Lexington's Affordable Housing Challenge and Potential Strategy
February 2014

czb for the City of Lexington, KY

czb

Executive Summary

Because of a great deal of hard work, Lexington, Kentucky is in the midst of a prosperous economic expansion. High wage jobs are being created. Businesses are locating to Lexington. Quality of life in Lexington is high. Moreover, Lexington remains a very affordable place to live with great housing choices at exceptionally good prices across most of the housing spectrum.

Since 2000, however, as Lexington has shifted to a more high-tech, service-oriented, new economy, the demand for high skilled workers has grown. With that, the cohort of Lexington workers with higher incomes has also grown.

While in the years ahead, Lexington will need to pay more attention to the challenges of affordable home ownership, today's real housing challenge is that there are too few apartments affordable to low income families, and that Lexington has a lot of low and very low income workers.

One important result of rising incomes is rising housing costs.

As more households have more to spend on housing, prices rise. And if overall demand rises as well - which has been the case - housing price escalation becomes even sharper. For Lexington, this means a two-part narrative has been taking shape the last decade.

For households making $40,000 or more a year, Lexington offers great value: extraordinarily high quality of life, amenities, and housing opportunities. For low wage earners (making less than $30,000), the opposite is true: fewer and fewer affordable housing opportunities and often substandard conditions in what remains affordable.

Indeed, in the last two decades, local rents have risen to such a degree that more than 28,000 apartment units in Lexington that were affordable to low-wage workers are no longer within reach.

So long as Lexington continues to grow economically, these housing trends - specifically a decreasing supply of affordable rental housing - will continue.

The magnitude of this problem is significant, and that is <u>*after* discounting for students</u>. Roughly 15,000 low-income households need housing assistance in Lexington today. Of them, about 9,000 now receive assistance or are accommodated by the private market. This leaves about 6,000 households, most of whom include at least one worker, that cannot find decent housing on the open market in Lexington at rates considered affordable (equal or less than 30% of their gross income). Consequently, these 6,000 working households either overpay or live in substandard or overcrowded conditions. When households overpay, the Lexington economy is deprived spending, costing Lexington valuable revenue. When households - whether overpaying or not - have no choice but to live in substandard or overcrowded conditions, Lexington's tax base suffers, and neighborhoods become less stable.

Also, this problem is likely to become more significant going forward. It is probably the case that the Lexington market will shed an additional 400 affordable rental units (on average) in each of the coming years.

If the Mayor and City Council want to do something about this problem, it is important to start with an understanding of the roots of this problem, of which there are two.

- **PRICE OF SUCCESS.** First, recent changes in the Lexington economy to one requiring more skills and education is at the center of today's affordability challenges. Think of this as a cost of becoming an increasingly competitive and prosperous city. Had Lexington gone more in the direction of St. Louis and Cincinnati (becoming weaker) instead of tracking with Raleigh and Chattanooga and Oakland and Albuquerque (becoming stronger), resulting and persistent soft market conditions would have meant cheaper housing. Buffalo and Detroit and Trenton remain cheap because too few businesses want to locate there and too few workers want to live there, and, consequently, demand is low, and prices reflect that. By contrast, Lexington is becoming more expensive - though still affordable to most - because the exact opposite is true. <u>This is a problem resulting from prosperity</u>. As Boulder and Seattle and Austin have discovered, addressing rising housing costs is a price of success.

- **STAGNATING WAGES FOR SOME.** Second, low-skilled workers' wages are not keeping pace. In Lexington there are thousands of poor residents in households who for generations have not been part of the mainstream economy. The majority of these households have been helped by federal programs, but the underlying situation has not changed much. <u>This is a legacy problem.</u> In this respect, Lexington resembles Durham, Richmond, Nashville, and Indianapolis – cities on the move in the right direction, <u>but with large portions of their working but low-income population unable to keep up</u>.

The recommended way to think about Lexington's <u>current affordability gap</u> – arising both from legacy on the one hand and as a prosperity consequence on the other – is as a problem that requires Lexington to **<u>catch up</u>**. That is, to close a gap that now (already) exists, a gap we estimate to consist of 6,000 households.

What about going forward?

In addition to the work of **<u>catching up</u>** (closing the current gap), the Lexington market will likely continue to become ever more expensive. That will likely result in an additional annual loss of another 400 affordable units. We project that by 2025, today's gap of 6,000 could become much larger. The way to think about the future affordability gap – arising from continued increases in prosperity and resulting housing price escalation – is as a problem that will require that Lexington **<u>keep up</u>** (*i.e.* not let the gap get any bigger than it already is).

Regardless of the pace that local housing prices have risen and will rise, the key underlying issue for the Mayor and City Council to come to terms with is that wages for low-skilled workers have not and will not keep pace with rising housing costs, and so there will be an affordability gap until they do. Furthermore, if this affordability gap for low-wage workers is not closed - for whatever reason - the problem is not one whose costs will simply go away. Rather, the costs will emerge in alternative form as declining neighborhood health, reduced tax base, higher crime and crime-fighting costs, higher demand for services and their costs, or commuting pressures and the costs of congestion, as well as air and water pollution. Housing affordability gaps are a "when" and "in what form" challenge, not an "if" problem.

WHAT IS THE SOLUTION? Affordability gaps can be closed in two basic ways: by reducing housing costs, or by increasing incomes. And they can be addressed through income subsidies on the demand side, or production efforts on the supply side. And, of course, all such approaches can be combined.

Most critical of all as regards a response - no matter how the gap is closed - is that the unit cost of addressing this problem will be roughly $6,000 per year per household. Whether as a rental subsidy of $500 per month (on average) per low-income working household, or as repayment of amortized debt taken on to construct new units, the per unit/per year scalable variable is $6,000.

Typical Low-Income Wage Earner HH in Lexington (based on a range of income earning possibilities and range of market rents)			
Annual Hours Worked (Range) (Average)	1,807		1,955
Hourly Wage (Average)		$7.25	
Monthly Gross Income (Average)	$1,092		$1,181
Affordable Rent (Average)	$328		$354
Market Rent 2+ BR Range (Average)	$723	$807	$860
Est. Annual Gap Range (Average)	$4,428	$5,436	$6,072
Est. Annual Mortgage Payment to Retire $75,000/unit Development Costs		$5,988	

For the sake of crafting policy, this $6,000 per year per household figure is the rounded multiplier that the community needs to understand. It is the multiplier that translates the problem of catching up completely to about $36M per year, (it is also the average annual cost to LHA in subsidies to a section 8 household. In addition, we project the cost of keeping up to be an amount that will grow by $2.4M annually thereafter until wages keep pace with housing prices.

This is a lot of money. The aggregate amount that Lexington employers pay in wages each year is roughly $5.7B, which works out to 6/10th of one percent of what's paid annually. While $36M a year *is a lot of money*, it is also a tiny fraction of the overall amount of wages paid, and is a form of employer cost shifting whereby employers pay a low wage, and the impacts of that low wage are paid for by everybody else in the form of higher taxes. Lexington's wage-housing cost gap is $36M a year of private gain at public expense, and this is growing by an additional $2.4 annually.

Beyond the scale of the problem is a capacity issue. *Even if the City "found" $36M+ a year to close these affordability gaps (regardless of where the money might come from), the Lexington housing system today is insufficient to the task; it does not have the capacity to implement a 6,000-unit program. Not today.*

To adequately address existing - and future - affordability gaps, Lexington needs both the financial resources to do so, and a system capable of implementing the strategies selected. Having neither at the present time, what is recommended is a scaled, two tiered approach.

First, It is recommended that the Mayor and Council set a goal of catching up within 11 years; that is completely closing today's gap of 6,000 units by steadily and persistently providing more rental subsidy to working families priced out of the market, and, when possible, through the development of new affordable units. Setting measurable, aggressive, and attainable goals of this kind is the hallmark of effective public policy. **Second, it is recommended that the Mayor and City Council aim to keep up thereafter**; that is, to add to the market the number of new affordable units each year needed to keep pace with continued price escalation.

To summarize, this work should be understood and described locally as having two vital parts: catching up (reducing the current 6,000 unit gap to 0) and keeping up. It should be based on our recommendation that the Mayor, Urban County Council and Planning Commission formally endorse a stated community objective that by 2025 any employee working in Lexington will be able to afford to live in Lexington.

