing the incentive to locate in flood hazard areas. However, we believe there is more to be done to ensure the government is not encouraging development in these critical areas while providing needed resources through a comprehensive process for target communities' ongoing flood mitigation efforts.

These subsidies have contributed to increased development in flood hazard areas.

#### **What is the solution?**

Smart Growth America recommends phasing out a portion of NFIP rate subsidies so that insurance rates better reflect the true risk of flooding. Rates should be risk-based and subsidies should be means tested. In addition, targeted assistance should be provided outside of the rate structure for low-income families, and mitigation funds should be used to help nationally targeted communities develop innovative flood mitigation strategies to achieve affordable, accessible and self-sustainable outcomes. This would ensure the program continues to help those most in need of support and create economically resilient communities.

We estimate that this strategy could save \$8 billion over the next 10 years.<sup>7</sup>

#### **How will this change meet the guiding principles for reform?**

Eliminating some NFIP rate subsidies to better focus on low- and middle-income families will improve the program's role as a safety net for American families. Subsidizing insurance for all flood hazard areas households, no matter their income level, is not an efficient use of federal dollars, leads to higher costs for taxpayers in the long run and does not serve the NFIP's goals.

## 2. Reform the Federal Housing Administration's single-family home program.

The Federal Housing Administration (FHA) plays a critical role in the U.S. housing market and has helped millions of first-time and low- to moderate-income households buy their homes. In times of economic distress FHA has stepped up to ensure mortgages were available more widely in the market. This is evidenced by the program's gain in market share during the recent recession, which grew from 5 percent in 2006 up to 30 percent by 2008. FHA's market share today remains at more than 25 percent.<sup>8</sup> Congress has been wary of altering FHA, given that it is now backing more loans than ever before. However, as the housing market rebounds now is the time to look at improving the agency and refocusing its mission.

Congress expanded FHA's reach to include upper-income borrowers, but that role is no longer required.

#### **Why take action?**

During the recent recession Congress expanded FHA's reach to include upper-income borrowers, but that role is no longer required.

Perhaps more pressing, FHA's fiscal health is at risk: For the first time in its history the agency may need to borrow funds from Treasury. FHA's fiscal year 2014 budget shows the agency may need to draw down just under \$1 billion; however a stress test recently showed that the agency could need as much as \$115 billion in the event of a significant downturn. Reforms should be made to ensure that FHA premiums are risk-based and can cover losses. This will also help FHA stabilize its finances.

#### **What is the solution?**

Smart Growth America recommends Congress lower FHA's loan limit from its current, historically high level of \$729,000 to a more traditional level.<sup>9</sup> Congress should also consider increasing guarantee fees and allowing FHA to seek indemnification from problem lenders, similar to provisions in legislation passed by the House in 2012.<sup>10</sup> In addition, FHA should do a thorough analysis of losses and delinquencies to determine if their creditworthiness

standards are appropriate. These changes would help FHA return its focus to insuring loans for creditworthy borrowers who otherwise could not become homeowners through the private mortgage market.

We estimate such reforms could save \$2.5 billion between 2011 and 2015.<sup>11</sup>

### How will this change meet the guiding principles for reform?

The original intent of FHA's loan programs was to help lower-income families become homeowners. Lowering loan limits will refocus the FHA's work on its original goal to help more Americans reach the middle class.

## 3. Better target real estate tax expenditures.

As Congress begins to consider comprehensive tax reform, all real estate tax programs deserve examination. Three in particular warrant closer review.

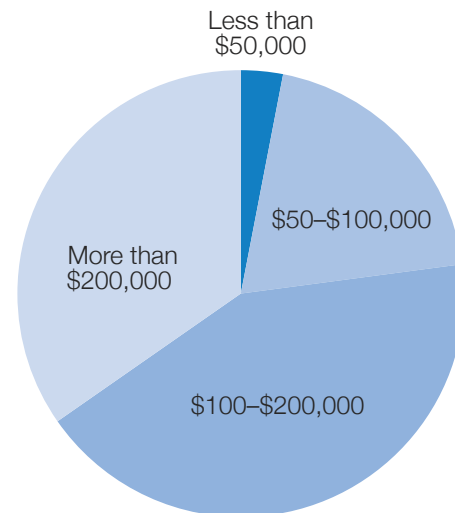
The mortgage interest deduction, one of the largest of all tax expenditures, averages \$70 billion annually. The real estate tax deduction, which makes property taxes deductible from income taxes, averages \$26 billion annually. And the capital gains exclusion, which exempts from income taxes profit from the sale of a home (within limitations), was worth over \$23 billion in 2013 alone.<sup>12</sup>

### Why take action?

The intent of these programs is to encourage broad homeownership. The reality, however, is that much of these benefits go to a relatively small number of taxpayers, and much of that benefit accrues when homeowners purchase expensive homes, not entry-level ones. As a result much of the benefit is less effective than it could be otherwise.

