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Cracks in a Pillar of Affordable Housing

William N. Hubbard at a Center Development Corporation complex in the Bronx where the government supplements tenants' rent payments.

Some landlords opt out of Section 8 as the government seeks to limit the costs.

By DENNIS HEVESI

WITH contracts covering 62,000 rent-subsidized apartments in the tristate region coming up for renewal in the next year, and some landlords wondering whether the time is right to take their buildings onto the open market, a linchpin of the New York area's already strained affordable housing structure -- the Federal Section 8 program -- is wiggling.

For decades, Section 8 -- a program guaranteeing landlords a modest profit for housing low-income people, with the government paying the difference between 30 percent of a tenant's income and the rent -- has been a pillar of housing for the poor. The landlords, however, are entitled to opt out of the program when their contracts expire, and then to rent the apartments at full market rates. So as the fortunes of various neighborhoods have brightened in recent years, buildings have been lost to the program.

While no one foresees a mass exodus of the landlords, who are also being buffeted by Washington-mandated efforts to trim costs, housing advocates say that any loss of Section 8 apartments leaves irreparable holes in society's safety net.

For nearly 25 years, William N. Hubbard has balanced the business interests of being a landlord with a commitment to be of service to the poor. He owns 10 apartment complexes housing 1,500 families whose rents are subsidized through the United States Department of Housing and Urban Development.

Now that sense of responsibility is being tested -- first, by a real estate market in which improving neighborhoods offer the possibility of higher profits, and then by what Mr. Hubbard and other landlords experience as a bureaucratic morass. The red-tape tangle stems from Congressional efforts to cut costs while, at the same time, carefully choosing which landlords to entice into staying in the program.

The push-pull, Mr. Hubbard said, "is demoralizing dedicated people who have worked in this field day to day for years."

As hundreds of 15- and 20-year Section 8 contracts expire, owners in rejuvenated neighborhoods must weigh whether to opt out and go on the market.

At the same time, there is a flip side to that situation: in still-depressed neighborhoods where, two decades ago, the government found it necessary to subsidize rents at levels insuring that the owners' construction and mortgage costs would be covered -- guaranteeing a limited but consistent profit -- Congressional directives to bring those rents down to current market rates are leaving many landlords feeling betrayed.

Mr. Hubbard finds himself struggling with the paperwork required to justify costs for eight of his properties while he also considers taking two others out of the program. "I've elected to renew two of the developments for five years, in order to avoid having to face this decision," he said.

Peter J. Alizio is the managing agent for five Section 8 buildings with 600 apartments in Far Rockaway and Astoria, Queens, that are owned by small groups of investors. "The owners feel good about providing nice housing for poor families, but they also have a lot of frustration with the burdens put upon them by the government," Mr. Alizio said.

"I literally have tenant files that are as deep as they are wide; 3,000 square feet of office space, most of it file cabinets," he said. "Some of my owners are seriously considering the pros and cons of withdrawing."

Officials of the Department of Housing and Urban Development say that, so far at least, the number of landlords who have opted out of the program -- about 2 percent of those eligible nationally and 4 percent in the New York area -- has been manageable. And they point out that the bureaucratic burden on the owners results from the Congressional mandate to rein in the burgeoning costs of contract renewals, while also carefully calculating which landlords are eligible for rent incentives to renew their contracts.

"I am sympathetic to the burdens and concerns," said John C. Weicher, the assistant housing secretary for HUD and commissioner of the Federal Housing Administration. "The landlord who has been in the program for 20 years has seen a respectable amount of paperwork."

"But we do have a responsibility not to pay more than we need to or are allowed to," Dr. Weicher continued. "We are tasked with keeping track of the money Congress has appropriated, and we do."

Housing advocates are concerned.

Victor Bach, director of housing policy and research at the Community Service Society, a nonprofit antipoverty organization, conceded that, so far, Section 8 losses have been contained. Still, Dr. Bach worries that the potential loss "of thousands of units in New York's tight and unaffordable rental market is significant, and it ought to be prevented." In all, the program assists 175,000 families in New York, New Jersey and Connecticut, most with annual incomes of less than $10,000.

The Section 8 program, an amendment to the 1937 United States Housing Act, was adopted by Congress in 1974. It actually has two components. In one, low-income people directly receive government rent vouchers and then go into the community to find housing on their own. In the other, called project-based Section 8, the government contracts with developers who build or rehabilitate housing for poor people with a guarantee that their costs and a reasonable profit will be covered by the rent.

At its peak in the early 90's, there were 1.7 million tenants in the voucher program across the nation and 1.5 million in the project-based program.

By 1975, the first project-based units -- most with 20-year contracts -- were under construction. And so, starting in 1995, those contracts began expiring, with the opt-out possibilities increasing year by year since then.

