Multifamily Properties:
Opting In, Opting Out and Remaining Affordable

U.S. Department of Housing and Urban Development
Office of Policy Development and Research

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Prepared for:
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FOREWORD

The U.S. Department of Housing and Urban Development's project-based multifamily housing stock includes more than 22,000 properties with more than 1.5 million units, representing a significant proportion of federally assisted housing for low-income families. The multifamily stock was developed under programs created in the 1960s and 1970s to supplement conventional public housing and promote privately owned development of affordable housing.

This study examines the characteristics of properties that have left the assisted stock, either through prepayment or through opt out, and compares them with properties that have remained in HUD programs. In addition, the study examines the affordability of rents charged at properties that have left the assisted stock.

The quantitative analysis uses data on the full HUD-assisted multifamily housing stock and compares properties whose owners chose to remain in the stock with properties that have left the stock due to opt-out/prepayment and with properties that are in foreclosure or that have been referred to HUD's Enforcement Center. Properties were more likely to opt out if they were in markets that could support higher rents upon opting out. These tended to be properties with rents that were below market rate, and in locations with relatively low poverty rates.

In order to illustrate the opt out decision making process, case studies were undertaken as part of the study. The case studies, not surprisingly, revealed that a key factor in the decision to opt out was whether the property was in a market that could support rents high enough to cover the property's costs.

This study represents a valuable summary of the current disposition of the HUD multifamily housing stock. It also provides some insights as to what characteristics are associated with leaving or remaining in the stock. As expected, markets matter. Properties with assisted rents below prevailing market levels are more likely to leave the stock than are properties with rents closer to market levels. Non-economic factors also influence owner decisions. Once properties leave the assisted stock, some owners do reposition properties and raise rents, but at least a portion of the properties that leave the stock remain rented and affordable to low-income households.

Darlene F. Williams
Assistant Secretary for Policy
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Executive Summary

The U.S. Department of Housing and Urban Development's (HUD's) assisted project-based multifamily properties are privately owned properties representing a significant component of federally assisted housing for low-income families. This is in contrast to the public housing stock, which is publicly owned and operated. The HUD-assisted project-based multifamily housing stock includes more than 22,000 properties with more than 1.5 million units. They were developed under programs that were created in the 1960s and 1970s to supplement the public housing program, as part of a policy change that aimed to promote more privately owned development of affordable housing.

In this study, we examine the characteristics of properties that have left the assisted stock either through prepayment or through opt out and compare them with the characteristics of properties that have remained in the HUD programs. In addition, the study examines the affordability of rents charged at properties that have left the assisted stock through either prepayment or opt out.

A variety of incentives and financial assistance were provided to private developers of multifamily housing in exchange for an agreement to rent the housing to low- and moderate-income households. Among the incentives provided was a provision that allowed them either to prepay a subsidized mortgage (under the older mortgage subsidy programs) after 20 years, or simply not renew a Section 8 contract when the initial subsidy contracts expired (termed "opting out" in this study). In either case, these incentives permitted owners to leave the assisted stock by converting their properties to another use and no longer required them to rent to low-income residents. Even with a variety of incentives and policy prescriptions available for maintaining low-income housing, many owners of both older and newer subsidized housing have chosen to prepay their mortgages and/or opt-out of their expiring Section 8 contracts, converting properties to alternative uses.

Summary of Key Findings

From the detailed results of this study, we can establish several key findings. First, it appears that family-occupied properties in relatively well-off neighborhoods with market rents greater than the rents charged in the assisted properties have a higher likelihood of leaving the HUD-assisted stock. Second, Older Assisted properties tend to leave the stock—either through prepayment/opt-out or through an enforcement action—to a much greater degree than Newer Assisted properties. Third, for properties that do leave the HUD-assisted stock, a majority of those units would be affordable to families who receive a voucher after the property has left the stock. Without vouchers, however, only a very small number of units would be affordable for families with very low incomes.

Study Design

The study had three components. The first is a quantitative analysis that compares characteristics of properties—such as age, location, and occupancy type—that have left the stock with those that have remained in the assisted stock, and with properties that have either been referred to the Enforcement Center or have had their mortgages foreclosed. This study component also includes a regression analysis to identify which types of properties are most likely to opt out of their Section 8 contracts. The second component uses onsite examinations of a small number of properties that have opted out of the program and properties that have "opted in" in the same metropolitan areas to identify factors that lead certain property owners to opt out and other owners to remain in the HUD programs. Site visits took place in cities where a significant number of opt-outs have occurred: Cincinnati, Dallas, and Sacramento. The third study component looks at the affordability of units after properties leave the assisted stock.

We present more detailed findings from each of the study components below.

Quantitative Analysis

This portion of the analysis used data on the full HUD-assisted multifamily housing stock to compare characteristics of properties whose owners chose to remain in the stock with characteristics of properties that have left the stock due to opt-out/prepayment, and with properties that are in foreclosure or have been referred to HUD's Enforcement Center. Properties were more likely to opt out if they were in markets that could support higher rents upon opting out. These tended to be properties with opt-out/prepayment rents that were below market rate, and in locations with relatively low poverty rates. In particular:

- Properties whose rents were less than the HUD-published Fair Market Rents (FMRs) were more likely to opt out. Indeed, the regression analysis indicates that a property's pre-opt-out rent level relative to the local FMR is the most important determinant, controlling for all other property, program, and location characteristics. These properties tend to be in markets that have higher rents than the rents at the opt-out properties, and the owners apparently believed they could obtain higher rents in the unassisted market.

- Older Assisted properties were significantly more likely than Newer Assisted properties either to leave the assisted stock (that is, in some terms to be financially successful), or to be in foreclosure/enforcement,[1] rather than remain in the assisted stock as financially viable properties.

[1] "Foreclosure/enforcement" includes properties that, as of December 2004, faced foreclosure or other payment or compliance challenges. "Enforcement" properties are those that have been referred to HUD's Enforcement Center for having some form of physical or financial difficulties and requiring remedial action.

- Both the cross-tabulation analyses and the regression analyses showed that properties that left the assisted stock tended to be in metropolitan/central city locations. Taken alone, the cross-tabulation analyses suggest that suburban properties are also likely to opt out relative to non-metropolitan locations, whereas the regression analysis indicates that non-metropolitan properties were more likely to opt out than those in suburban areas.

- Properties that opted out were also located in neighborhoods with higher median incomes, higher median rents, and lower poverty and vacancy rates. Foreclosure/enforcement properties were in neighborhoods with the lowest median incomes and homeownership rates, and in neighborhoods with the highest vacancy and poverty rates of the groups of properties examined.

- Properties that remained in the assisted stock were more likely to have zero- and one-bedroom units, consistent with an elderly/disabled tenancy. Properties that left the stock and properties in foreclosure or referred to the Enforcement Center were more likely to have two- and three-bedroom (family) units. Properties with units for large families (four or more bedrooms) were even more likely to be in foreclosure/enforcement. The vast majority (91.1 percent) of properties in foreclosure/enforcement were family-designated.

- Properties that left the assisted stock had on average lower rating scores on physical condition than those that stayed in. The median Real Estate Assessment Center (REAC) score was above 60 for properties that left the assisted stock, for those that stayed in the stock, and for those that were in the foreclosure/enforcement group. A portion of all properties in the aforementioned categories had scores below 60. However, the foreclosure/enforcement category had the highest percentage of scores below 60, followed by the properties that left the stock voluntarily. (Perhaps the owners of these properties were not maintaining them during the period before they left the assisted housing program because they planned to undertake major renovations for the conversion to market rate.)

- As expected, nonprofit owners were much less likely to opt out compared with for-profit owners. Nonprofit owners are often mission-driven to continue to provide affordable housing. In addition, some nonprofit owners were precluded from opting out based on use restriction agreements that were required by lenders as a condition for receiving the funding.

- The regression analysis indicates that family occupancy and smaller development size are other factors associated with an increased likelihood of opting out.

- All else being equal, the regression analysis shows that properties with 100 percent of units receiving project-based assistance are at a higher risk of opting out.

- The regression analysis also indicates that properties located in census tracts with high poverty rates are much less likely to opt out, presumably because those markets cannot support rents high enough to make opting out attractive. Properties located in the Pacific, Mountain, and West South Central regions have a higher probability of opting out that those in the South Atlantic region.

Case Studies

To learn about the full range of factors (including the non-market factors) that lead some owners to leave the Section 8 program and other owners to remain in the program, this analysis included case studies in three metropolitan statistical areas (MSAs) that have experienced large numbers of opt outs. In each of the three MSAs—Sacramento, Dallas, and Cincinnati—we visited two pairs of seemingly similar properties in terms of neighborhood, size, and occupancy type. One property owner in each pair had opted out of the Section 8 program, while the second owner had chosen to keep the property in the Section 8 stock.

The case studies, like the predictive analysis, focused only on Section 8 properties. Not surprisingly, the case studies revealed that a key factor in the decision to opt out was whether the property was in a market that could support rents high enough to cover the property's costs. Beyond this expected market-related factor, however, other key findings include the following:

- Non-economic issues also had an influence on the opt-out decision. Several of the owners opted out of the Section 8 program, even though it did not seem to make financial sense to do so. This decision was largely attributed to uncertainty about the future and difficult relationships with local HUD offices.