In 2012, 77 percent of mortgage interest deduction benefits went to homeowners with incomes above \$100,000.<sup>13</sup> Homeowners with incomes above \$200,000 received 35 percent of mortgage interest deduction benefits and an average subsidy of \$5,000.<sup>14</sup> Meanwhile, homeowners with incomes below \$50,000—about 40 percent of all homeowners—received only 3 percent of the benefits from the mortgage interest deduction.<sup>15</sup> Because homeowners must itemize their return in order to claim the deduction, it is more likely to be used by higher income households. These households are more likely to use the deduction for higher-cost homes and even second homes—neither of which are within the deduction's policy objectives.

Mortgage interest deduction benefits by household income



We estimate such reforms could save more than \$378 billion over the next 10 years

The real estate property tax deduction is also primarily taken by higher-income households. Of tax filers who claimed this deduction, 75 percent earn above \$100,000 per year.<sup>16</sup>

The capital gains exclusion for home sales was raised to \$500,000 per household in 1986 and it can be claimed every two years. It does not help spur homeownership, provide a safety net, nor increase housing choices.

### What is the solution?

Smart Growth America recommends limiting the mortgage interest deduction to primary residences, and capping the deduction at \$500,000 instead of \$1 million in mortgage value.<sup>17</sup> We also recommend limiting the real estate tax deduction for households earning over \$100,000 per year. In addition, the capital gains exclusion should be lowered from \$250,000 for individuals and \$500,000 for households to \$125,000 for individuals and \$250,000 for households. The ability to claim the exclusion should be limited to once every 10 years to ensure that this tax benefit is not being used for activities like housing speculation.



We estimate such reforms could save more than \$378 billion over the next 10 years.<sup>18</sup> Even if these changes were phased in over five years, savings could still be as high as \$197 billion over 10 years.<sup>19</sup>

### How will this change meet the guiding principles for reform?

Better targeting real estate tax expenditures would ensure that these subsidies return to their original intent of promoting homeownership and helping more Americans reach the middle class. Phasing in these changes gradually will give the market time to adjust without major disruption.

## 4. Preserve and increase the Low Income Housing Tax Credit.

Demand for rental homes is surging in the United States. The number of households that rent homes increased by one million in 2011, the largest annual increase since the early 1980s.<sup>20</sup> This number is projected to grow by between 360,000 and 470,000 annually over the next decade.<sup>21</sup>

Compounding the rising demand for rental homes is the fact that the United States loses a significant portion of rental housing each year. Of the rental stock available in 1999, 6.3 percent was permanently lost by 2009.<sup>22</sup> The growing number of renters and the loss of housing stock combined with anticipated population growth means demand across the rental market is tightening.

This is particularly a problem for people seeking affordable rentals. Between 1999 and 2009, for every two rental units that moved down to the low-cost category (renting for less than \$400 in 2009 dollars), three rental units moved to higher rent levels—resulting in a 9.1 percent loss of low-cost housing stock.<sup>23</sup> In 2009, 18 million very-low-income renters competed for 11.6 million affordable and available rental units.<sup>24</sup> This left a supply gap of 6.4 million units, demonstrating the need for investment in affordable rental housing.<sup>25</sup>