The federal subsidies agreed to in the project-based contracts were based on a formula called the Fair Market Rent -- and there's the rub.

AS Shaun Donovan, who during the Clinton administration was deputy assistant secretary for multifamily housing at HUD, put it, "The joke within housing circles was that the Fair Market Rent was like the Holy Roman Empire -- it wasn't holy and it wasn't Roman."

' 'Essentially, it was impossible to calculate," Mr. Donovan said. "It's like somebody asking you, 'What's the market rent for New York City?' Obviously, there is no single market rent for New York City. So, at best, these were estimates for large areas."

In some communities -- Mr. Donovan cited the South Bronx as an example -- the market-rate rents were so low at the time the contracts were signed that they could not support the construction of new housing. So the rent subsidies were set at higher levels.

But in 1997 -- in its first major effort to deal with the coming renewal crunch -- Congress passed legislation requiring that all rents in the project-based program be brought down to local market rates. "Everyone was screaming about the huge cost of Section 8 renewals to the government," Mr. Donovan said, "and the basic Congressional directive was to no longer pay more than true market."

There are complications to that simple directive.

The above-market rents, in most cases, pay off loans to owners who would default if the rents were lowered. And many of those loans are insured by the Federal Housing Administration. "That would mean the taxpayer paying off the loans and the government having to take over the properties and sell them at auction," Mr. Donovan said.

The result was the Mark to Market Program, which might more precisely be dubbed Mark Down to Market.

Under Mark to Market, rents would no longer be based on the Fair Market Rent formula, but on property appraisals paid for by the landlords, based on "comparables" in the community and even on the block. For properties where the government had insured the owners' mortgages, the government would also reduce the loan burden through payments to the bank.

Despite that accommodation, many landlords are troubled. "Owners are completely unhappy with the program," said Mr. Donovan, who is now a research fellow at the New York University Law School's Center for Real Estate and Urban Policy. "Fundamentally, what the government is saying to them is: 'Build housing for low-income families; we will sign a contract with you to pay a rent that supports a decent return for you.' And 20 years later, the government comes back and changes the terms of the deal."

Having been on the official side of the bargain, Mr. Donovan points out that the government's position is that the deal was for 20 years, the government lived up to the terms and the owner, like any developer, took a risk. Landlords in those still-depressed neighborhoods, however, are finding their properties reduced in value, he said, "and because many owners manage their properties, their management fees and other fees are also being reduced."

Mr. Hubbard, whose company, the Center Development Corporation, owns buildings in the Bronx, Harlem and the East Village, pointed out that a two-bedroom apartment in a 160-unit building on Garrison Avenue in Hunts Point, the Bronx, had rented for $1,470, with Section 8 subsidies. Under Mark to Market, the new rent will be $850.

On top of that, there is the paperwork maze -- not just for the new appraisals, but for a myriad of cost-cutting initiatives requiring owners to justify their operating expenses. "To meet the requirements of Mark to Market we have been told to significantly reduce costs," Mr. Hubbard said, "and if we don't comply we face having the subsidies eliminated and defaulting on the mortgage."

Section 8 landlords are now "embroiled in a paperwork nightmare," he said, "trying to restructure mortgages all over the city based on 'comparable rents' -- reports, authorizations, project histories, reviews of service contracts, commercial leases, utility bills, property tax assessments, insurance policies, evaluation of physical conditions. It's driving people crazy."

An irony of Mark to Market, however, is that because of heated rental markets in many neighborhoods since the program's inception, far fewer Section 8 projects than anticipated now collect rents that are higher than those in their communities.

"You can imagine this dynamic," Mr. Donovan said, "where if you have a Section 8 project in Manhattan below 96th Street there's immense pressure on owners to take their properties out of the program and convert them to market to get higher rent."

Mr. Hubbard is one of those owners. "It's ironic," he said, "but when we began in the East Village, part of our objective was to help upgrade the neighborhood. Very few people could envision how the developments would unfold over two decades."

"The ideal of a mixed-use, mixed-income community, similar in some respects to the West Village, was certainly a consideration," he said. "Now the East Village has blossomed. It was never contemplated that the pioneers would be displaced."

Currently, about half of the Section 8 units in the country are in communities where the market-rate rent is higher than what is allowed under the program. And the number of projects coming up for contract renewal is increasing.

Nationally, according to HUD data, there are 1.3 million Section 8 units under contract. During the 2002 fiscal year, which for the federal government started on Oct. 1, about 507,000 of those units will come up for renewal, with an additional 396,000 coming due during the following three years.

In the tristate area, 61,900 units come up for renewal during the current fiscal year, with another 51,400 during the following three years. And in New York City and its nearby suburbs, taken alone, 27,000 units come due this year, and 21,000 more by the end of 2005.