- Owners with portfolios that included both assisted and unassisted properties said that as more of their portfolio left the Section 8 stock, it became less economically feasible to maintain the Section 8 portion of their portfolios. This was because operating a Section 8 property requires administrative skills specific to the program, and as a smaller portion of the portfolio is in Section 8, the owners may not be able to economically maintain staff members with the needed skills.

- Not all properties that left the assisted stock became unaffordable to low- and moderate-income households. In each of the three MSAs visited, at least one of the opt-out properties was still occupied primarily by low-income households.

Affordability Analysis

The level of policy concern about opt-out properties will vary depending on what happens to rents at the properties after they leave the stock. If rents at those properties become unaffordable to low-income households, the level of concern will be much higher than if these properties continue to provide affordable housing to low-income households. To address this issue, we compared post-opt-out rents in a sample of units that left the assisted stock with the local FMRs to assess the degree of affordability in the opt-out units. We also estimated the degree to which those units were affordable for unassisted households earning various incomes. Key findings include the following:

- At the end of 2004, nearly 60 percent of the opt-out units had rents that were below the FMR, indicating that the units would be affordable to households with vouchers. An additional 31 percent had rents that were between 100 and 125 percent of the FMR, indicating they might still be affordable to voucher holders, depending on the payment standards chosen by voucher program administrators and families' ability to pay more than 30 percent of their income for housing.

- Only 6 percent of the units would have been affordable to unassisted households earning 30 percent of the local area median income. Sixty-four percent would have been affordable to unassisted households earning 50 percent of the local area median income.

- We cannot determine whether the rents for the opt-out units are now higher than the contract rents on the basis of which HUD paid subsidies when the units were part of the assisted stock, because we do not have rent data for that period.

Policy Recommendations

Based on the results of this study, we make the following policy recommendations to HUD:

If HUD's policy goal is to maintain properties in the assisted housing stock, we suggest that HUD consider policies to offset both the economic and the non-economic incentives to opt out. We have two recommendations for policies bearing on economic factors: First, consider whether the Section 8 project-based program rules can be made less complex or supported more fully through software to reduce the burden on owners. Second, target resources and incentives to areas where rents after opt-out are less affordable.

With respect to non-economic factors, we suggest that HUD establish better communication regarding rent-setting policies, not only within the Mark-to-Market program, but also for the Mark-up-to-Market policy affecting regular renewals.

1. Introduction

This study compares the U.S. Department of Housing and Urban Development's (HUD's) project-based assisted multifamily properties that have left the HUD programs—either through opting out of a Section 8 contract or prepaying a subsidized mortgage—with other properties whose owners actively choose to continue receiving HUD subsidies ("opt-ins"). The report also examines the degree to which properties remain affordable after they have opted out or prepaid and left the HUD-assisted inventory.

1.1 Background

The study focuses on properties that were developed under project-based Section 8 programs, as well as under earlier subsidized mortgage-interest programs. The main characteristic of all these multifamily properties is that they have HUD project-based assistance that is linked to the property (rather than the tenant), through project-based Section 8 or other type of rental assistance, or through subsidized mortgage interest.

The HUD-assisted project-based multifamily programs fund low-income housing properties that are privately owned. They represent a significant component of federally assisted housing for low-income families. These programs, created in the 1960s and 1970s, led to the development of roughly 1.5 million units of assisted housing with restrictions on the incomes of the people who may live there and the rents that the owners may charge.

HUD multifamily programs are distinct from the public housing program, which produces publicly owned and operated housing. The HUD-assisted multifamily programs were created to supplement the public housing program as part of a policy change that aimed to promote more privately owned development of affordable housing.

The project-based multifamily programs fall into two distinct groups. The first group is made up of the "older" mortgage subsidy programs that were based on pre-Section 8 types of subsidies. Approximately 700,000 units were built under these mortgage subsidy programs from the mid-1960s through the mid-1970s. Specifically, these programs are the Federal Housing Administration (FHA) Section 221(d) (3) Below Market Interest Rate (BMIR) program and the Section 236 program. The subsidies for these two programs covered the difference between expenses based on a market-rate mortgage and expenses based on a below-market-rate mortgage. A large number of these properties also have Section 8 rental assistance subsidy contracts. In some cases, a few properties developed under these programs received an older form of rental subsidy through the Rent Supplement (RS) or Rental Assistance Payment (RAP) programs.

The second group, the "newer" project-based inventory, generally refers to properties developed under the Section 8 New Construction/Substantial Rehabilitation and Moderate Rehabilitation programs. The subsidy for these properties is based on the difference between what the tenant can afford (paying 30 percent of income for rent) and the agreed-upon rent of the project. This rent was sometimes above the market-rate rent. Most of the "newer" inventory was built in the late 1970s and early 1980s. In 1983, funding for development of new and substantially rehabilitated properties ceased, although the Moderate Rehabilitation program continued for several more years. Much of the Newer Assisted Stock has mortgages insured under the Section 221(d) (4) program. Many were financed, however, by state Housing Finance Agencies (HFAs) through mortgage revenue bonds, by the Rural Housing Service's (formerly Farmers Home Administration) Section 515 program, or by Section 202 direct loans.[2] Approximately 800,000 units were developed during this period, including roughly 200,000 units that received both Section 8 rental subsidies and development loans under the Section 202 program for elderly and disabled residents.

Private developers of this multifamily housing received several types of incentives and financial assistance in exchange for an agreement to rent the housing to low- and moderate-income households at affordable rents. The "older" programs provided a mortgage interest subsidy, which bought down the interest rate on the mortgage from the higher prevailing market rates at that time to a subsidized level of 1 percent or 3 percent. The subsidized interest was passed on to lower income households in the form of lower rents.

The primary form of rental subsidy in HUD multifamily properties was Section 8. Under the Section 8 program, there were several different forms of this assistance, depending on the purpose. This set of project-based Section 8 programs includes the following five categories:

- Loan Management Set-Aside
- Property Disposition
- Preservation
- Moderate Rehabilitation
- New Construction/Substantial Rehabilitation.

The Section 8 New Construction/Substantial Rehabilitation program was described above. A description of each of the other four programs follows:

Loan Management Set-Aside (LMSA)

In 1974, the Section 8 Housing Assistance Payments program was introduced, and most of the RAP and RS contracts were converted to this form of subsidy. Many other BMIR and Section 236 properties also received allocations of Section 8 subsidies through the Loan Management Set-Aside (LMSA) Program. In the LMSA program, HUD contracts with owners of HUD-insured multifamily or HUD-held housing projects experiencing financial problems. The program seeks to minimize defaults on HUD-insured multifamily rental projects by ensuring a reliable income stream. It may be used in conjunction with the Flexible Subsidy program. Families receive a rental subsidy equal to the difference between

[2] The study does not include projects funded by the Section 811 and post-1990 Section 202 programs, because rental assistance for those projects is provided through the Project Rental Assistance Contract (PRAC) or Project Assistance Contract (PAC) rather than project-based Section 8. Also, prepayment decisions are not relevant for those projects because they were financed by capital grants rather than mortgages.

their share of the rent (normally 30 percent of adjusted household income) and the rent charged by the owners, which was not to exceed applicable Fair Market Rents (FMRs).

Property Disposition
This is the program through which HUD forecloses on HUD-held multifamily mortgages and sells HUD-owned multifamily properties with Section 8 assistance.

Preservation program
This program assists multifamily properties by providing project-based Section 8 subsidies to preserve low-income status.

Moderate Rehabilitation program
The Office of Public and Indian Housing manages most projects assisted with Section 8 moderate rehabilitation. These projects are not included in the Real Estate Management System (REMS) or a comparable database. The REMS database only includes the subset of such projects that are also associated with the Section 8 Property Disposition program. Consequently, our analysis of the Section 8 Moderate Rehabilitation projects in this study is limited to this part of the stock.

At issue are the effects of regulations allowing owners to remove their properties from the assisted housing program. To encourage owners to invest in low-income housing, program regulations allowed profit-motivated owners to prepay a subsidized mortgage (under the older mortgage subsidy programs) after 20 years, and/or allowed them to elect not to renew Section 8 subsidies when those subsidy contracts expired. These incentives permitted owners to convert their properties to another use and no longer rent to low-income residents. Many owners of both older and newer project-based assisted multifamily housing have chosen to opt out of a Section 8 program or prepay a subsidized mortgage, converting the properties to an alternative use.[3] This occurred despite a variety of incentives available for maintaining this housing assisted stock as low-income housing.

Another, relatively recent program to help maintain the low-income housing stock is the **Mark-to-Market** program, established in 1997 by the Multifamily Assisted Housing Reform and Affordability Act of 1997, as a process for restructuring the financing of multifamily properties insured by the Federal Housing Administration (FHA) when their contracts expire. The program's goal is to reduce federal spending on housing subsidies by making it financially feasible for multifamily properties currently charging rents greater than comparable market rents to survive and offer quality, market-competitive housing at comparable market rents.