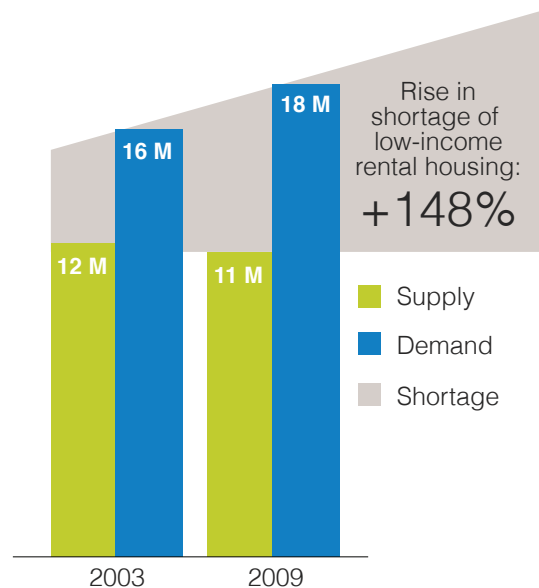
The Low Income Housing Tax Credit is the principal way the federal government supports the construction and preservation of affordable rental housing. Since its creation in 1986, the credit has proven to be one of the most effective federal programs in addressing our growing need and demand for affordable housing. The credit has provided financing for more than 2.5 million affordable homes and leveraged more than \$75 billion in private investment capital.<sup>26</sup>

### Why take action?

The credit continues to help the private sector add about 100,000 rental units annually. However, this support does not build enough affordable rental housing to meet the current and growing market demand in communities across the country.

When the credit was created, the amount awarded to development projects was based on a formula that used the federal cost of borrowing to determine the credit rate. This created a floating credit rate. This means that the amount of credits that may be used to build development with the Low Income Housing Tax Credit decreases as the federal cost of borrowing falls.

In recent years, the cost of federal borrowing has been low, meaning the amount of credits available has been low as well. In response, Congress enacted legislation in 2008 which set a fixed minimum credit rate of nine percent for new construction and substantial rehabilitation for properties put in service through 2013, based on the original rate when the program was created. This provision has simplified state administration of the program, and removed the financial uncertainty and risk associated with underwriting credit-financed properties using the floating rate system.<sup>27</sup> This provision has been extended to apply to any projects receiving credit allocations through the end of 2013.





## The Low Income Housing Tax Credit in action

A model for this reform is Home Renewal Systems, which used the Low Income Housing Tax Credit to help finance affordable rental housing development in Fremont, Michigan. Specifically, Home Renewal Systems used the credit to finance the redevelopment of a downtown building into the Gateway Senior Apartments. These senior housing units are ideally located in walking distance to downtown Fremont, which features a full range of commercial and retail services, including restaurants, beauty and barber shops, and a farmers' market.

### **What is the solution?**

Smart Growth America recommends making the nine percent fixed minimum credit rate, which applies to new construction and substantial rehabilitation, permanent.<sup>28</sup> This policy has proven to be successful in increasing the efficiency and effectiveness of the credit at little or no cost to the federal government.<sup>29</sup> Making the minimum rate permanent would allow the federal government to provide more private equity for any given project, enabling more deals to be financially feasible. Additionally, a fixed floor rate for the acquisition credit at no less than four percent should be enacted to further enhance the efficiency of the program. These policy changes will maintain private investment in the program by reducing the financial risk and uncertainty associated with the floating rate system. Maintaining the minimum credit rate will not increase the amount of credits awarded, so it would have minimal cost.

In addition, we recommend increasing the credit's annual allocation by 50 percent.<sup>30</sup> The credit plays a crucial role in producing virtually all of the nation's affordable housing, and demand is growing. Increasing the credit's annual allocation could support the preservation and construction of 350,000 to 400,000 additional affordable rental housing units over the next 10 years.<sup>31</sup>

We estimate these reforms would cost \$4 billion annually.

### **How will this change meet the guiding principles for reform?**

By ensuring the Low Income Housing Tax Credit is a permanent part of the tax code and by increasing its effectiveness and efficiency, policymakers will bring affordable housing to more communities and provide a crucial safety net for American families. The credit also supports balanced housing choices by providing financing tools to meet demand for affordable rental housing choices.



## 5. Improve the Rehabilitation Tax Credit.

Rehabilitating existing buildings and revitalizing neighborhoods reduces costs for municipalities and adds to the local tax base.<sup>32</sup> This process creates an asset for a community and can help attract new private-sector investment in the surrounding area.

### The current scope of the Rehabilitation Tax Credit limits its effectiveness.

Despite redevelopment's significant benefits, these projects often face significant financial barriers. Decades worth of deferred maintenance must often be addressed before redevelopment can occur, and these upfront costs can make redevelopment projects cost-prohibitive.