1. **Most of the catching up should be done through the provision of rental subsidies attached to inspection requirements.** Working households in Lexington who are priced out of decent housing *are instead procuring substandard housing or paying too much for it, or sometimes both*. Catching up should be done by providing these households with rental vouchers. These vouchers - worth an average of $6,000 per year per household - would only be redeemable if the housing unit meets certain Lexington standards. This will have the immediate effect of triggering upgrades that will bring units into line with minimum standards, a direct result of which will be more stable property values and stronger neighborhoods. Most of the gap could be closed this way, given existing capacity that exists now and could be expanded at the Housing Authority (or other appropriate partners) to manage vouchers and property inspections. The balance could be closed through infill redevelopment.

2. **Keeping up (addressing the annual additional projected shortfall of 400 units) is best done through proactive planning measures that tap into and leverage the market.** Policies such as density bonuses, transfers of development rights, tax increment financing, and land banking all are proven tools for raising development revenue. For such tools to work, they need to be deeply embedded into Lexington's Comprehensive Plan, its Zoning and Development Codes, its Design Guidelines, its Small Area or Neighborhood Plans, its transportation policy, and its economic development strategy. Such explicit emphasis on affordable housing does not now exist in Lexington's guiding planning tools. The City of Lexington's Comprehensive Plan - new and exciting and visionary in many respects - should be revised to state that "*any employee working in the City of Lexington will be able to afford to live in Lexington*.

At its most basic, this is a $36M a year problem to solve. Lexington can get there in numerous ways - policy tools, development, rental subsidy - but it is a $36M a year problem, and, as noted *growing*.

czb recommends a *system-wide* response.

1 - **COORDINATION: Coordination of all housing-related matters by the Department of Planning, Preservation and Development.**

- In line with recommendations from the recent Homelessness Commission, <u>an Office of Homelessness Intervention and Prevention should be established</u> and reside in DPPD
  - While access to an affordable home is directly part of addressing homelessness, housing affordability as a line of preservation and development work is distinct from the essence of what this office would be tasked with, which is service coordination.
  - An Office of Homelessness Intervention and Prevention's principle function would be to focus on planning, coordination, advocacy, and awareness about the changing needs and gaps of services within Lexington.
  - In the recent Homeless Commission report, it is recommended that this office serve as an administrative agent of a housing trust fund (if created); czb does not endorse this specific recommendation. czb recommends that each year the Office of Homelessness Intervention and Prevention apply for resources from any future trust fund.
- <u>Housing-related programs now under the Office of Grants and Special Programs should be moved to DPPD</u>
  - Administration of ESG and other homeless-related grant programs should be shifted to a new Office of Homelessness Intervention and Prevention.
  - Current emphasis on affordable home ownership should shift to preservation and production of affordable rental housing.

2 - **FUNDING: Creation and funding of a <u>trust fund</u> for affordable housing** administrated by the Department of Planning, Preservation, and Development.

- Pre-arranged resources to address homelessness would flow to the Office of Homelessness Intervention and Prevention.
- Annual rental subsidies would be distributed to the Housing Authority (or other appropriate partners) acting as a subcontractor to DPPD
  - Oriented to address both households' cost burdens and housing units' physical condition. This will likely require collaboration between city code enforcement staff and rehabilitation specialists, and LHA staff currently overseeing the Section 8 program.
- DPPD would receive and evaluate affordable housing development proposals (from the private as well as nonprofit sectors) seeking trust funds

3 - **PLANNING: Changes should be made to current planning guidelines.**

- Changes should be made to current Planning and zoning regulations.
  - The Comprehensive Plan should include a stated community objective that by 2025 any employee working in the City of Lexington will able to afford to live in Lexington as the embodiment of the Comprehensive Plan[1]s vision for affordable housing in Lexington. This objective shall be used to point all policies in the same general direction of achieving top priorities.
  - Zoning and development regulations should be revised as necessary to achieve the community objective and drive resource generation. Alignment of the land use and development regulations towards the affordability challenge will result in result in reduced gaps and increased long term economic competitiveness.

One closing point must be made in this summary, and that is the issue of leverage.

Leverage should be thought of as the multiplier effect - the amount of additional resources brought to bear on a problem by an initial investment, resources that would otherwise not exist and which thus would have have been triggered, or *leveraged*. When a developer of affordable housing utilizes a federal tax credit to help finance a project, at some point they have to put their own money in the deal. Their own money is what leverages the tax credit; their own money is what leverages debt financing.

Right now, 15,000 non-student, low-income households need assistance in Lexington. They either don't have jobs or the jobs they have pay too little.

Presently, the United States federal government and the government of the Commonwealth of Kentucky are paying to help house 9,000 of these households. In fact, the federal and state share of this help is very nearly 100%.

<u>In effect, Lexington now benefits from a near infinite leverage ratio</u>, having put in close to zero dollars towards its affordable housing problem, and having the federal and state government pay nearly all of the tens of millions of dollars a year that is spent on current and legacy housing costs (all HUD costs for public housing, vouchers, and other assistance direct and indirect, averaged, since the 1937 construction of Bluegrass-Aspendale).

That leaves about 6,000 households without assistance; 6,000 primarily working households.

We estimate that future federal and state assistance for these 6,000 households will be nearly zero. **This means that if any assistance for these 6,000 households is to materialize, it will have to come from local sources almost exclusively.** On balance, over time, this probably works out to a leverage ratio of 1:1, or for every Lexington dollar committed to housing (provided all 15,000 households are assisted) it will have been matched by one non-Lexington dollar.

The Challenge

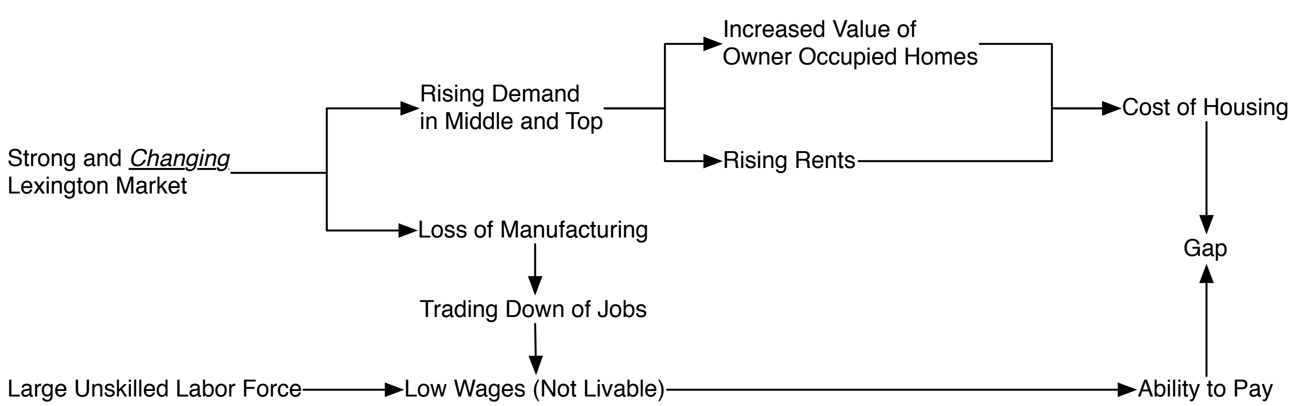
Lexington has a serious affordable housing problem. For tens of thousands of Lexington families, decent housing costs more than they can afford to pay. What's more, the Lexington market has all the signs of becoming even stronger in the years ahead. Therefore, the City must find ways to strike a balance through redevelopment: to preserve affordability and also manage and enhance neighborhood quality of life.

While in the years ahead, Lexington will need to pay more attention to the challenges of affordable home ownership, <u>today's real housing challenge is that there are too few apartments affordable to low income families, and that Lexington has a lot of low and very low income workers</u>.

What policymakers in Lexington need to be aware of is that the magnitude of the affordable rental housing problem is so acute that, at current production rates for low and moderate income working households, it would take an estimated 100 years to close existing deficits (to catch up). If the Lexington community is truly committed to addressing this problem - the costs of which the whole of Lexington already pays in the form of neighborhood distress, reduced tax receipts, and costly public services - it will have to come to terms with the fact that it is truly a big problem.