The Mark-to-Market program is geared exclusively toward properties that have *above-market* rents. There is, however, another class of FHA-insured properties found typically in high-cost markets, in which the rents are below comparable market rents. This group of properties began experiencing a loss of units between 1996 and 1999 when many owners chose to opt

[3] Some owners of Section 236 properties prepaid with restrictions and retained their interest reduction payments (IRP) from the prior mortgage.

out of their Section 8 contracts and convert for a purpose in which they could receive a higher return. This experience led Congress to pass legislation in 1999 providing HUD the ability to mark FHA-subsidized properties *up to market*. Under the **Mark-up-to-Market** program, HUD may renew Section 8 contracts at market-comparable rents for a period of 5 years or, under recent changes, for any agreed-upon period. To the extent properties also have subsidized mortgages with expiring use restrictions, prepayment is not allowed during the contract renewal term.

1.2 Purpose of the Study

The purpose of this study is to examine the characteristics of “opt-out” and “prepayment” properties and to compare them with properties that have remained in the HUD programs. The study also examines the types of owners who have opted out and how they arrived at that decision. Finally, the study examines the extent to which the rents at properties that have opted out are affordable for low-income households. With the exception of three case studies, the study relies exclusively on available administrative data from various HUD multifamily data systems and other secondary sources such as the 2000 census.

1.3 Glossary of Key Terms

For purposes of this study, we use the following terms to describe the status of a property:

Active Section 8—a property with a Section 8 contract that has not yet reached its expiration date and is subject to rent and income use restrictions.

Active 236 or BMIR—a property assisted under the older mortgage interest subsidy programs (Section 236 and Section 221(d) (3) BMIR) that has not yet prepaid and is subject to rent and income use restrictions.

Enforcement Center—HUD’s Enforcement Center works cooperatively with HUD’s program offices to ensure compliance with business agreements and regulations. The Enforcement Center receives referrals of distressed multifamily properties. Properties may be referred due to unsatisfactory physical inspection conditions or for financial discrepancies.

Fair Market Rents (FMRs)—FMRs are estimates of gross rent that include the costs of rent and utilities, except telephone. HUD sets FMRs to ensure that a sufficient supply of rental housing is available to participants. FMRs must be both high enough to permit a selection of units and neighborhoods and low enough to serve as many families as possible. In most places HUD sets the FMR at the 40th percentile of local gross rents, although in some places the FMR is set at the 50th percentile.

Foreclosure—a property that is either failing (in foreclosure) or has the possibility of failing (referred to the Departmental Enforcement Center).

Mixed Active Property—a property assisted by both a Section 8 contract and a subsidized 236 or BMIR mortgage; for purposes of this study, it can also mean a property that has opted out of its Section 8 but has not yet prepaid its subsidized mortgage, or a property that has prepaid its subsidized mortgage but not yet opted out of its Section 8 contract.

Opt-in—a property whose owner chooses to renew an expiring project-based Section 8 contract, thereby extending the rent and income restrictions (or "use restrictions").

Opt-out—a property whose owner chooses not to renew an expiring Section 8 contract and decides to opt out of the Section 8 program.

Prepayment—a property that leaves the HUD-assisted stock through prepayment of a mortgage subsidized either under the FHA Section 236 or Section 221(d) (3) BMIR program. Once the mortgage is prepaid and assuming no ongoing Section 8 subsidies, the associated project-based federal rent and income restrictions are terminated and the owner is free to choose how to use the property.

1.4 Overview of Final Report

This document describes the research objectives of this study, the methodology we used to address those objectives, and the findings from the study. The report also provides some policy recommendations that stem from the findings. It consists of six chapters. Following this introduction, Chapter 2 discusses the study's research objectives and methodology. The chapter highlights the research questions and presents the goals and methodology for the case studies and affordability analysis.

Chapter 3 presents the findings of a quantitative analysis we conducted that compares opt-out properties with opt-in properties and with those in foreclosure or the Enforcement Center. The chapter also includes a multivariate analysis to predict the likelihood that a property will stay in or opt out of the program. Chapter 4 summarizes the findings from visits we made to three communities to develop case studies on the opt-out decision by owners. Chapter 5 assesses the affordability of properties after they leave the HUD-assisted stock, based on information we gathered about a sample of units in properties that opted out of the Section 8 program or prepaid their insured mortgage. Finally, Chapter 6 offers conclusions and policy implications for the study as a whole.

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2. Research Objectives and Methodology

2.1 Research Objectives

The primary objective of this study was to aid HUD in understanding the factors leading to opt-out decisions made by owners of multifamily housing. Those factors included the role played by the characteristics of the owners, the housing itself, the surrounding neighborhoods, and the cities where the properties were located. We sought to identify the factors that were correlated with these decisions and to determine what patterns could be detected as a result. The study also sought to identify policy implications of owners' decisions to opt in or out of the program. This could help HUD identify any needed changes to policies to encourage property owners to maintain their properties in the stock, or to assist tenants when properties leave the stock. In the study, we consider and examine the attributes of these properties, which may influence whether the properties remain assisted by the HUD programs or leave the stock. For most of the quantitative and qualitative analysis, properties—rather than units—are the unit of analysis.[4] The research analyzes HUD and other secondary source data, and then supplements this analysis with case studies that are based on site visits to a sample of multifamily properties.

More specifically, the study addresses the following questions:

- Do basic characteristics, such as physical attributes and neighborhood characteristics, of project-based multifamily assisted properties explain the major differences between opt-outs/prepayments and opt-ins?

- Are certain types of owners and properties more likely to opt out/prepay or remain in the HUD programs, such as profit-motivated owners or properties with few or many Section 8 units?

- Have prepayments or Section 8 contract expirations occurred at the same time or at different times and, if at different times, which occurs first?

- What has been the experience of properties held by nonprofit owners and are they more likely to opt in than to opt out or prepay?

- Do location and ownership type make it possible to predict the likelihood of a property opting out/prepaying or opting in?

- What are some of the non-economic reasons that affect an owner's decision not to prepay or let his or her Section 8 contracts expire?

[4] An exception is the affordability analysis that relies on a non-random sample of units for which we were able to obtain post-opt-out or prepayment rent data.

- Is the affordability of rents in opt-out properties for low-income families affected and are units affordable with regular or enhanced vouchers?

We describe our analytic strategies and methodological approach in greater detail in the sections that follow.

2.2 Data Sources and Data Sets

Data Sources

The universe of properties we examined included "opt-out" and "prepayment" properties as well as properties that have remained in the HUD programs ("opt-in"). We sought information on the physical and financial characteristics, owner characteristics, and neighborhood characteristics of these properties, as well as on the residents in these properties. These data were obtained from a variety of HUD sources as well as the U.S. Census Bureau. Those sources included:

HUD Office of Housing's (FHA) Real Estate Management System (REMS) Data. The primary database we used for describing physical, financial, and owner characteristics of properties was REMS. This database contains a wealth of property- and contract-level information for the entire portfolio of multifamily properties managed by FHA. It includes variables on Section 8 contract status, contract expiration date, development size, unit mix (that is, number of one-bedroom units, two-bedroom units, and so forth), occupancy type (family, elderly/disabled), HUD assistance program type (section of the Housing Act), and the location of the property.

HUD FHA's Multifamily DataMart (MPRD) files. We used two extracts of FHA's multifamily MPRD files, a current (2004) extract and a prior-year (1998)[5] extract, to define the universe of study properties. The MPRD database contains information on properties that are active and currently receiving HUD subsidies. A key advantage of the MPRD database is that it pulls raw data at the mortgage and contract levels from REMS and F-47 and organizes them into project-level variables. However, it does not include any information on properties with a terminated mortgage/assistance contract, so we had to rely on REMS for this information.

HUD FHA's Multifamily Insurance System (MFIS) or F-47 data. We used FHA's F-47 data to support defining the universe of properties (essentially the Section 236 and BMIR properties) as well as to examine the types of FHA mortgage financing used in the study properties. The F-47 data system is used to track the origination, payment status, and termination of FHA-insured mortgages. It also includes financing information such as loan terms, Section of the Housing Act (SOA), monthly debt service amount, and unpaid principal balance.

[5] The 1998 extract was available from previous work.

- **HUD Real Estate Assessment Center (REAC) Data.** We used REAC data to compare the physical condition and financial operating characteristics of the study properties. Since 1998, REAC has been collecting very specific financial and physical information on the entire HUD rental stock. Property owners are required to submit Annual Financial Statements (AFS) electronically to REAC. Currently, these annual snapshots on the financial performance of the assisted stock are available from 1998 to 2003.[6] REAC has also devised a composite score that measures the overall financial health of each property's operation. HUD uses AFS data to determine whether a property is financially troubled or at risk of becoming financially troubled.

  A physical inspection is performed annually on each property to identify neglected properties in need of repair and to ensure that timely maintenance is performed on all properties. REAC inspectors summarize the inspection result for each property into a numerical score ranging from 0 to 100. A property with an inspection score below 60 is considered sub-standard. Currently, physical inspection data are available for 1998 to 2003.