To address these barriers, in 1976 the federal government created the Rehabilitation Tax Credit. This credit may be taken to cover 10 percent of the costs of the rehabilitation of non-residential and non-historic buildings constructed prior to 1936. For mixed-use projects, the credit may be used on non-residential parts of the building.

#### Why take action?

The current scope of the Rehabilitation Tax Credit limits its effectiveness. First and foremost the credit can now only be used for commercial development and excludes residential properties. It also can only be claimed for buildings built before 1936, making many structures ineligible. And it can only be claimed on one building at a time. Because older buildings are sometimes in blighted areas, however, some revitalization projects must go beyond a single building to be effective and economically feasible.

#### What is the solution?

Smart Growth America recommends Congress reform and improve the Rehabilitation Tax Credit to better match revitalization project market realities to ensure maximum private-sector leverage.

We recommend increasing the credit to 15 percent of rehabilitation costs; broadening eligibility to include redevelopment costs beyond those associated with a specific building; making residential buildings eligible; and changing the age criteria so that any building over 50 years old would be eligible for the credit.<sup>33</sup>

To qualify for the credit under these new terms, a building would need to be placed into service more than 50 years ago. Twenty-five percent of the new construction costs associated with the project would be eligible for

the 15 percent credit. However, the credit could not exceed the total rehabilitation costs of all the buildings older than 50 years within the project. To better support investment in existing communities, we also recommend a provision to encourage projects within one-half mile from a town center or an existing or planned transit facility.

We estimate these changes would cost \$1.6 billion annually.

### **How will this change meet the guiding principles for reform?**

Building rehabilitation, by its definition, reinvests in existing communities and neighborhoods, and expanding the Rehabilitation Tax Credit would make this easier for communities across the country.

## **6. Establish individual mortgage savings accounts.**

Homeownership can help individuals and families build wealth, and plays a significant role in the economic security of America's middle class. Many federal real estate programs are designed to promote homeownership but none address the biggest barrier to becoming a homeowner in the first place: the down payment.

### **Why take action?**

Saving for a down payment is challenging for many families, and in the aftermath of the real estate bust many lenders have increased down payment requirements. This fact may be part of why homeownership rates are falling: over the past 5 years the homeownership rate in the United States has fallen from 67.3 percent in 2005 to 64.6 percent in 2011.<sup>34</sup> Declines exceed 5 percent for households aged 44 and lower, and exceed 4.5 percent for 45–54 year-olds.<sup>35</sup>

Homeownership doesn't always make sense for everyone, and as we have noted earlier non-homeowners shouldn't be penalized for that. For families and individuals who do want to become homeowners, however, the federal government could more effectively target its assistance by making it easier to save for a down payment.

### **What is the solution?**

Smart Growth America recommends Congress establish individual mortgage savings accounts.

This optional tool would direct an individual's pre-tax contributions into a savings account established for this purpose. Individuals would be required to use the money in the account within 10 years of the account being established and any amount that is not expended on eligible home purchase costs or on December 31 of the last year of the 10-year period would be taxed as ordinary income.

With individual mortgage savings accounts, the federal government could incentivize potential homebuyers to begin saving for homeownership. However, these savings accounts and their tax status should be very clearly limited to first-time homeownership.

We estimate a significant increase in first-time homebuyer purchases, and an average annual cost of \$1 billion over the first 10 years.<sup>37</sup>

### **How will this change meet the guiding principles for reform?**

Saving for a down payment can be challenging but it can bring benefits for families and their broader community. By providing additional tools to help Americans with their first down payment, we will be helping more families reach the middle class.

### **Montana's first-time homebuyer savings accounts**

This recommendation is based on a similar tool already available in the State of Montana. Montana's First-Time Homebuyer Savings Accounts can be opened at a bank, savings and loan or credit union, and the money placed in the account is not subject to state income tax. Money in the account must be used by the tenth year following the year in which the account was established. Withdrawals for any purpose other than eligible first-time home buyer expenses are treated as ordinary income and taxed accordingly at the state level.<sup>36</sup>



Mortgage savings accounts would make it easier for families to save for the down payment on their first home.

## 7. Create an Innovative Financing for Infrastructure Rehabilitation Program.

Infill development—redeveloping land within existing communities—generates an average of 10 times the revenue of conventional suburban development, can create neighborhoods that are economically strong and benefit municipalities financially.<sup>38</sup> But significant hurdles can stand in the way: deteriorating roads, transit systems, water and sewer lines, power distribution and other infrastructure challenges. These problems are often the result of decades of under-investment in or deferred maintenance of infrastructure, and the price tag to fix these issues often far exceeds the money available from federal, state and local sources combined.