Housing advocates in Lexington have long known the problem is serious. Recent studies have confirmed that. Attempts have been made to create funding streams to address the problem, but so far major changes in the way Lexington handles this issue have not emerged. And, in the combination of Lexington's post-recession economic strength (boosting rents faster than wages for poor households could keep up) and the net loss of public housing units owing to Hope VI redevelopment, it is clear that this is a serious problem requiring a serious response

What are the root causes of Lexington's affordable housing challenge?



There are principally two: 1) **PROSPERITY**, or a strong market that is resulting in higher cost housing, and 2) **LEGACY**, a large unskilled labor force not earning livable wages owing mainly to lack of skills and education suited for the new economy Lexington has now moved fully into.

To elaborate, the reason that many Lexington households are not able to keep up with housing costs is that <u>the Lexington housing market - and the Lexington economy overall – is becoming stronger</u>.

As Lexington has become stronger economically –with the influx of employers, recovery from the recession, slight changes in the nature of the economy, and UK growth - the <u>demand for rental housing</u>

has increased, and as demand has increased, existing supplies have become more expensive. In addition, new development of rental properties has pushed rents higher.

Second, while the rental market has been growing in value, **wages paid for the jobs performed by Lexington's low-income earners have not kept pace either with rising housing costs or with wage gains made by others.**

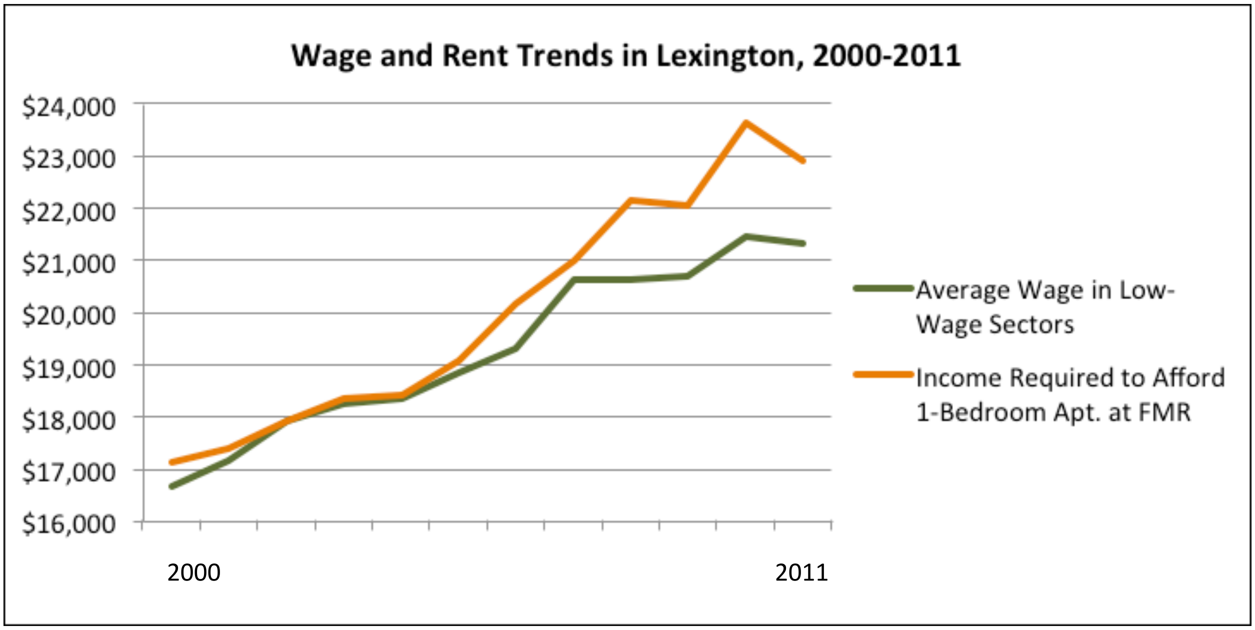
This in turn has two elements.

- One is that Lexington has a large number of poor families without the skills to compete for higher wages. In other words, while many poor Lexington families struggle to make a housing payment, the real underlying problem is not a housing problem but a structural workforce quality problem. As long as Lexington has a large underclass, it will have a large number of households with housing cost burdens; as long as this can is kicked down the road, these legacy costs will continue. Regarding workers in retail, arts and entertainment, educational services, and the food industry, wages from 1998-2011 rose just 36%. During that same period, wages for health care workers, finance, management, insurance, and other sectors rose between 60% and 80%. As workers in other fields have more purchasing power, they push rents up beyond what earners in jobs with more stagnant wages can afford. Adding to this is the loss of manufacturing jobs - a 54% decline from 1998-2011 - which means many trade down and obtain lower wages as they seek replacement employment.

Job Category	Average Hourly Wage	Average Annual Income (if Full-time)	Maximum Affordable Rent	Number of Employees
Accommodations and Food Services	$7.25	$15,080	$377	16,567
Educational Services	$11.42	$23,744	$594	2,762
Retail; Arts, Entertainment and Recreation	$11.59	$24,109	$603	21,627
Other Services	$13.33	$27,733	$693	15,445
All Jobs	$19.76	$41,104	$1,028	139,249

Sources: County Business Patterns, czbLLC.

- The result: typical wages in several lower-paying sectors are no longer "livable," *i.e.* not high enough to afford housing in Lexington's private housing market. This is a **structural** problem that stems from how the economy functions. From 2000-2004, the average wage in these low-wage sectors was consistently high enough to afford a 1-bedroom apartment in Lexington priced at Fair Market Rent. In 2005, however, a gap began to develop between the rent level affordable to the average wage for low wage work and the fair market rent for a 1-bedroom apartment. Since then, this gap has only grown: by 2011, households at the average wage in these sectors were about $130 short of affording this rent each month.



Sources: County Business Patterns, Department of Housing and Urban Development, czbLLC.

For a sense of scale: there are roughly 15,000 low-income, non-student households and now just 8,945 low-cost rentals to accommodate them – nearly twice as many households as rentals.

In 2000, nearly half (44%) the apartments with cash rents had gross rents below $500 per month – and were therefore affordable to households with incomes up to $20,000 (30% of the Area Median Income). By 2012, just 17% of apartments had rents below $500, and the number of apartments at this price range had fallen by more than half – from 20,238 in 2000 to 8,945 in 2012. **That year, nearly all (90%) of the city's renter households with incomes below $20,000 (the equivalent of a full time job at $10/hr) had unaffordable rents – paying more than 30% of their household income on rent.**

A significant number of these low-cost rental units (6,105 in all) are public or publicly subsidized units. Lexington has 1,365 public housing units and 2,046 Housing Choice Vouchers operated and overseen by LHA, and 2,694 privately-owned but publicly subsidized units, developed using monies from HUD's project based Section 8, Section 811, Section 202, Section 221 (D) (4), Section 236, and Section 221 (D) (3) BMIR programs; and the Low-Income Housing Tax Credit Program and the HOME Investment Partnerships Program.