Tenant Rental Assistance Certification System (TRACS). We used TRACS data to examine tenant characteristics of households affected by the opt-in/opt-out choices of owners. TRACS is FHA's system for income certification of households participating in the project-based rental assistance programs. A household-level administrative database, TRACS provides a snapshot of the assisted households at the end of each fiscal year. In addition to household income, assets, and public assistance status, TRACS contains an array of household demographics relevant to this study.

PIH Information Center (PIC) data. For the affordability analysis, we used a 2005 extract of PIC to link a group of voucher households to properties that either opted out of the Section 8 program or prepaid their insured mortgage. We then used information from PIC on gross rents paid to the owners to assess whether they were renting above or below the FMR. PIC is the TRACS equivalent for households participating in HUD's Public Housing and Housing Choice Voucher programs. Administered by local public housing agencies (PHAs) and HUD's Office of Public and Indian Housing (PIH), it contains many of the same data elements that are collected in TRACS and REMS. Electronic records are entered into the system and updated periodically by local PHAs.

1990 and 2000 Census of Population and Housing data. We used Census Bureau tract-level data to compare neighborhood characteristics of opt-in/opt-out properties. We examined characteristics such as geographic region, median rent level, vacancy rates, median household income, race/ethnicity, and poverty rate.

FHA's List of Opt-out Properties (Opt-out List). To determine which properties were affected by opt-out choices, we used a list maintained by FHA's Office of Program Systems Management of HUD Section 8 properties that have completed the opt-out process since

[6] Between 1993 and 1998, AFS were submitted in hard copy and entered into an electronic database by a HUD contractor. However, these data are not in the REAC database.

1992. Records in the list are identified by the reporting fiscal year Section 8 contract number and REMS project number, and they can be easily linked to the REMS data. We used a list that was dated November 2004.

As noted above, the main source of data for much of the quantitative research was REMS. Given how contract renewal information is handled in the REMS system, however, it is difficult to identify properties that have opted in at contract expiration for a particular fiscal year. The REMS system immediately overwrites the prior contract expiration date for a project when the Section 8 renewal is approved. Therefore, with a single extract of the REMS data, if the expiration date is in the future it is impossible to determine whether the owner had the opportunity to opt out and, instead, chose to renew and opt in.

Our solution was to use two MPRD extracts made at different times. We used extracts from 1998 and 2004 to identify the universe of Section 8 properties. The MPRD extracts allowed us to track changes in a property's status between 1998 and 2004, the period during which most opt-outs have occurred. To identify the universe of properties financed by Section 236 or Section 221(d) (3) BMIR mortgages, we used the F-47 Multifamily Mortgages Database. We merged the F-47 sets with the MPRD extracts by REMS project identification number and by FHA case number to create the universe of analysis properties. (See Section 2.3 for further discussion of this universe.)

The Opt-out List maintained by FHA's Office of Program Systems Management identified the group of Section 8 opt-out properties for the study. Using the two MPRD extracts, the F-47 file, and factoring in properties on the Opt-out List, we could identify all the properties that have opted out or prepaid since 1998, as well as identify those properties that fell into foreclosure or were referred to the Enforcement Center between 1998 and 2004.

Data Elements

Certain variables had a substantial amount of missing data for properties that have left the inventory, such as for opt-outs/prepayments and foreclosure properties. For example, 60 percent of the opt-out and foreclosure properties had missing management review score data. Some of those data are not available, most likely because the owners have left the program either through opt out or foreclosure; they are thus no longer required to comply with reporting requirements. Table 2.1, below, summarizes the data elements and sources used for the quantitative analysis.

Table 2.1. Data Elements and Sources for the Quantitative Analysis

Data Element	Data Source
Development size (total number of units)	REMS/MPRD
Unit mix (distribution of units by bedroom type)	REMS/MPRD
Number of assisted units	REMS/MPRD
Occupancy type (family, elderly, or people with disabilities)	REMS/MPRD
Building structure type (garden, high-rise, row-house, etc.)	REMS/MPRD
HUD assistance program type (NC/SR, Section 236, etc.)	REMS/MPRD
Sponsor/developer type (for-profit, limited dividend, nonprofit, or other)	REMS/MPRD
Address (street and ZIP code)	REMS/MPRD/PIC
Census tract identification number	REMS/MPRD
Type of location (central city, suburb, non-metropolitan)	REMS/MPRD
Financed by state housing finance agency (bond financed)	REMS/MPRD
Section 8 contract status	REMS/MPRD
Section 8 contract expiration date	REMS/MPRD
Section 8 contract rent (current)	REMS/MPRD
Current rent-to-FMR ratio	REMS/MPRD
FMR	REMS/MPRD
Management review rating	REMS
REAC physical inspection score	REAC
REAC financial performance score	REAC
Operating costs, revenues, reserves for replacement, and surplus cash	REAC/AFS
FHA mortgage insurance type (Section of the Housing Act)	F-47/MFIS
FHA mortgage identification number	F-47/MFIS
Primary/supplemental loan indicator	F-47/MFIS
Loan status (active or terminated)	F-47/MFIS
Date of loan termination	F-47/MFIS
Reason for loan termination	F-47/MFIS
Age of original mortgage (proxy for property age)	F-47/MFIS
Original mortgage amount	F-47/MFIS
Unpaid principal balance (UPB)	F-47/MFIS
HUD-held or HUD-owned mortgage status	F-47/MFIS
Enhanced voucher payment amount	PIC
Length of residence	TRACS
Household size	TRACS
Race/ethnicity of household head	TRACS
Disability status of household head	TRACS
Age of household head	TRACS
Gender of household head	TRACS
Neighborhood demographic and housing characteristics (median rent, vacancy rate, poverty rate, etc.)	1990 and 2000 Census of Population and Housing

2.3 Methodology

Study Approach—Three Parts of Study

The study began with a quantitative analysis that compared opt-out and prepayment properties (opt-out/prepays) with those that remained in the Section 8 program (opt-ins). The descriptive tables compare these two categories of properties with properties that are in foreclosure or have been referred to the Enforcement Center, and with all other properties. Using data extracted from HUD's administrative data systems, including the REMS, we examined a variety of property characteristics, including number of units, percent of assisted units, occupancy type, ownership characteristics, age of building, location of the property, and rent. The quantitative analysis also used multivariate logistic regressions that focused on Section 8 properties only, and attempted to predict the owners' opt-out/opt-in decisions based on an array of property, owner, program, and location variables.

In the second part of the study, we present qualitative descriptions of case studies to contextualize the data. By visiting Section 8 properties whose owners have opted out of the program and properties whose owners have opted in within the same metropolitan statistical areas (MSAs), we sought to identify factors that lead some property owners to opt out and other owners to remain in the HUD program. The observations we present are from visits we made to Sacramento, Dallas, and Cincinnati, three cities in which a significant number of opt-outs have already occurred; we visited four properties in each, for a total of 12 properties.

The third part of the study is a separate activity, consisting of a quantitative assessment of the affordability of units after properties leave the stock either through the owners' opting out of the Section 8 program or prepaying their assisted mortgage.

Methodology for Conducting Quantitative Analysis—Cross Tabulations

To develop a clear understanding of the types of properties the study would cover, we analyzed the data to create descriptive cross-tabulations showing a variety of characteristics of the properties. In descriptive cross tabulations, we calculated percentages, means, and medians for properties rather than units. For example, in Table 3.2 on page 24, the percentage of properties owned by different ownership types is calculated as a percent of properties—not units. For this effort, we created a master data file that incorporated all relevant variables for the 22,471 unique projects identified in our analysis.

For the quantitative descriptive analysis, we examined the properties along six dimensions according to the following characteristics:

- Property
- Owner
- Financing
- Location
- Tenant
- Physical and financial operating.

Analytic Categories of Properties

Types of Properties

To define the analytic categories of projects for this study, we began by sorting the universe of study properties into three major groupings, according to the type(s) of HUD assistance originally associated with them in 1998. The three major groupings are the following:

> *Type 1.* Properties currently or once assisted by project-based Section 8 rental subsidies and not financed by Section 236 or Section 221(d)(3) BMIR mortgages (75 percent).
>
> *Type 2.* Properties financed by Section 236 or Section 221(d)(3) BMIR mortgages that never received any Section 8 assistance (8 percent).
>
> *Type 3.* Properties currently or once assisted by Section 8 rental subsidies and financed by Section 236 or Section 221(d)(3) BMIR mortgages (17 percent).

Table 2.2 identifies these groupings and the distribution of properties in each group.

Types of Outcomes

For each of the three groupings of HUD-assisted properties, Table 2.2 further separates the properties into outcome types as of the end of 2004 based on the owner's opt-out and mortgage prepayment decisions and enforcement action. We identified a total of 16 outcome types, as shown in the table.

Properties that have opted in *since* 1998 were separated from those that opted in *before* 1998 or have not yet reached a decision point. Because the vast majority of the opt-outs have occurred since 1998, separating out the post-1998 opt-ins permits us to focus better on the 1998 through 2004 period. Comparing the characteristics of properties in these two groups can shed light on the determinants of the owners' opt-out/opt-in decisions.