In 1999, to deal with the expiration problem, HUD devised a counterpart to the Mark to Market program -- Mark Up to Market -- providing rent incentives for landlords to renew their contracts.

' 'The problem is that raising the rents of all the properties up to market would have cost $600 million to $800 million a year," Mr. Donovan said, "and Congress didn't provide the money."

HUD had to decide which projects to focus on. "We ended up picking properties that were in the hottest real estate markets, or which had the most vulnerable residents," Mr. Donovan said, "the elderly, the disabled, large families."

Before Mark Up to Market, the rate of opt-outs for all contracts coming up for renewal was about 4 percent; since then, the rate has dropped by nearly half. Dr. Weicher, HUD's current assistant secretary for housing, said, "In terms of the magnitude of the possible problem, we've had, in the last four years, between 2 and 2.5 percent of the inventory opting out." That, he said, is out of a national inventory of 1.3 million units. In the metropolitan area, 2,060 units, or 4.1 percent of the inventory of about 50,000 units, have opted out since 1996

' 'The potential is there for a problem," Dr. Weicher said, "but it hasn't developed."

But any measurable loss of inventory for poor people in the metropolitan area -- and particularly in the city -- is of consequence, housing specialists say.

David Buchwalter, president of AdCar Associates, a consulting service for owners and managers of HUD-related housing, does not see the surge in contract renewals as a crisis, but "clearly a matter of concern."

"We've handled 120 renewals of which five were opt outs," Mr. Buchwalter said. "That's 578 units that opted out."

"How representative that is I don't know," he said. "But the project-based Section 8 program is an invaluable resource for a segment of the population that doesn't have much choice for housing, and any loss of that housing is something to worry about."

According to the 2000 census, the vacancy rate for rental housing in New York City fell by almost 1 percentage point during the 1990's, from 4.14 percent to 3.24 percent -- with anything less than 5 percent deemed a housing emergency, according to city and state law. And the tight housing market has led to rapidly rising rents. According to the 1999 New York City Housing and Vacancy Survey, 24.3 percent of all renters pay more than half their incomes in rent.

"The vast majority of these families with crushing rent burdens have low incomes and are just the people for whom Section 8 housing was targeted," said Michael Schill, director of the N.Y.U. Law School's real estate center. "Therefore, the continuing loss of Section 8 housing would make a bad situation even worse."

The government is trying to contain the problem. Nearly half of HUD's $30 billion budget request to Congress for the 2002 fiscal year (the department is currently operating at last year's allocation level) is designated for contract renewals. And Dr. Weicher, HUD's assistant housing secretary, said that the Bush administration "committed early in the year to continue the same process that was established in earlier administrations."

Dr. Weicher also pointed out that there are safeguards in place for tenants who already live in Section 8 buildings. "If a landlord chooses to opt out, we protect the tenants with enhanced vouchers, which makes them able to pay the market rent in the apartment they are already living in, or to take the voucher to any other rental housing within the area," he said. Under enhanced vouchers, the government pays the difference between 30 percent of the tenant's income and the market-rate rent being charged by the owner who has opted out.

BUT that can be a costly alternative. "When an owner doesn't renew and the rents go to market," said Michael Bodaken, president of the National Housing Trust, a nonprofit affordable housing preservation group, "the average rent hike for those that we've been able to track nationally is over 40 percent."

One Section 8 landlord, who spoke only on condition of not being identified, said a two-bedroom apartment in one of his buildings in lower Manhattan was receiving a HUD-subsidized rent of $1,450, but an appraisal indicated that he could charge $2,100 if he opted out of the program.

"Enhanced vouchers are a good mechanism for the individual or family in the short run," Mr. Bodaken said. "But in the long run, vouchers don't protect the affordability of the stock itself."

Dr. Bach at the Community Service Society concurred, saying, "I am concerned about the loss of brick-and-mortar housing resources accessible to low-income families who want to apply for either kind of Section 8." When poor families eventually leave what used to be a Section 8 building, their apartments are lost to the program.

"The stock is eroding," Dr. Bach said. And poor people, even with a voucher in hand, already have a difficult time finding shelter.

Jose Cruz knows that too well.

For seven years, Mr. Cruz, 44, lived in a one-bedroom apartment on West 95th Street; he moved out last December. "The rent went from $349 to $600 in three years," he said. "I'm on disability and I only get $611 a month for food, clothing, everything."

Mr. Cruz is now renting a room from a friend on the East Side. But the friend's roommate is soon to return from a job out of town. "I reported to Section 8 at the Housing Authority," Mr. Cruz said.

For two months, voucher in hand, he has been looking for an apartments.

"I called about 50 brokers," Mr. Cruz said. "They tell me they either don't have anything or they don't take Section 8. I'm very aggravated and worried that I'm not going to find anything. It is very scary."