### Why take action?

Local governments often attempt to get private-sector developers to fund infrastructure fixes by requiring them as part of infill development proposals. However the costs of these improvements can make the projects financially unfeasible for developers. Infill development typically costs around \$163 to \$191 per square foot,<sup>39</sup> whereas conventional suburban development costs an average of \$100 to \$132 per square foot. These higher expenses and the fact that many of infill’s costs are front-loaded can make financing a major barrier for these projects. As a result, many projects that would provide significant fiscal benefits and private-sector funds for public infrastructure renewal are never built.

Upfront loans for infrastructure repairs would make infill projects more financially feasible for developers, and help communities reap the benefits that requirements alone cannot always achieve.

### What is the solution?

Smart Growth America recommends Congress create an Innovative Financing for Infrastructure Rehabilitation Program to help developers meet upfront infrastructure costs. Modeled after the Transportation Infrastructure Finance and Innovation Act (TIFIA), such a program would provide low interest loans, loan guarantees or other credit for smaller scale projects (i.e., projects under \$50 million) funded through the Department of Treasury. Value created from new development would pay back loans over time with interest.

As with any loan program, funding for an Innovative Financing for Infrastructure Rehabilitation Program would be paid back.



Eligible expenses for such a program would be limited to rehabilitation of existing infrastructure to facilitate redevelopment of previously developed sites, including: demolition of vacant buildings; earthwork construction, including the clearing and grubbing, scalping, and removal of existing structures and obstructions;<sup>40</sup> site utilities, including improving, upgrading or providing new infrastructure or rehabilitating existing, or providing new infrastructure for drinking water, wastewater, electric and gas utilities; roads and walks, including connecting the gaps in existing streets and sidewalks; decontaminating land; lawns and planting, including environmental remediation and infill park development; and hard costs of accessory use parking, including construction of off-street structured parking facilities and building parking replacement.

Additionally, to ensure Americans have balanced housing choices, we recommend requiring projects that use this tool include a minimum of 15 percent workforce housing as defined by individual states. And to support investment in existing neighborhoods, we recommend requiring projects to be within rural community centers or one-half mile of an existing or planned major transit facility.

As with any loan program, funding for an Innovative Financing for Infrastructure Rehabilitation Program would be paid back. By encouraging developers to address infrastructure needs, this program comes with another benefit: relieving the federal government of these repair costs. Smart Growth America recommends an annual authorization of \$500 million for this program.

### **How will this change meet the guiding principles for reform?**

An Innovative Financing for Infrastructure Rehabilitation Program would spur direct reinvestment in existing neighborhoods and help address existing communities' infrastructure maintenance backlog by bringing private-sector funding to the problem. Additionally, policymakers would ensure Americans have balanced housing choices by addressing the current gap in affordable workforce housing.

## Conclusion

The current shortcomings of federal real estate programs are costing families, communities and ultimately taxpayers.

Refocusing these programs could save the federal government billions of dollars. As Congress looks for ways to streamline and maximize federal spending, now is a crucial time to make these reforms.

Creating a wider array of housing choices for families, supporting America's neighborhoods, providing a safety net for and growing the middle class are the reasons the federal government is involved in real estate. Our recommendations are designed to make programs more efficient and effective at achieving these goals.

Improving these programs goes beyond individual families or the federal budget. When done well, development can strengthen entire regions and better federal investments are a key part of realizing that potential. Cities and towns across the country recognize the benefits of better development strategies and they are using federal programs to accomplish that. We can make this important work easier for a greater number of communities by changing how federal real estate programs are structured.

This set of recommendations is just a starting point. More must be done to ensure that federal programs on real estate are meeting our national needs, strengthening communities and providing economic opportunity. But the time to act is now.

Federal real estate programs have the potential to help families grow more prosperous, create economically resilient communities and get a strong return on taxpayer investment at the same time. It's time for Congress to rethink real estate.

Development can strengthen entire regions and better federal investments are a key part of realizing that potential.

## Learn more

Visit [smartgrowthamerica.org/federal-real-estate](https://smartgrowthamerica.org/federal-real-estate) to learn more about these recommendations and to take action.