Table 2.2. Properties and Units by HUD Assistance Type and Outcome

Outcomes of HUD-Assisted Properties	Number of Properties	Number of Units
1. Section 8 only; no Section 236/BMIR in place		
1A1: Opted in since 1998	9,268	635,582
1A2: Opted in before 1998 or not yet reached opt out/in point	6,056	370,010
1B: Opted out	894	47,916
1C: Foreclosure/enforcement center	582	28,995
Total	**16,800**	**1,082,503**
2. Section 236/BMIR only; no Section 8 in place		
2A: Active	348	36,770
2B: Prepaid	429	45,088
2C1: Foreclosure/enforcement center	1,018	73,514
2C2: Other termination	93	9,453
Total	**1,888**	**164,825**
3. Section 8 + Section 236/BMIR		
3A1: Opted in since 1998; Section 236/BMIR active	1,858	149,561
3A2: Opted in before 1998 or not yet reached opt out/in point; Section 236/BMIR active	49	1,695
3B: Opted out of Section 8 + prepaid Section 236/BMIR	392	27,689
3C1: Opted in since 1998; prepaid Section 236/BMIR	588	57,642
3C2: Opted in before 1998 or not yet reached opt out/in point; prepaid Section 236/BMIR	3	78
3D: Opted out of Section 8; Section 236/BMIR active	77	3,810
3E1: Foreclosure/enforcement center	785	80,436
3E2: Other termination	31	2,924
Total	**3,783**	**323,835**
Grand Total	**22,471**	**1,571,163**

Categories Used for Analysis

We combined the initial groupings identified in Table 2.2 into four categories, as follows:

(1) “Opt-in” refers to properties whose owners chose to renew an expiring project-based Section 8 contract since 1998. When a given contract expires, the owner must make an active decision whether to renew or not. Those owners whose properties were financed with a Section 236 or Section 221(d) (3) BMIR mortgage and who are eligible to prepay do not face such an explicit, time-limited choice.

(2) The “Opt-outs/Prepays” category comprises properties whose owners have chosen not to renew their project-based Section 8 rental assistance contracts. Prepayments are properties with a subsidized mortgage (Section 236 or Section 221(d) (3) BMIR) whose owners chose to prepay their mortgage and end their low-income use restriction.

Sometimes this decision was made when a Section 8 contract expired. The vast majority of opt-outs/prepays have happened since 1998.

(3) The "Foreclosure/Enforcement" category includes properties that, as of December 2004, faced foreclosure or other payment or compliance challenges. "Foreclosure" refers to a property whose owner is unable to make timely mortgage or debt service payments. Upon conclusion of foreclosure, the creditor takes possession and can dispose of the property in accordance with the law and particular circumstances surrounding a specific property. "Enforcement" properties are those that have been referred to HUD's Enforcement Center for having some form of physical or financial difficulties and requiring remedial action. We have grouped Foreclosure and Enforcement properties together since they reflect properties that are troubled.

(4) "All other" describes properties that do not belong in categories 1 through 3. This group primarily consists of properties whose owners either opted in before 1998 or have not yet reached an opt-out decision. The "all other" category comprises properties whose owners have not prepaid and do not have Section 8 contracts, those that have Section 8 contracts that have not yet expired, those reflecting pre-1998 opt-ins, and a few other miscellaneous, idiosyncratic properties.

Table 2.3 shows how the Table 2.2 groups were combined into the four basic categories used in the analysis. These groupings were based on similarity of the outcomes. For example, those properties considered "Opt-In" were those that, based on the data, have clearly opted in since 1998. This includes two groups: those properties that have Section 8 only (Group 1A1), and those that have Section 8 and are financed by either a Section 236 or 221(d) (3) BMIR mortgage (Group 3A1).

Table 2.3. Categories of Analysis

Analysis Category	Table 2.2 Groups	# of Properties	# Units
Opt-Ins	1A1, 3A1	11,126	785,143
Opt-Outs/Prepays	1B, 2B, 3B	1,715	120,693
Foreclosure/Enforcement	1C, 2C1, 3E1	2,385	182,945
All Other	1A2, 2A, 3A2, 3C2, 3C1, 3D, 2C2, 3E2	7,245	482,382

We faced a number of challenges in defining these categories. Many of the Older Assisted properties in the study universe have already reached their initial contract expiration date and have been renewed. But because the expiration date is overwritten in REMS, it is not clear whether the contract has been renewed or not. Because we cannot clearly determine whether a property's owner renewed a contract prior to 1998, we did not include such properties in the opt-in category, but rather placed them in the "All Other" category. We do not think this is a serious flaw because there were relatively few opt-ins prior to 1998. Moreover, the present emphasis is on the distinction between opt-ins and opt-outs.

In contrast, there are some Housing Finance Agency (HFA)-financed Section 8 New Construction properties that had a 30- to 40-year contract term and, therefore, have not yet reached the opt-out/opt-in point. The remaining current stock of assisted properties does not just consist of early (pre-1998) opt-ins, but also of those that have never reached a decision point. This is the reason there are so many properties in the "All Other" category.

Methodology for Conducting Quantitative Analysis—Multivariate Logistic Regression

The quantitative analysis also included a multivariate logistic regression analysis to explain the owners' opt-out/opt-in decisions based on an array of property, owner, program, and location variables. We conducted this part of the study after examining the correlation among the variables and data patterns shown in the descriptive analysis.

Multivariate analysis is important in this context for three reasons. First, cross-tabulations may lead to incorrect inferences because they focus on only one variable at a time. For example, since Table 3.6 on page 28 shows that opt-outs tend to be located in central cities, one may conclude that properties located in central cities are more likely to opt out in general. However, this relationship might disappear after controlling for other influences, such as neighborhood location and ownership type.[7] Therefore, it is useful to test whether some of the observations found using cross-tabulations hold in a multivariate framework.

Second, multivariate analysis can help identify the consequences of opting out. For instance, if the census tract poverty rate has a strong negative influence on opting out (that is, high poverty is negatively associated with the probability of opting out), then one could conclude that opting out is reducing the number of HUD-assisted projects in low-poverty neighborhoods (that is, low poverty is positively associated with the probability of opting out).

Third, multivariate analysis allows policymakers at HUD to predict and monitor which projects currently in the Section 8 assisted-housing stock are most likely to opt out when their current contracts expire.

For a logistic regression, causality is sought between a dichotomous dependent variable and a series of explanatory variables. The dependent variable thus takes on a value of 0 or 1. In the present analysis, the outcome variable is coded "1" for opt-out properties and "0" for opt-ins. A key feature of regression analysis is that it allows us to examine the impact of each explanatory variable on the owners' decisions, while holding all other variables constant.

We confined the regression analysis to the opt-out and opt-in decisions of Section 8 properties only. Our analysis excluded projects with Section 236 or BMIR assistance. By narrowing the focus in this way, we avoided having to account for two different decisions (opting out of project-based Section 8 and mortgage prepayment) with the same model. The

[7] Cross-tabulations presented in the previous section remain valuable because they highlight the differences between the opt-out/prepay properties and the other property groups. In addition, as a descriptive tool, they show how the opt-out/prepay properties are distributed in terms of location, program, owner, and project characteristics.

model thus provides a probabilistic assessment of the variables that influence owners' opt-in and opt-out behavior. Moreover, to ensure that the model focuses on projects for which the owners had a choice whether to opt out or not, we limited the study properties to the opt-ins and opt-outs since 1998 (that is, groups "1A1" and "1B" in Table 2.2).

This process resulted in a total of 8,992 projects with non-missing values for all the variables included in the model. Among them, 8.5 percent (763 projects) are opt-outs.

Methodology for Conducting Case Studies

The case studies included two opt-out and two opt-in properties in each of the three selected MSAs (Cincinnati, Dallas, and Sacramento) for a total of 12 properties. The areas were first chosen based on the large number of opt-out properties located in those areas. Other criteria for selection included geographic distribution of the three metropolitan areas and varying trends in population growth. The case studies supplement the quantitative analysis by addressing issues that cannot be addressed using available data, and by providing additional context for the study.

The case studies are the source of information on the motivations of owners who choose to opt out of their Section 8 contracts and those who continue to remain in the program. The case studies also address questions relating to ongoing affordability of Section 8 properties and site issues associated with opting out and opting in. Given the small sample size, we did not examine any prepayment properties.

Methodology for Conducting Affordability Analysis

To address accurately the question of how affordable the units remain after properties opt out or prepay, we would need to see the full rent roll of these properties. Ideally, we would identify in REMS the addresses of buildings in properties that have opted out or prepaid, and then use the PIC system to locate units at those addresses that were rented to recipients of tenant-based vouchers, including those with enhanced vouchers. These data are not available, however, in any of the data systems to which we have access, and it would be beyond the resources available for this research to gather this information from a suitable sample of properties. We do have information on the rents paid by assisted residents in these developments, and so we used the proxy method of examining the rents of housing units in opt-out/prepay properties currently occupied by tenants with Housing Choice Vouchers.[8] However, HUD currently does not have a file that contains addresses of all buildings in assisted properties. It is thus not possible to identify all voucher recipients who live in opt-out/prepay properties. With assistance from HUD, we were able to link a group of voucher recipients (using an extract of PIC from late 2004) to the opt-out/prepay properties (from REMS) using the property owners' Tax Identification Number (TIN), which is common

[8] Gross rents to the owners are reported in line item 12P of Form HUD-50058.

across both database systems. We identified a total of 24,883 records of such voucher recipients by this method.