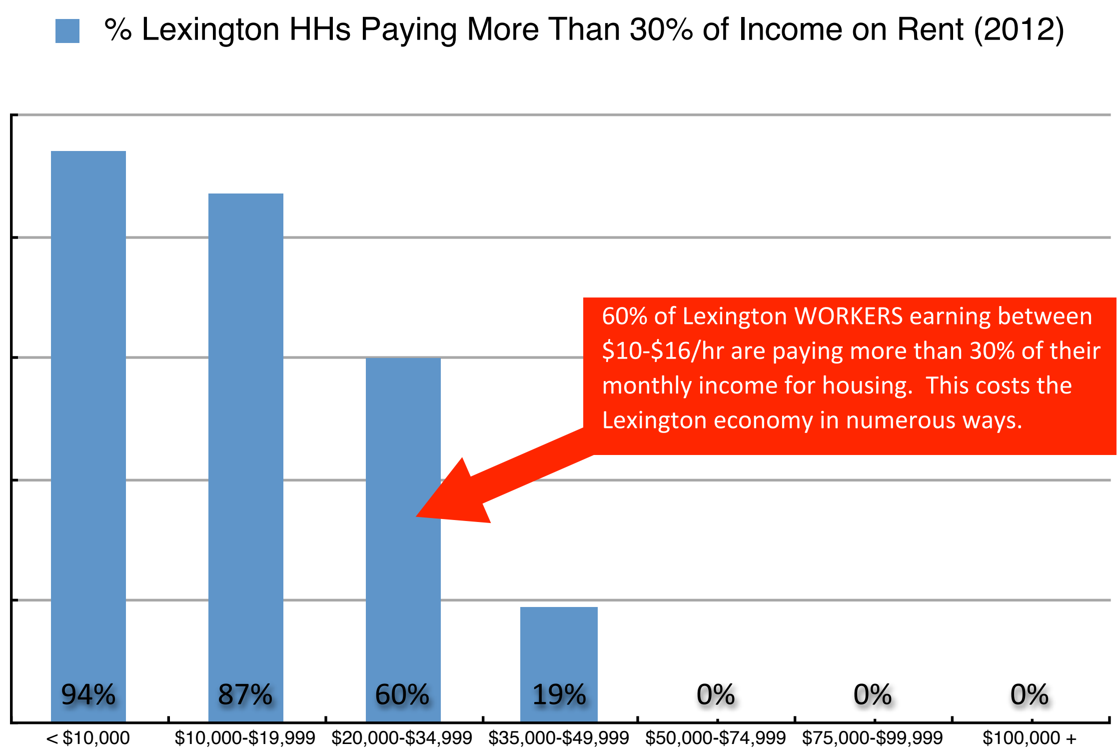
Rounded Numbers to Facilitate Discussion and Understanding	
Total # of Poor (NON STUDENT) Households	15,000
Existing Affordable (Public and Private) Housing Units	9,000
Remaining Gap	6,000

To reiterate, **PROSPERITY** (Lexington becoming a **stronger market** with rising rents) and **LEGACY** (Lexington being home to a large number of **low-income households**, for whom market-rate rentals are proving increasingly out of reach) have left the city with a 6,000 unit gap.

Findings

Having recently drafted a 10-Year Plan to End Homelessness and through the work of the Mayor's Commission on Homelessness, Lexington public officials and community stakeholders are well aware of the challenges the city's low-income households face when it comes to affording a place to live. Beyond the nearly 1,500 county residents living in shelters or on the streets, thousands more live at risk of becoming homeless – paying well in excess of 30 percent of household income on rent or mortgage payments. This reality is driven by the troublesome mix of stagnating incomes and rising housing costs.

The problem of housing stability and affordability is particularly acute for households at the bottom of the income spectrum or in the lowest income quintile - those with incomes less than roughly $20,000. Nearly all (94%) of renter households with incomes below $10,000 pay more than 30% of income on rent, as do the vast majority (87%) of those with incomes between $10,000 and $19,999.



Source: U.S. Census, 2012 American Community Survey 1-Year Estimates, Table B25074

If Lexington policy makers and advocates are to fully understand the nature of the local "affordable housing challenge," it is necessary to know more about who these low-income households – those most likely to face such housing costs burdens – are, as well as how many of them there are.

One challenge of looking at the data on all households is that Lexington's large student population – roughly 43,000 undergraduate and graduate students – tends to skew the numbers. Most college students either do not work while enrolled in school or work only part time, meaning their incomes for that period are very low. Most of these students, though, have not just their own resources but those of their families as well to afford housing, and therefore do not need to be considered among those to target with housing and housing-related initiatives. These students largely live in what the Census defines as "non-family households." (In fact, there are roughly 8,000 non-family households headed by someone under 25 in the county.) As a result, this analysis primarily focused instead on "family households" (as defined by the Census). Before focusing solely on "family households," however, it is worth noting that nearly 15,000 Lexington households relied on cash public assistance and/or Food Stamps/SNAP in 2012. These households had a median income of $17,676 that year.

Public Assistance Income or Food Stamps/SNAP in the Past 12 Months

	Fayette County
Households with Cash Public Assistance or Food Stamps/SNAP	14,988
Median Income of Recipient Households	$17,676

Source: 2012 American Community Survey 1-Year Estimates, Tables B19058 and B22008

Looking only at family households, there are 7,493 families (representing over 10% of all families) living below the poverty line. There are also 5,466 poor non-family households headed by someone 45 years old or older and 2,184 poor non-family households headed by someone 25 to 44 (although some portion of these households is likely made up of students.) Adding the 5,466 to 7,650 (5,466 + 2,184) non-student poor "non-family households" to 7,493 poor "family households" in Lexington gets to a number similar to the roughly 15,000 generated by public assistance and food stamp receipt, suggesting that 15,000 represents a good estimate of "affordable housing need."

Who are these poor families? Most (83%) include children under 18 and 61% are families with children headed by single mothers. (The poverty rate among these families – single mothers with children – was 42% in 2012.) Minority families are also over-represented among Lexington's poor families: while 24% of all Lexington families are headed by a minority householder, this is true of 57% of poor families. (The poverty rate is 24% for African American families and 37% for Hispanic families, compared to just 6% for non-Hispanic white families.) Not surprisingly, families headed by someone who has not graduated from high school are also over-represented among poor families.

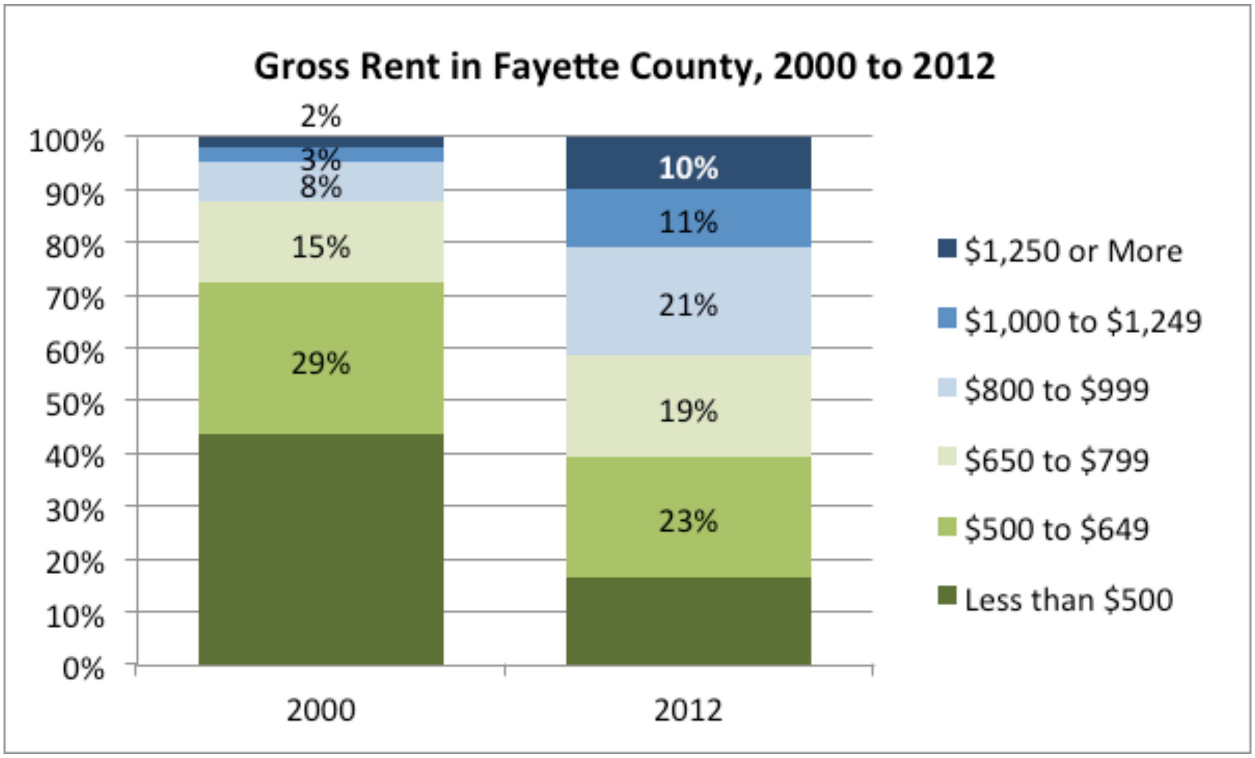
Profile of All Families and Those Below Poverty