## Endnotes

- <sup>1</sup> Smart Growth America. (2013, January). *Federal Involvement in Real Estate: A Call for Examination*. Retrieved June 28, 2013, from [www.smartgrowthamerica.org/documents/federal-involvement-in-real-estate.pdf](http://www.smartgrowthamerica.org/documents/federal-involvement-in-real-estate.pdf).
- <sup>2</sup> National Association of Realtors. (2011, March 18). *The 2011 Community Preference Survey: What Americans are looking for when deciding where to live*. Retrieved December 7, 2012, from [www.realtor.org/reports/2011-community-preference-survey](http://www.realtor.org/reports/2011-community-preference-survey).
- <sup>3</sup> Robert Charles Lesser & Co. (2008, January). "Measuring the Market for Green Residential Development." Retrieved December 27, 2012, from [www.rclco.com/pdf/Measuring\\_the\\_Market.pdf](http://www.rclco.com/pdf/Measuring_the_Market.pdf).
- <sup>4</sup> Smart Growth America. (2013, May). *Building Better Budgets: A National Examination of the Fiscal Benefits of Smart Growth Development*. Retrieved May 21, 2013, from [www.smartgrowthamerica.org/building-better-budgets](http://www.smartgrowthamerica.org/building-better-budgets).
- <sup>5</sup> National Flood Insurance Program. About the National Flood Insurance Program. Retrieved June 28, 2013, from [www.floodsmart.gov/floodsmart/pages/about/nfip\\_overview.jsp](http://www.floodsmart.gov/floodsmart/pages/about/nfip_overview.jsp).
- <sup>6</sup> King, R. O. (2012, December). The National Flood Insurance Program: Status and Remaining Issues for Congress. Congressional Research Service. Retrieved May 30, 2013, from [www.fas.org/sgp/crs/misc/R42850.pdf](http://www.fas.org/sgp/crs/misc/R42850.pdf).
- <sup>7</sup> Third Way. (2011, September 15). Third Way's Bipartisan Savings Package for the Joint Select Committee on Deficit Reduction. Retrieved June 28, 2013, from [content.thirdway.org/publications/442/Third\\_Way\\_Letter\\_-\\_Deficit\\_Reduction\\_Recommendations\\_to\\_Super\\_Committee\\_.pdf](http://content.thirdway.org/publications/442/Third_Way_Letter_-_Deficit_Reduction_Recommendations_to_Super_Committee_.pdf).
- <sup>8</sup> House Committee on Financial Services. (2013, February 6). FHA: The Need to Scale Back Their Market Share. Retrieved May 10, 2013, from [financialservices.house.gov/uploadedfiles/hhrg-113-ba00-wstate-asanders-20130206.pdf](http://financialservices.house.gov/uploadedfiles/hhrg-113-ba00-wstate-asanders-20130206.pdf).
- <sup>9</sup> The traditional FHA loan limit is 87 percent of the Government Sponsored Enterprises loan limit. See: The George Washington University School of Business. (2011, June). FHA Assessment Report. Retrieved July 1, 2013, from [http://nationalmortgageprofessional.com/sites/default/files/GWU\\_Study\\_06\\_30\\_11.pdf](http://nationalmortgageprofessional.com/sites/default/files/GWU_Study_06_30_11.pdf).
- <sup>10</sup> H.R. 4264 (112th): FHA Emergency Fiscal Solvency Act of 2012. Retrieved June 28, 2013, from [www.govtrack.us/congress/bills/112/hr4264](http://www.govtrack.us/congress/bills/112/hr4264).
- <sup>11</sup> Congressional Budget Office. (2010, May 6). Cost Estimate: H.R. 5072, FHA Reform Act of 2010. Retrieved May 29, 2013, from [www.cbo.gov/sites/default/files/cbofiles/ftpdocs/114xx/doc11488/hr5072.pdf](http://www.cbo.gov/sites/default/files/cbofiles/ftpdocs/114xx/doc11488/hr5072.pdf).