Because TIN is owner-specific rather than property-specific, however, multiple properties belonging to the same owner can have the same TIN. Thus, we used an address-matching algorithm to further ensure that the PIC addresses of the voucher recipients found in the TIN matching were in the properties with address locations of the opt-out/prepay properties identified in REMS. This check yielded a final study sample of 9,012 voucher recipients. Gross rent information was available on the PIC file for 8,956 of the housing units occupied by these voucher recipients. Together, they represent housing units from 449 opt-out properties. These units are 34 percent of the 26,691 total units in these properties. We identified a total of 2,267 units that received enhanced vouchers and 6,689 that received regular vouchers.

This approach does have a number of drawbacks. Properties that have converted to condominiums will be left out of the analysis. Moreover, if rent increases are very high and all original tenants move, then we are unable to track these properties because they will be unaffordable with vouchers. Both of these drawbacks bias the results toward affordability.

3. Results from the Quantitative Analysis

The quantitative analysis produced some telling results about the characteristics of the properties and their owners, as well as physical and economic factors associated with the opt-in opt-out decision. Key findings include the relationship between property location, size, and age and owners' decisions to opt in or out. In this chapter, we describe the insights yielded by the analysis. The cross-tabulations (presented in Tables 3.1 through 3.8) show that properties more likely to opt out include properties that are older, occupied by families, owned by for-profit owners, or where the rents are substantially below the FMRs. In the first part of the chapter, we include a series of tables describing the characteristics of four groups of properties: opt-out/prepay properties, opt-in properties, foreclosure/enforcement properties, and "all other" properties. In the second, we summarize results from the multiple regression analysis that explain the opt-out/opt-in decision for the subset of Section 8 properties. These analyses yielded information about:

- The basic characteristics of properties in the program and what the major differences are between opt-outs/prepays and opt-ins.
- Whether certain key factors, such as types of owners or kinds of properties, are more likely to opt out/prepay.
- The timing of prepayments and Section 8 contract expirations.
- The disposition of older, nonprofit properties.
- Likelihood of a property in a particular location with a particular ownership type opting in or opting out/prepaying.

Specific key findings of the logistic regression model are consistent with the cross-tabulations and show that:

- Properties with rents that were less than 80 percent of the FMR were more likely to opt out. These results are discussed more fully in Section 3.2, Multivariate Analysis of Opt-out Decision. To see the key findings noted here in context, see Table 3.11, Coefficient Estimates of Opt-out Logistic Regression Model.
- Family occupancy type properties were twice as likely as elderly housing properties to opt out.
- Properties operated by nonprofit organizations were much less likely to opt out than were properties operated by for-profit owners.

3.1 Descriptive Cross Tabulation Analyses

This section presents the results of a series of descriptive analyses comparing several important characteristics of properties that have opted out/prepaid with those that opted in, as well as those that have undergone foreclosure or enforcement action. Properties were examined along six dimensions according to the following characteristics:

- Property
- Owner
- Financing
- Location
- Tenant, and
- Physical and financial operating.

The unit of analysis is property. Property-level descriptions allow a focus on outcomes by ownership entity. Small properties have as much weight as large properties. Decisions by owners in the Section 202 and 515 programs, with small unit counts per mortgage, have greater influence in this approach.

Property Characteristics

This section describes several important characteristics of properties in the study universe. Table 3.1 summarizes the results by property characteristics.

Table 3.1. Property Characteristics

Property Characteristics	Opt-ins	Opt-outs/ Prepays	Foreclosure/ Enforcement	All Other	Total
Number of properties	11,126	1,715	2,385	7,245	22,471
Percent of properties	49.5%	7.6%	10.6 %	32.2%	100.0%
Development Size					
Less than 50 units	38.4%	32.2%	33.1%	47.7%	40.4%
50–99 units	30.2%	25.5%	27.6%	24.0%	27.6%
100–199 units	25.3%	30.5%	26.2%	21.5%	24.6%
200 or more units	6.2%	11.8%	13.1%	6.8%	7.4%
Average number of units	81	98	103	78	83
Unit Size					
0–bedroom units	7.4%	2.9%	4.0%	7.5%	6.6%
1–bedroom units	50.2%	30.2%	24.7%	54.7%	46.8%
2–bedroom units	28.2%	48.2%	45.0%	25.4%	31.1%
3–bedroom units	12.4%	17.1%	22.3%	10.9%	13.5%
4+–bedroom units	1.8%	1.6%	4.0%	1.6%	2.0%
Average number of bedrooms	1.51	1.84	1.98	1.45	1.57

Table 3.1. Property Characteristics (continued)

Property Characteristics	Opt-ins	Opt-outs/ Prepays	Foreclosure/ Enforcement	All Other	Total
Occupancy Type					
Elderly/disabled	49.2%	12.8%	8.9%	62.7%	47.1%
Family	50.8%	87.2%	91.1%	37.3%	52.9%
Building Type					
Row house	9.0%	7.1%	7.7%	10.1%	9.1%
Townhouse	1.8%	3.2%	3.9%	5.0%	3.1%
Semi-detached	8.5%	7.5%	10.0%	6.8%	8.0%
Garden/walkup	40.1%	60.7%	51.7%	30.1%	39.4%
Mid-rise	1.7%	0.5%	0.6%	4.1%	2.3%
Mixed/group	11.7%	10.6%	9.8%	13.7%	12.1%
Mixed High-rise	27.3%	10.4%	16.3%	30.2%	26.0%
HUD Program Type					
Newer assisted	69.9%	29.8%	10.9%	76.8%	63.4%
Older assisted	30.1%	70.2%	89.1%	23.2%	36.6%
Detailed HUD Program Type					
Sec. 8 NC/SR	33.8%	23.6%	6.1%	11.8%	23.1%
Sec. 202	16.7%	0.9%	1.2%	33.5%	19.5%
Sec. 8/LMSA	25.7%	41.7%	30.4%	8.6%	21.8%
Sec. 8/515	12.9%	2.4%	0.5%	0.6%	6.9%
Sec. 8/HFDA	5.9%	2.5%	1.0%	30.3%	13.1%
Sec. 8/Preservation	2.5%	0.2%	2.3%	0.9%	1.8%
Sec. 8/PD	1.6%	3.0%	6.9%	1.6%	2.2%
Sec. 8/Mod. Rehab.	0.6%	0.5%	2.0%	0.7%	0.8%
Rent Supp/RAP	0.3%	0.2%	1.8%	6.0%	2.3%
No Rental Subsidy	0%	25.1%	47.7%	6.1%	8.5%
Average Percentage of Assisted Units	87.1%	72.1%	83.4%	85.8%	85.2%
Categories of Rent-to-FMR ratio					
Below 80% FMR	14.9%	59.0%	49.4%	13.9%	19.3%
Between 80% & 100%	24.9%	26.5%	29.5%	19.2%	23.3%
Between 101% & 120%	25.5%	9.5%	14.0%	19.4%	21.8%
Between 121% & 130%	10.8%	2.3%	3.1%	9.3%	9.3%
Between 131% & 140%	7.4%	1.5%	1.5%	8.8%	7.1%
Between 141% & 160%	9.4%	0.7%	1.5%	13.6%	9.8%
Over 160% FMR	7.1%	0.4%	0.9%	15.9%	9.3%
Building Age Categories					
Before 1975	22.6%	53.1%	56.7%	16.8%	25.4%
1975 – 1979	22.4%	17.5%	13.1%	20.9%	20.8%
1980 – 1985	52.3%	25.7%	23.1%	30.3%	40.9%
After 1985	2.7%	3.6%	7.0%	32.0%	12.9%

Note: The categories are largely all inclusive so columns add to 100 percent. Each cell shows the percentage of subjects who share the combination of traits. In this report, missing values are omitted from totals. Thus, percentages of records with non-missing values are displayed. Only extant records are included in the analysis.