Fayette County	All Families		Poor Families		Poverty Rate
	#	%	#	%	
All Families	69,738	100%	7,462	100%	10.7%
All Families with Children <18	35,276	51%	6,173	83%	17.5%
Single Mother	15,926	23%	4,778	64%	30.0%
Single Mother with Children <18	10,900	16%	4,578	61%	42.0%
Non-Hispanic White Householder	53,123	76%	3,241	43%	6.1%
Minority	16,615	24%	4,221	57%	25.4%
Black Householder	9,926	14%	2,422	32%	24.4%
Hispanic Householder	3,593	5%	1,337	18%	37.2%
Householder has <HS Degree	5,454	8%	1,445	19%	26.5%

Source: 2012 American Community Survey 1-Year Estimates, Table S1702

Most poor families (71%, or 5,357 out of 7,493) and an even larger share of families receiving Food Stamps (84%, or 8,198 out of 9,786) include at least one worker. **In all, there are 16,211 employed Lexington residents living below the poverty level.**

Why are they facing housing cost burdens in such high numbers? The need for more affordable housing in Lexington appears so acute today not only due to the large number of very-low-income families but also because, not long ago, these households were fairly well served by the private housing market. As recently as 2000, for example, almost half (44%) of all apartments with cash rents had gross rents below $500 per month – and therefore affordable to households with incomes up to $20,000 (30% of the Area Median Income). **By 2012, just 17% of apartments had rents below $500, and the number of apartments at this price range had fallen by more than half – from 20,238 in 2000 to 8,945 in 2012.**



Source: 2000 Census, 2012 American Community Survey 1-Year Estimates, Table B25063 for ACS, H062 for 2000 Census

While the number of apartments renting for $500 to $649 stayed fairly constant, the numbers in all higher price ranges rose. And while the number of apartments renting for $650 to $799 rose modestly, the number renting for $800 to $999 more than tripled and the number renting for more than $1,000 rose more than five times over.

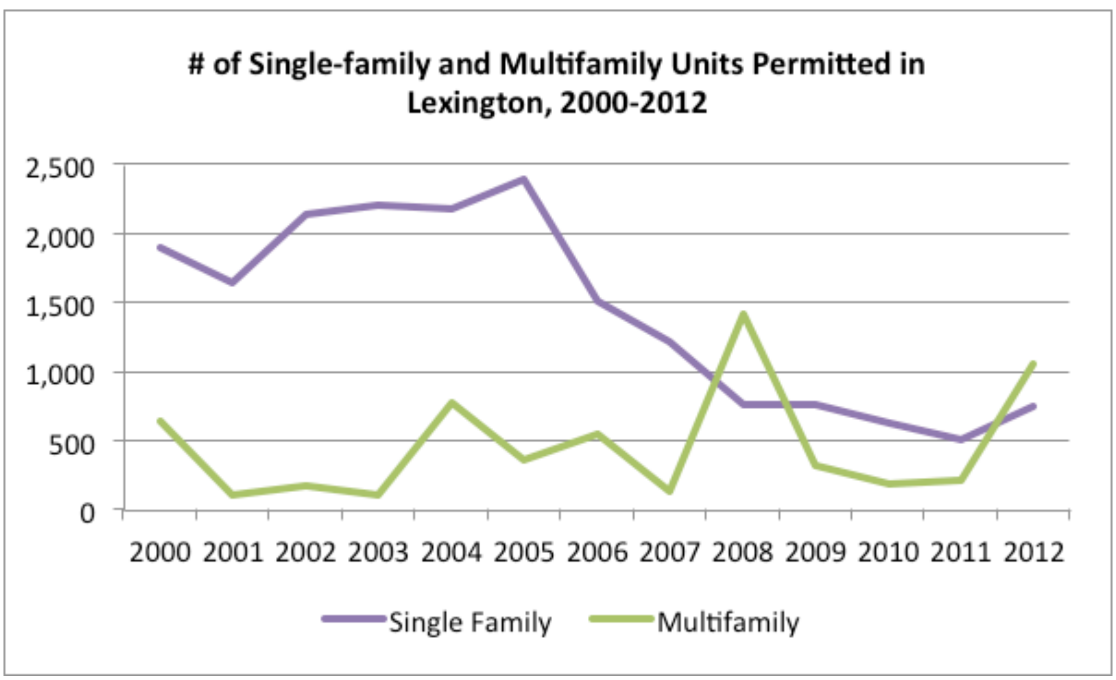
Gross Rent in Renter-Occupied Housing Units

Fayette County	2000	2006	2008	2010	2012
Less than $500	20,238	14,066	10,821	10,240	8,945
$500 to $649	13,205	11,960	10,792	11,498	12,311
$650 to $799	7,074	7,637	10,045	9,625	10,266
$800 to $999	3,561	7,046	8,035	10,965	11,050
$1,000 to $1,249	1,156	2,957	3,671	6,799	6,047
$1,250 to $1,999	738	2,136	2,909	3,025	3,909
$2,000 or More	232	586	1,136	712	1,351

Source: 2000 Census, American Community Survey 1-Year Estimates (2006, 2008, 2010, and 2012), Table B25063 for ACS, H062 for 2000 Census

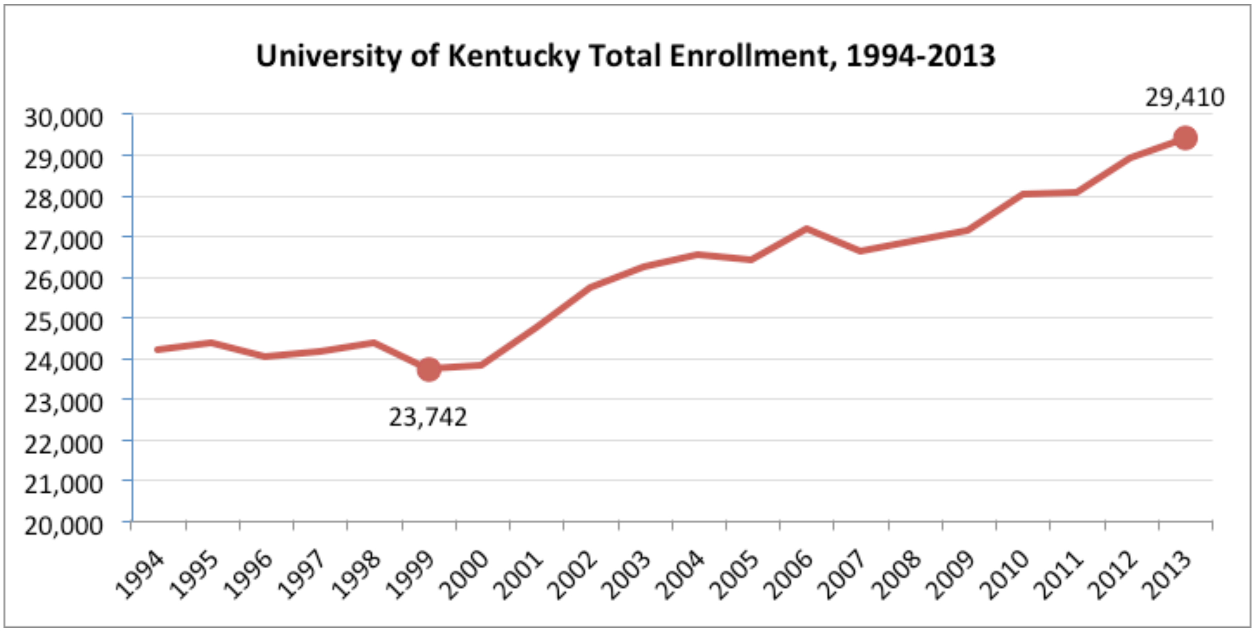
In other words, even though housing remains fairly moderately priced in Lexington, households with incomes below $20,000 and looking for rental units are increasingly being priced out of the market. For a sense of scale: there are now just 8,945 low-cost rentals to accommodate the roughly 15,000 very-low-income households.

What's more, this kind of pressure on the rental market shows no signs of abating. Building permits for multifamily units reached a high point in Lexington in 2008 and nearly matched that amount in 2012.



Source: U.S. Census Bureau, Building Permits Reported

At the same time, the University of Kentucky "is in the midst of a building boom" with plans to update and add to its on-campus and near-campus housing options for students. And this while the campus is experiencing record enrollments, exceeding 29,000 for the first time in the University's history (link to UK).