- <sup>12</sup> Joint Committee on Taxation. (2013, February). Estimates Of Federal Tax Expenditures For Fiscal Years 2012-2017. Retrieved May 30, 2013, from [www.jct.gov/publications.html?func=startdown&id=4503](http://www.jct.gov/publications.html?func=startdown&id=4503).
- <sup>13</sup> Joint Committee on Taxation. (2013, April). "Present Law, Data, And Analysis Relating To Tax Incentives For Residential Real Estate." Retrieved June 28, 2013, from [www.jct.gov/publications.html?func=startdown&id=4516](http://www.jct.gov/publications.html?func=startdown&id=4516).
- <sup>14</sup> Center for Budget Policy and Priorities. (2013, April 4). Mortgage Interest Deduction is Ripe for Reform. Retrieved May 10, 2013, from [www.cbpp.org/cms/?fa=view&id=3948](http://www.cbpp.org/cms/?fa=view&id=3948).
- <sup>15</sup> *Ibid.*
- <sup>16</sup> Congressional Budget Office. (2008, February). The Deductibility of State and Local Taxes. Retrieved June 11, 2013 from [cbo.gov/sites/default/files/cbofiles/ftpdocs/88xx/doc8843/02-20-state\\_local\\_tax.pdf](http://cbo.gov/sites/default/files/cbofiles/ftpdocs/88xx/doc8843/02-20-state_local_tax.pdf).
- <sup>17</sup> These recommendations are similar to those proposed by the National Commission on Fiscal Responsibility and Reform. See: The National Commission on Fiscal Responsibility and Reform. (2010, December). The Moment of Truth. Retrieved July 1, 2013, from [http://www.fiscal-commission.gov/sites/fiscalcommission.gov/files/documents/TheMomentofTruth12\\_1\\_2010.pdf](http://www.fiscal-commission.gov/sites/fiscalcommission.gov/files/documents/TheMomentofTruth12_1_2010.pdf).
- <sup>18</sup> Katz, B. (2012, November). "Cut To Invest: Reform The Mortgage Interest Deduction To Invest In Innovation And Advanced Industries." The Brookings Institution. Retrieved May 30, 2013, from [www.brookings.edu/~media/research/files/papers/2012/12/06\\_federalism/06\\_mortgage\\_interest\\_deduction.pdf](http://www.brookings.edu/~media/research/files/papers/2012/12/06_federalism/06_mortgage_interest_deduction.pdf).
- <sup>19</sup> Center for Budget Policy and Priorities. (2013, April 4). Mortgage Interest Deduction is Ripe for Reform. Retrieved May 10, 2013, from [www.cbpp.org/cms/?fa=view&id=3948](http://www.cbpp.org/cms/?fa=view&id=3948).
- <sup>20</sup> Joint Center for Housing Studies of Harvard University. (2012, June 14). The State of the Nation's Housing 2012. Retrieved October 31, 2012, from [www.jchs.harvard.edu/research/publications/state-nation's-housing-2012](http://www.jchs.harvard.edu/research/publications/state-nation's-housing-2012).
- <sup>21</sup> Joint Center for Housing Studies of Harvard University. (2011, April). America's Rental Housing: Meeting Challenges, Building Opportunities. Retrieved January 4, 2013, from [www.jchs.harvard.edu/sites/jchs.harvard.edu/files/americasrentalhousing-2011-bw.pdf](http://www.jchs.harvard.edu/sites/jchs.harvard.edu/files/americasrentalhousing-2011-bw.pdf).
- <sup>22</sup> *Ibid.*
- <sup>23</sup> *Ibid.*
- <sup>24</sup> "Very-low-income" households are defined as those earning between 30 and 50 percent area median income.
- <sup>25</sup> Joint Center for Housing Studies of Harvard University. (2011, April). America's Rental Housing: Meeting Challenges, Building Opportunities. Retrieved January 4, 2013, from [www.jchs.harvard.edu/sites/jchs.harvard.edu/files/americasrentalhousing-2011-bw.pdf](http://www.jchs.harvard.edu/sites/jchs.harvard.edu/files/americasrentalhousing-2011-bw.pdf).