Table 3.1 shows the following key findings:

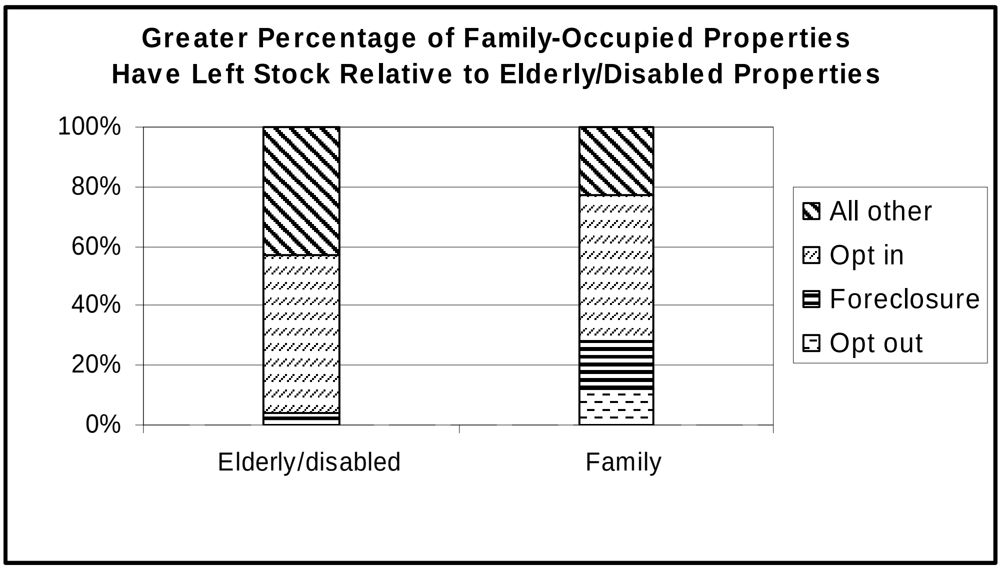
- The ratio of rents in opt-out/prepayment properties relative to their market rents (as reflected by HUD's FMR) generally tend to be lower than for opt-in properties, reflecting the potential economic advantage of the opt-out/prepayment decision for those properties.[9]

- Older Assisted properties are significantly more likely than Newer Assisted properties either to opt out (that is, in some terms to be financially successful) or to be troubled (that is, to be in foreclosure/enforcement).

- Properties designated for the elderly/disabled represent more than 49 percent of the opt-in properties, but only 12.9 percent of opt-out/prepays and 8.9 percent of the foreclosure/enforcement categories. Conversely, 91.1 percent of the properties in foreclosure/enforcement are family-occupied properties and 87.2 percent of opt-outs/prepays are family-occupied.

The latter point is significant and can be viewed in another manner. Figure 3.1 shows that nearly 30 percent of all family-occupied properties have left the stock because of opt-out/prepayment or foreclosure/enforcement, whereas less than 4 percent of elderly and disabled properties have left the HUD-assisted stock.

Figure 3.1. Status of Properties by Occupancy Type



[9] The prevalence of above-FMR rents on opt-ins, despite Mark-to-Market legislation, likely represents three factors: properties exempt from Mark-to-Market, properties that had site-specific market rent determinations that were higher than FMR, and "exception rent" properties that were restructured at above-market rents in the Mark-to-Market program.

Table 3.1 shows the following additional findings regarding differences in property characteristics:

- Opt-in properties are more likely to include zero- and one-bedroom units, consistent with an elderly/disabled tenancy.
- Opt-out/prepayment and foreclosure properties are more likely to include two- and three-bedroom (family) units.
- Buildings with units for large families (four or more bedrooms) are found more frequently among foreclosure/enforcement properties than among properties with other outcomes.
- The percentage of opt-outs with LMSA contracts[10] was 41.7.
- One-quarter of the opt-out/prepay group did not have any Section 8 contracts, but only subsidized mortgages prepaid by the owner.[11]
- Nearly half (47 percent) of the foreclosure/enforcement properties were Older Assisted properties with no rental assistance.
- Buildings constructed before 1975 were prevalent in the opt-out/prepay and foreclosure/enforcement categories.

Owner Characteristics

In this section we examine the distribution of the properties by ownership type and management performance assessment ranking. HUD field office staff rank properties based on the overall management performance of each project. These comparisons of owners' relative performance in managing their properties to comply with HUD standards reveal certain factors underlying their decisionmaking, as summarized below. The assessment ranking comprises four categories: superior, satisfactory, below average, and unsatisfactory. Both ownership and management ranking information are available for only a percentage of properties as shown in Tables 3.2 and 3.3. While incomplete, the data provide a sample that is large enough for us to draw valid inferences. Results for Table 3.2 are summarized as follows:

[10] LMSA assistance was usually provided to properties with financial difficulties. The properties could have been assisted or unassisted, and the percentage of LMSA could vary from a few units to 100 percent of the property. The addition of subsidy allowed properties to reduce turnover and market to potential residents who otherwise could not afford the rent. Previously unassisted properties that became partially assisted continued to operate in a market rate environment and would find opting out an easier task if market conditions improved.
[11] These properties benefited from mortgage subsidy but had a relatively higher income tenancy, since they selected tenants who could afford rents without income-based subsidy. Income limits at entrance for residents, depending on program, were 80 or 95 percent of median income; residents could remain if incomes increased.

- For-profit owners (limited dividend and profit motivated) have a higher proportion of representation in both the opt-in and opt-out/prepay categories relative to their percentage of the total group of properties.

- Most properties received a management review score of “satisfactory” or better.

- Not surprisingly, the foreclosure/enforcement category has the highest percentages of “below-average” or “unsatisfactory” projects.

- Somewhat more surprising is that the opt-out/prepay category has lower management review scores than the opt-in category. Some owners who chose to opt out may have done so because of disagreements with HUD housing management staff or may have been delaying management or property improvements until after they left the program. Conversely, owners choosing to stay in the program may attempt to keep their properties in compliance with HUD rules.[12]

Table 3.2. Owner Characteristics

Owner Characteristics	Opt-ins	Opt-outs/ Prepays	Foreclosure/ Enforcement	All Other	Total
Number of properties	11,126	1,715	2,385	7,245	22,471
Percent of properties	49.5%	7.6%	10.6%	32.2%	100.0%
Ownership Type					
Nonprofit	36.0%	9.2%	27.9%	61.3%	41.9%
For-profit	61.8%	86.1%	63.4%	33.5%	54.5%
Other	2.2%	4.7%	8.8%	5.2%	3.6%
Total	100%	100%	100%	100%	100%
Missing data	8.5%	53.9%	53.5%	27.7%	22.9%
Management Review Score					
Average score	2.03	2.25	2.39	2.03	2.08
Superior (score = 1)	9.7%	7.6%	3.5%	14.2%	10.3%
Satisfactory (score = 2)	80.1%	69.7%	68.0%	74.7%	76.3%
Below average (score = 3)	7.4%	13.5%	15.6%	6.8%	8.6%
Unsatisfactory (score = 4)	2.6%	8.3%	12.0%	2.9%	4.1%
Not available	0.1%	0.8%	0.1%	1.4%	0.9%
Total	100%	100%	100%	1.4%	100%
Missing data	9.8%	64.2%	59.6%	34.7%	27.3%

[12] Renewals with below average or unsatisfactory ratings may be explained by commitments to rehabilitation, management, or ownership changes. In recent years the Mark-to-Market program has restructured mortgages on a significant number of troubled properties, providing for rehabilitation and significant additions such as air conditioning, which offers owners with negative management reviews an opportunity to correct underlying property problems.

The percentage of nonprofits that opted out was low. To understand why, we performed additional analysis to look at the disposition of the nonprofit projects by HUD assistance type (Older Assisted versus Newer Assisted). Findings are presented in Table 3.3.

As can be seen in the table, a very small portion of nonprofit-owned properties have opted out or prepaid. Of the older nonprofit-owned properties, two-thirds have chosen to opt in. Fewer than half of the newer nonprofits have chosen to opt in, but more than half of these properties are in the "all other" category, generally because they opted in before 1998 or have not yet reached the decision point. This finding is consistent with the fact that in many cases nonprofits are precluded from leaving the stock. In addition, many nonprofits are motivated by the goal of providing affordable housing to low-income people, and would not opt out even if they could leave the stock.

Table 3.3. Nonprofit Owner Characteristics

Type	Opt-ins	Opt-outs/ Prepays	Foreclosure/ Enforcement	All Other	Total	Total Number of Properties
Newer Nonprofit	45%	0.5%	0.5%	54%	100%	5,332
Older Nonprofit	65%	3%	14%	19%	100%	1,916

Financing Characteristics

Table 3.4 displays the type of financing for the properties. It shows the following:

- FHA-insured properties make up the bulk of opt-ins (61.4 percent), opt-outs/prepays (84.6 percent), and foreclosure/enforcement (77.4 percent) properties, but only 21.9 percent of "all other" properties.

- A large portion (more than 70 percent) of FHA-insured properties have required an opt-out/prepay or opt-in choice, reflecting the maximum 20-year Section 8 contracts for New Construction/Substantial Rehabilitation and the maximum 15-year contracts for Loan Management Set-aside and conversions.

- Virtually all of the USDA's 515 program owners have had to make a decision regarding opt out, and a very large proportion have decided to opt in.[13] The result is that these properties, averaging about 30 units per mortgage, are highly represented in the "opt-in" category, and very few appear in the "all other" category.

- Fewer 202/811 properties (less than half) have been in a choice situation, but they nonetheless make up a sizeable fraction of the opt-in category (18.3 percent).

[13] This may have to do with restrictive prepayment conditions, currently a subject of litigation with USDA.