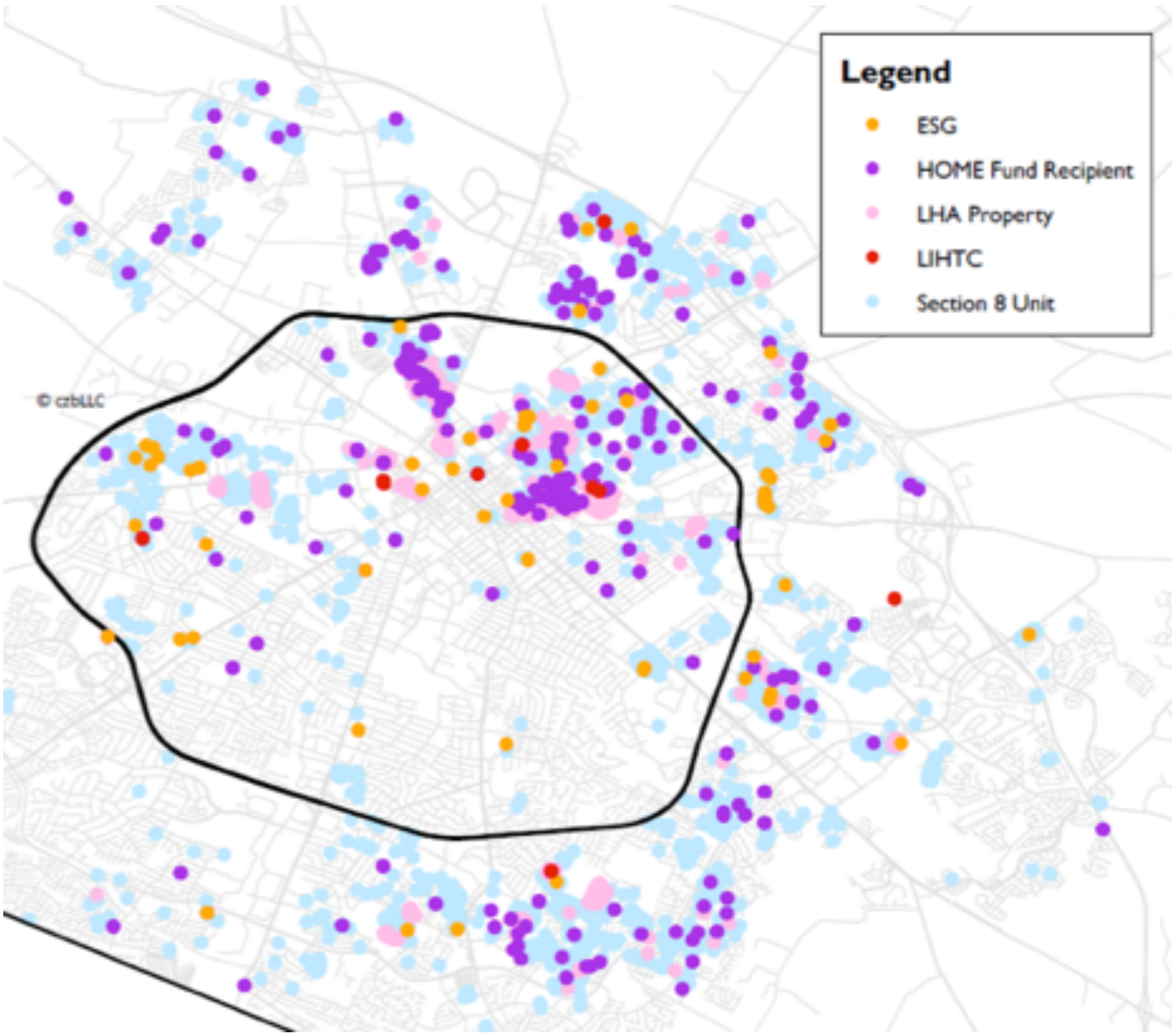
Sources: http://www.kentucky.com/2013/09/10/2814457/university-of-kentucky-enrollment.html#storylink=cpy; http://www.uky.edu/IRPE/students/enrollment/histcollege/enroll.deglev.f9403.all.html; http://www.uky.edu/IRPE/students/enrollment/histstatus/9908all_ukbystatus.html

Put together, these trends have translated into more housing instability and higher housing cost burdens for Lexington's lower income households. To improve the housing situation of low-income households, *10-Year Plan to End Homelessness* as well as the *Report of the Mayor's Commission on Homelessness* both recommend working to increase incomes and wages on the one hand, and increase the amount of affordable housing, transitional units, and rental vouchers on the other.

The Current Response

The City of Lexington and the Lexington Housing Authority (LHA) have several efforts working along these lines. In addition to 1,365 public housing units and 2,046 Housing Choice Vouchers operated and overseen by LHA, there are also 2,694 privately-owned but publicly subsidized units, developed using monies from HUD's project based Section 8, Section 811, Section 202, Section 221 (D) (4), Section 236, and Section 221 (D)(3) BMIR programs; and the Low-Income Housing Tax Credit Program and the HOME Investment Partnerships Program.

City of Lexington's Subsidized Housing Stock



Source: City of Lexington/Fayette County

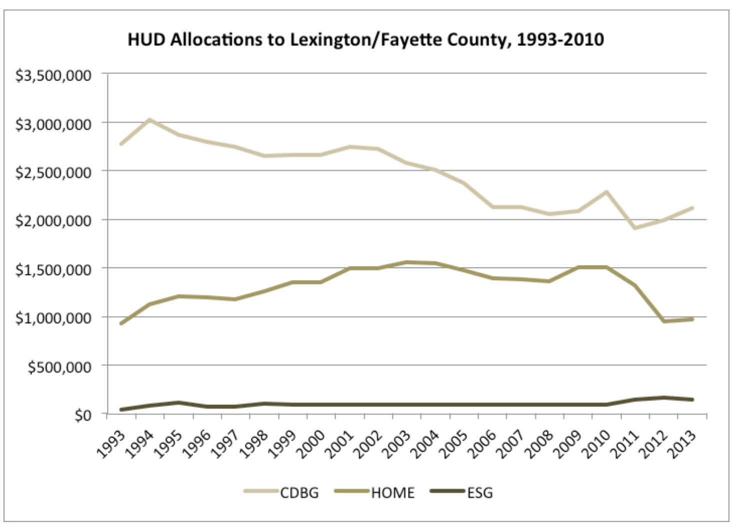
Yet, even with these efforts - ALL OF WHICH ARE FUNDED WITH NON-LEXINGTON DOLLARS - the city remains roughly 6,000 units short of meeting its needs. This leaves roughly 6,000 Lexington households – most of whom include at least one child, and most of whom include at least one worker – facing serious housing cost burdens and housing instability.

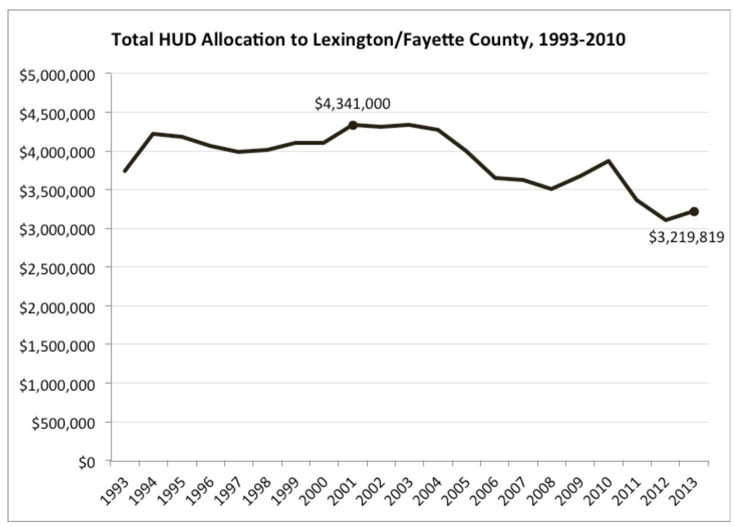
Programmatic Recommendations for "Catching Up" and "Keeping Up"

Several recent planning and community outreach processes – primarily around the issue of homelessness – have highlighted how important it is for the city to act on this substantial gap between the number of low-income households and the number of available low-cost (particularly rental) housing units in Lexington. With a robust approach to preventing and addressing homelessness gaining more support, it makes sense to move the conversation to one focused on how the city should go about addressing this remaining gap. The options before the city are somewhat constrained by the fact that the amount of federal and state funding going to municipalities for the development or provision of affordable housing, funding that has been largely responsible for producing the city's current supply of public and publicly subsidized units, is decreasing.