- <sup>26</sup> Enterprise Community Partners. (2012, July 20). Issue Background: Low-Income Housing Tax Credit. Retrieved October 31, 2012, from [www.enterprisecommunity.com/low-income-housing-tax-credits-policy](http://www.enterprisecommunity.com/low-income-housing-tax-credits-policy).
- <sup>27</sup> Enterprise Community Partners. (2012, July 20). Issue Background: Low-Income Housing Tax Credit. Retrieved June 28, 2013, from <http://www.enterprisecommunity.com/low-income-housing-tax-credits-policy>.
- <sup>28</sup> The recommendations on a fixed minimum credit rate and a fixed floor rate for the acquisition credit are similar to ones proposed by the National Low Income Housing Coalition and Enterprise Community Partners. See, for example: Enterprise Community Partners. (2012, July 20). Issue Background: Low-Income Housing Tax Credit. Retrieved July 1, 2013, from <http://www.enterprisecommunity.com/low-income-housing-tax-credits-policy>.
- <sup>29</sup> *Ibid.*
- <sup>30</sup> This recommendation is similar to one proposed by the Bipartisan Policy Center. See: Bipartisan Policy Center. (2013, February). Housing America's Future: New Directions for National Policy. Retrieved July 1, 2013, from [http://bipartisanpolicy.org/sites/default/files/BPC\\_Housing%20Report\\_web\\_0.pdf](http://bipartisanpolicy.org/sites/default/files/BPC_Housing%20Report_web_0.pdf).
- <sup>31</sup> *Ibid.*
- <sup>32</sup> Smart Growth America. (2013, May). *Building Better Budgets: A National Examination of the Fiscal Benefits of Smart Growth Development*. Retrieved May 21, 2013, from [www.smartgrowthamerica.org/building-better-budgets](http://www.smartgrowthamerica.org/building-better-budgets).
- <sup>33</sup> The recommendation on new age criteria is similar to one proposed by the National Trust for Historic Preservation. See: National Trust for Historic Preservation. (n.d.). The Creating American Prosperity Through Preservation (CAPP) Act. Retrieved July 1, 2013, from <http://www.preservationnation.org/take-action/advocacy-center/additional-resources/historic-tax-credit-maps/CAPP-Facts-FINAL.pdf>.
- <sup>34</sup> Joint Center on Housing Studies at Harvard University. (2012, June 14). The State of the Nation's Housing 2012. Retrieved March 12, 2013, from [www.jchs.harvard.edu/sites/jchs.harvard.edu/files/son2012.pdf](http://www.jchs.harvard.edu/sites/jchs.harvard.edu/files/son2012.pdf)
- <sup>35</sup> *Ibid.*
- <sup>36</sup> Montana State University Extension. (2013, April). First-time Home Buyer Savings Account. Retrieved June 28, 2013, from [msuextension.org/publications/FamilyFinancialManagement/MT199918HR.pdf](http://msuextension.org/publications/FamilyFinancialManagement/MT199918HR.pdf).
- <sup>37</sup> We assumed eligible participants are below the age of 55 and over 16, with an average of 10 percent participation rate over 10 year period.
- <sup>38</sup> Smart Growth America. (2013, May). *Building Better Budgets: A National Examination of the Fiscal Benefits of Smart Growth Development*. Retrieved May 21, 2013, from [www.smartgrowthamerica.org/building-better-budgets](http://www.smartgrowthamerica.org/building-better-budgets).
- <sup>39</sup> Michigan Suburbs Alliance. (2012). The Climate Strategies Library: Infill Development. Retrieved May 24, 2013, from [www.michigansuburb-salliance.org/wp-content/uploads/MSA-CAP-Strategy-Library\\_Infill-Development\\_20121017.pdf](http://www.michigansuburb-salliance.org/wp-content/uploads/MSA-CAP-Strategy-Library_Infill-Development_20121017.pdf).
- <sup>40</sup> Other earthwork construction costs that tend to be higher for infill projects include the preparation of foundations and embankments, disposal of excavated material, borrow excavation, preparation of sub-grade, proof rolling and placement of granular sub-base and base courses, structure of backfills and instrumentation.



**Smart Growth America**

Making Neighborhoods Great Together

Smart Growth America advocates for people who want to live and work in great neighborhoods. We believe smart growth solutions support thriving businesses and jobs, provide more options for how people get around and make it more affordable to live near work and the grocery store. Our coalition works with communities to fight sprawl and save money. We are making America's neighborhoods great together.

Smart Growth America is the only national organization dedicated to researching, advocating for and leading coalitions to bring smart growth practices to more communities nationwide. Visit us online at [www.smartgrowthamerica.org](http://www.smartgrowthamerica.org).

1707 L St. NW Suite 250, Washington, DC 20036

202-207-3355

**[www.smartgrowthamerica.org](http://www.smartgrowthamerica.org)**