Grant funds through the Department of Housing and Urban Development – Community Development Block Grants (CDBG), HOME Investment Partnership Program (HOME), and Emergency Solutions Grants (ESG) – are allocated to entitlement communities based on formulas. CDBG dollars, for example, are allocated based on a municipality's or county's total population, number of overcrowded housing units, population in poverty, and older housing units (those built before 1940). In a similar way, HOME funds are allocated based on localities' supply of substandard rental housing, number of low-income families in poor quality rentals, the cost of building housing, and the local poverty rate.

Lexington/Fayette County is an "entitlement community" for these resources; as a result, the county receives an automatic allocation (determined by the formula for each) every year. The amount flowing to the county, however, has been steadily declining over the last decade – in fact, *by 2013, the county received more than $1 million less in funding than it had ten years prior*.





Source: National Association of Counties (http://www.naco.org/counties/Pages/cdbghome.aspx); Department of Housing and Urban Development (http://portal.hud.gov/hudportal/HUD?src=/program_offices/comm_planning/about/budget#home; http://archives.hud.gov/offices/cpd/about/budget/budget01/index.cfm).

At the same time, the Lexington Housing Authority (LHA) - *which is funded by the federal government* - is able to provide far less housing than local residents demand. According to the *Report of the Mayor's Commission on Homelessness*, as of November 2012, 2,376 households were on the waiting list a public housing unit and 316 were on the waiting list for a Section 8 rental voucher (17). Making a *local* monetary commitment "to increase the supply of affordable housing units…, and to provide services necessary to ensure stability for those in housing," is increasingly necessary in the face of rising housing cost burdens for the working poor and declining federal funds available to respond.

Recent studies further suggest that inaction actually brings its own significant costs. The Housing First program would address Lexington's problem of chronic homelessness, thereby reducing costs while providing help.

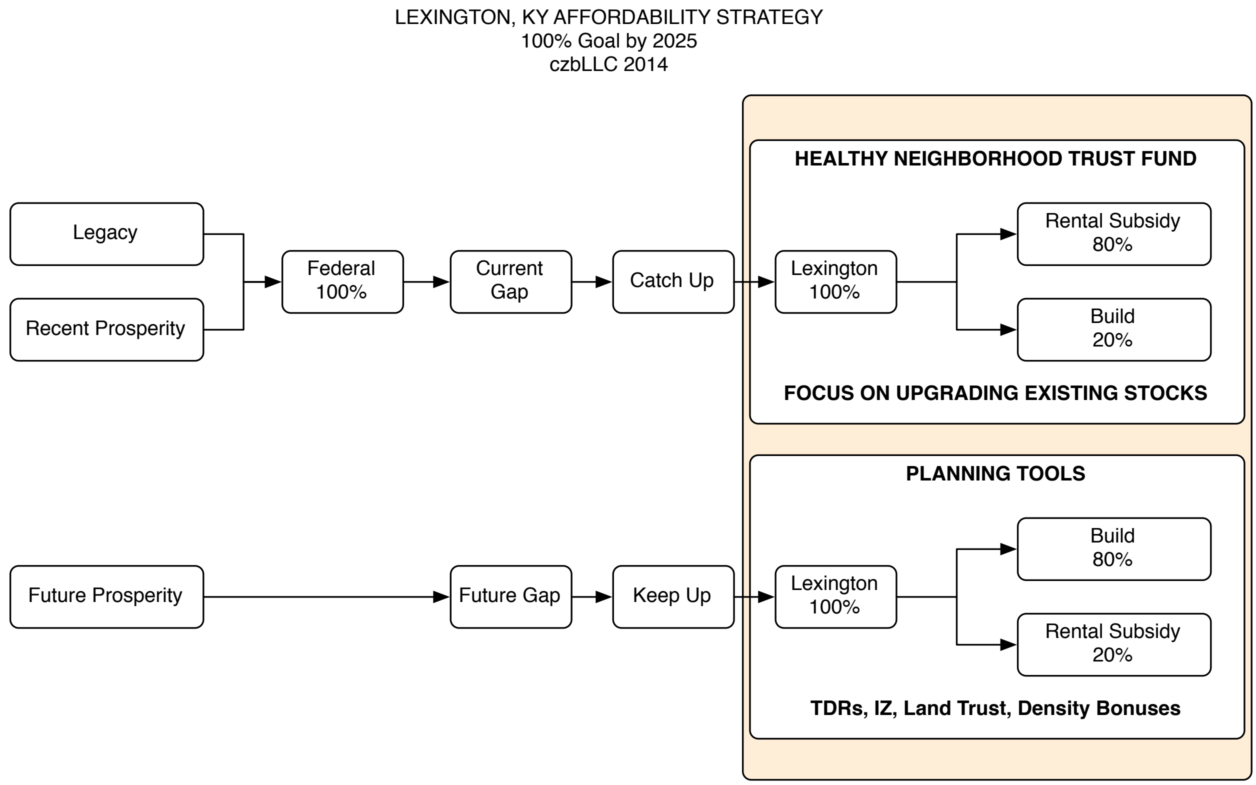
As a result, the Mayor's Commission on Homelessness proposed a 1% increase in the fee levied by the local government on insurance premiums would generate nearly $4 million in funding per year to spend on these goals – split in half between efforts to reduce housing cost burdens and make quality affordable housing more readily available; and as targeted homelessness interventions such as a Housing First approach to serving currently homeless individuals and families (19).

Catching Up and Keeping Up

Based on our analysis, we propose a local contribution to affordable housing financing (subsidy) of roughly $20 million per year paid into a trust fund for affordable housing. The below table illustrates an incremental approach of providing - on average - 500 new rental vouchers and 167 redeveloped units each year until Lexington catches up.

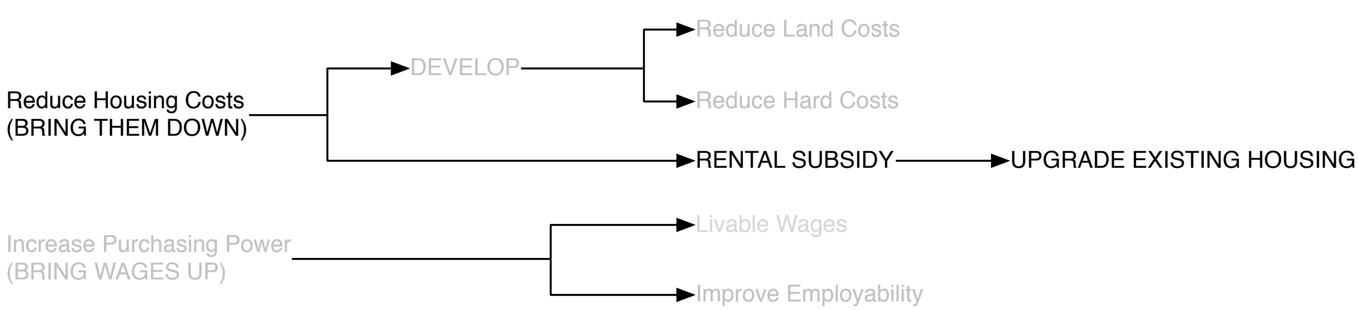
	Year	Gap	Market Loss	Resulting Gap	Voucher Units	New Units	IH/TDR Units	Total New	Actual Gap	Gap NI Market Loss	Cost
1	2015	6,000	400	6,400	333	0	0	333	6,067	5,667	1,998,000
2	2016		400	6,467	520		policy	520	5,947	5,147	5,118,000
3	2017		400	6,347	520		policy	520	5,827	4,627	8,238,000
4	2018		400	6,227	520		policy	520	5,707	4,107	11,358,000
5	2019		400	6,107	520		policy	520	5,587	3,587	14,478,000
6	2020		400	5,987	520	200	policy	720	5,267	2,867	18,798,000
7	2021		400	5,667	520	200	policy	720	4,947	2,147	23,118,000
8	2022		400	5,347	520	200	policy	720	4,627	1,427	27,438,000
9	2023		400	5,027	520	200	policy	720	4,307	707	31,758,000
10	2024		400	4,707	507	200	policy	707	4,000	0	36,000,000
11	2025		400	4,400			policy	0	4,400	0	36,000,000
											214,302,000
			400		500	167	0	545			19,482,000

While well below the amount needed to close the entire 6,000-household gap between the number of low-income households and the number of low-cost rentals, creating a Trust Fund starting with $4 million in annual revenue, $2 million of which would be designated for the city's affordable housing strategy in the first year, is an important first step. An initial $2M first step of this sort could provide renal vouchers to more than 300 working households, and if connected to code compliance, have a significant impact on substandard housing stocks. In fact, these dollars could be thought of as "start-up funds" for a larger local commitment to meeting affordable housing needs: they give the city the opportunity to put organizational structures and key personnel in place, and also to help existing service providers and affordable housing developers to increase their own capacity to build, rehabilitate, or manage affordable units or vouchers.



In the interim, it is important to realize that when it comes to subsidizing affordable housing, $2 million is not a lot of money.

One challenge with relying on new construction to tackle the city's gap is its shear expense (financial and political), in addition to the distance between the local capacity to build affordable housing (LIHTC and HOME funds support roughly 75 and 80 units per year) and the number that would need to be produced to make a noticeable dent in local affordable housing needs.



Alternatively, market-rate rents, though clearly out of reach for households between 0% and 30% of the Area Median Income, are not excessively expensive. As a result, there is only a small spread between what a poor household can afford to pay and what private apartments cost. Addressing that spread – utilizing subsidies modeled after the federal Housing Choice Voucher Programming – is a possibly far more efficient way of making housing affordable. For example, the average Section 8 subsidy for rental assistance in Lexington is $6,000 per household per year, a figure well below the roughly $100,000 it would take to build a new unit of affordable housing. In other words, while $2 million would fund the construction of just 20 new affordable housing units, it could support rental assistance for 300 households – nearly enough to clear the entire Section 8 waiting list.

It is recommended that there be an alignment of the management and oversight of these new locally funded rental vouchers with the system currently managing and overseeing the federally funded Section 8 program, particularly in terms of program accounting and intake (determining eligibility, getting onto a wait list, etc.) This would be a chance, too, to address ways to strengthen the Section 8 program and make it work better for households and neighborhoods – for example, ensuring properties are inspected regularly and making participating landlords eligible for grants and/or low-cost loans to address code violations and make façade improvements.

Ultimately, the goal should be designing a program that makes it worth landlords' while to participate and also requires good behavior on landlords' part that will generate spillover benefits beyond affordability, most notably in terms of housing quality and neighborhood quality.

According to data from the Code Enforcement office, there are currently nearly 200 residential properties with active, serious code violations and another 1,000 with active, less serious code violations.

Land Use Code	All Properties	Properties with Less Serious Code Violations		Properties with Serious* Code Violations	
		#	%	#	%
Apartments, 1-19 Rental Units	1,360	95	7.0%	27	2.0%
Apartments, 20-39 Rental Units	78	18	23.1%	7	9.0%
Apartments, 40+ Rental Units	214	73	34.1%	10	4.7%
Condominiums	5,458	11	0.2%	1	0.0%
Single-family Homes, Duplexes, Townhouses	88,267	880	1.0%	151	0.2%
All Residential Properties	95,377	1,077	1.1%	196	0.2%

** Properties with "serious" code violations include those that are Boarded/Vacant, have Frame Damage/Deterioration, have Mold/Mildew, have No Electric/Gas/Heat/Hot Water, have Structural Damage, or are Unfit for Human Habitation. "Less Serious" code violations include all others that relate to the property. (This latter category does not violations for "Weeds" or "Nuisances.")*
Sources: Fayette County, czbLLC.

While code violations affect a significant number of multifamily buildings (nearly one-third of properties with 20 to 39 rental units and 39% of properties with 40 or more rental units), they impact just 1% of single-family units, duplexes and townhouses.

To ensure that lower-income renters receive not just affordable housing but *quality* affordable housing, any affordable housing strategy should be oriented to address both households' cost burdens and housing units' physical condition. This will likely require not only additional funding but also additional collaboration between city code enforcement staff and rehabilitation specialists, and LHA staff currently overseeing the Section 8 program.

The combination of rental subsidy plus new construction - as shown in the table on p 19 - can reduce the gap of 6,000 to zero by 2025, and by tying subsidies to property inspections, trigger needed upgrades across Lexington. This means the “system” that is recommended be built fundamentally consist of three pipelines.

1. The first is the delivery of rental subsidy to low income households for use in pre-inspected code compliant rental units.
2. The second is the construction of new or redevelopment of existing units when possible.
3. The third is policy-created units through planning and zoning frameworks as noted.

This third point is crucial. Creating and resourcing a trust fund - even one that fully zeros out the current 6,000 unit gap by 2025 - still leaves Lexington in an additional 4,400 unit gap by 2025, because, as noted, the market will continue to shed affordable units at a sizable annual clip. In 1990, 88% of the rental units in Lexington were affordable to low-income working households. By 2000 that had shrunk to 44% By 2010 it had dropped to 19% and by 2012 to 17%

To ensure that by 2025 this gap is also zeroed out, the City of Lexington will have to aggressively refine its current repertoire of planning tools. Tools such as zoning and development rights transfers are market-oriented planning mechanisms that trade additional profit to the market in exchange for housing resources or more economically sustainable neighborhood outcomes. The Department of Planning, Preservation and Development would have the responsibility of working with Lexington’s planning division and related boards and commissions to refine the city’s Comprehensive Plan and related development documents, pointing all municipal tools in one common direction, something that does not now exist.

Summary

Lexington is short 6,000 affordable rental units. This will grow by about 400 a year if the city does nothing.

Each of these units will cost about $6,000 per year per household to address, and this cost will not go away. Affordable housing gaps (problems) are not ever *solved* in the conventional way solutions tend to be thought of. The only way to "solve" such a problem is to raise the earning power of workers to the point where wages keep pace with housing costs.

In the absence of such a shift in earning (either through actual wages or wage subsidies), working low-income earners in Lexington will either overpay for housing or live in substandard conditions, and in either case, cost the Lexington economy in one way or another.

Creating a housing trust fund to begin addressing this problem is a wise direction to take. But the magnitude of the challenge is so large that unless a trust fund is commensurately large, the problem will remain significant, and, as noted, actually grow. In addition to creating a fund to close affordability gaps, it is important that the whole armada of city land use and development policies be reshaped so as to harness market capacity in ways that keep the affordability problem from getting worse.

Fully funding the tools needed for such a large endeavor will be very costly. But the Lexington economy is very large, and fully capable of absorbing these costs. This is not an issue of whether Lexington can zero out its affordable housing gaps and keep them narrow, but whether it wants to badly enough.

Seattle wanted it badly enough to twice pass affordable housing levies each in excess of $100M. Boulder, Colorado requires all single family housing developers to pay a 25% inclusionary zoning in lieu fee into a local trust fund that also collects a 20% inclusionary fee for multifamily rental housing development. In the case of Seattle, the funds are distributed annually on a competitive basis - aligned with many of the elements of the State of Washington's tax credit allocation process - to local nonprofit developers that - over the last 20 years, have build significant capacity. In Boulder the funds are generally distributed back to Boulder Housing Partners, the city's housing authority. New York City under the Bloomberg Administration wanted it badly enough to massively upzone large sections of four of the five city's boroughs, and in the process created 165,000 affordable housing units. Park City, Utah wanted it badly enough to create a development rights trading bank, with incentives for developers to provide affordable units. Alexandria, Virginia wants it badly enough to evaluate all development proposals from the perspective of impact on affordable housing; in Alexandria, city staff provide City Council with an estimate of affordable units projected to be, and, in turn, developers must remedy that.

The common denominator in the above examples is that these are cities in the thick of coping with the consequences of prosperity. And they have been at it for a long while, and thus have become accustomed to addressing housing affordability as a matter of course. That doesn't mean they have "solved" their problems. They haven't. But they are committed to addressing affordability gaps for low-income working households using their own resources.