- Housing Finance Agencies (HFAs) that did financing without FHA insurance generally required 40-year Section 8 contracts for those properties, compared with 20-year contracts for FHA-insured properties. Thus, most HFA non-insured owners were not in a situation requiring them to make an opt-out/opt-in choice during the study period.

- Of those HFA-financed properties that did face the decision, most opted in. When looking only at opt-in and opt-out/prepay properties, of a total 702 properties in these two categories, only 42 opted out/prepaid—6 percent of the total number.

Table 3.4. Financing Type

Financing Characteristics	Opt-ins	Opt-outs/ Prepays	Foreclosure/ Enforcement	All Other	Total
Number of properties	11,126	1,715	2,385	7,245	22,471
Percent of properties	49.5%	7.6%	10.6%	32.2%	100%
Primary Form of Financing					
FHA Insured	61.4%	84.6%	77.4%	21.9%	52.1%
Section 202/811	18.3%	1.5%	1.6%	33.6%	20.2%
Section 515	12.6%	2.3%	0.5%	0.5%	6.6%
All Other	7.7%	11.5%	20.6%	44.0%	21.1%
Total	100%	100%	100%	100%	100%
HFA Related Properties					
Number of HFA related properties	660	42	21	2,187	2,910
Percent of HFA related properties	22.6%	1.4%	0.7%	75.2%	100%
FHA-insured	82.1%	64.3%	47.6%	5.3%	23.8%
Non-insured	17.9%	35.7%	52.4%	94.7%	76.2%
Total	100%	100%	100%	100%	100%

Location Characteristics

We discuss the characteristics of each census area below. To clarify what states fall under each category, we first provide Table 3.5, which lists the states within each Census Division.

Table 3.5. States Associated with Defined Census Division

Census Division	States
New England	Connecticut, Massachusetts, Maine, New Hampshire, Puerto Rico, Rhode Island, Vermont
Mid Atlantic	New Jersey, New York, Pennsylvania
East North Central	Illinois, Indiana, Michigan, Ohio, Wisconsin
West North Central	Iowa, Kansas, Minnesota, Missouri, North Dakota, Nebraska, South Dakota
South Atlantic	District of Columbia, Delaware, Florida, Georgia, Maryland, North Carolina, South Carolina, Virginia, West Virginia
East South Central	Alabama, Kentucky, Mississippi, Tennessee
West South Central	Arkansas, Louisiana, Oklahoma, Texas
Mountain	Arizona, Colorado, Idaho, Montana, New Mexico, Nevada, Utah, Wyoming
Pacific	Alaska, California, Fed State of Micronesia, Guam, Hawaii, Northern Mariana Islands, Oregon, Palau, Virgin Islands, Washington

Table 3.6 displays geographic, economic, and racial/ethnic characteristics of the properties:

- The Pacific Census Division, with 13 percent of the properties, had 21 percent of the opt-outs/prepays. The Mountain and West South Central Divisions were also highly represented in opt-outs/prepays, relative to their percentages of the sample.

- Opt-outs/prepays tended to be more often in suburban and metropolitan/central city locations and less frequently in non-metropolitan locations than all projects in such locations.

- Opt-out/prepay properties, not surprisingly, are located in neighborhoods with relatively higher median incomes, higher median rents, and lower poverty rates and vacancy rates than opt-ins, or than the study sample as a whole.

- Foreclosure/enforcement properties (with significant missing records) have the lowest neighborhood median income and homeownership rates, and the highest vacancy rates and poverty rates. More than two-thirds of these properties are located in metropolitan/central city locations.

- Opt-in properties fairly closely mirror the racial/ethnic composition of the sample and opt-out/prepay properties, whereas foreclosure/enforcement properties have a significantly higher minority population.

Table 3.6. Location Characteristics

Financing Characteristics	Opt-ins	Opt-outs/ Prepays	Foreclosure Enforcement	All Other	Total
Number of properties	11,126	1,715	2,385	7,245	22,471
Percent of properties	49.5%	7.6%	10.6%	32.2%	100%
Census Division					
New England	7.8%	5.1%	10.7%	13.4%	9.7%
Mid Atlantic	11.4%	5.4%	12.3%	15.0%	12.2%
East North Central	18.8%	19.5%	26.5%	17.3%	19.2%
West North Central	12.1%	8.7%	8.9%	10.6%	11.0%
South Atlantic	15.6%	17.3%	12.2%	15.9%	15.5%
East South Central	9.1%	4.0%	4.2%	5.7%	7.1%
West South Central	7.2%	10.7%	8.0%	6.8%	7.4%
Mountain	5.6%	7.7%	2.5%	3.9%	4.9%
Pacific	12.5%	21.2%	14.6%	11.4%	13.1%
Total	100%	100%	100%	100%	100%
Metropolitan Location					
Suburb	26.8%	35.5%	22.9%	31.9%	28.7%
Metropolitan/central city	44.0%	51.8%	67.3%	43.6%	46.8%
Non-metropolitan	29.3%	12.7%	9.9%	24.5%	24.5%
Total	100%	100%	100%	100%	100%
Neighborhood Characteristics					
Median income	$32,365	$36,489	$28,752	$34,272	$32,944
Median rent	$491	$578	$497	$524	$509
Homeownership rate	51.3%	47.6%	40.6%	47.6%	48.7%
Poverty rate	20.0%	17.9%	26.7%	17.1%	19.6%
Vacancy rate	8.7%	7.2%	10.1%	7.5%	8.3%
Racial/ethnic composition					
Asian	2.9%	4.5%	2.8%	3.0%	3.1%
African American	21.5%	19.8%	42.1%	18.8%	22.6%
Native American/Other	9.1%	11.2%	13.4%	9.2%	9.8%
White	66.5%	64.6%	41.8%	68.9%	64.5%
Total	100%	100%	100%	100%	100%
Minority	38.5%	41.9%	64.8%	36.5%	40.9%
Non-Minority	61.5%	58.1%	35.2%	63.5%	59.1%
Total	100%	100%	100%	100%	100%

Tenant Characteristics

Table 3.7 displays characteristics of tenants in properties using data from HUD's TRACS system. Note that the descriptive categories are not discrete: for example, a household could be headed by someone who is both elderly and disabled, and also have children in residence.

Table 3.7. Tenant Characteristics

Average Tenant Characteristics	Opt-ins	Opt-outs/ Prepays	Foreclosure/ Enforcement	All Other	Total
Number of properties	11,126	1,715	2,385	7,245	22,471
Percent of properties	49.5%	7.6%	10.6%	32.2%	100%
Length of residence (years)	6.0	5.3	5.7	5.8	5.9
Household size	1.7	2.1	2.2	1.5	1.7
Percent minority-headed	42.1%	50.6%	72.7%	35.8%	42.4%
Percent household heads with disabilities	18.5%	12.5%	13.6%	29.9%	21.6%
Percent elderly-headed households	48.5%	27.9%	19.3%	47.5%	45.0%
Percent households with children	25.0%	42.8%	48.6%	16.8%	24.9%
Household income as a percentage of area median income (AMI)	27.7%	27.9%	23.8%	28.9%	27.8%

Source: 1998 and 1995 Tenant Rental Assistance Certification System (TRACS) data.
Notes: Income measures are as of 1995. All other are as of 1998.

Table 3.7 shows the following:

- Consistent with other findings (for example, the high percentage of Section 202 properties opting in), elderly headed households are highly represented in opt-in properties.
- Elderly households are the least heavily represented in foreclosure/enforcement properties.
- Households with children are highly represented in both opt-out/prepay and foreclosure/enforcement properties.
- Household income in the property as a percent of area median income (AMI) does not vary greatly, but it is lowest for foreclosure/enforcement properties.
- Minority-headed households are particularly highly represented in foreclosure/enforcement properties.

Physical and Financial Operating Characteristics

Table 3.8 displays summary physical and financial scores from the REAC systems and selected financial data and ratios. Expenses are on a per-unit per-month basis. Physical inspection scores reflect as-is condition with negative adjustments for certain health and safety issues. Generally, a score of 60 is minimally acceptable. Properties with scores of 60 and above are divided into groups requiring annual, bi-annual, and every-third-year physical inspections, based on how close the prior inspection score was to one hundred. The REAC financial performance score also is considered to be acceptable at scores of 60 and above.

Table 3.8. Physical Condition and Financial Operating Characteristics (1998–1999)

Physical and Financial Characteristics	Opt-In	Opt-out/ Prepays	Foreclosure/ Enforcement	All Other	Total
Number of properties	11,126	1,715	2,385	7,245	22,471
Percent of properties	49.5%	7.6%	10.6%	32.2%	100%
REAC Physical inspection score (1-100)					
Median	84.0	78.0	70.0	87.0	84.0
1-59	13.0%	17.8%	33.5%	10.4%	14.1%
60-69	10.1%	13.9%	16.2%	9.1%	10.5%
70-89	40.1%	42.8%	32.2%	37.1%	39.1%
90-100	36.8%	25.6%	18.1%	43.4%	36.3%
Total	100.0%	100.0%	100.0%	100.0%	100.0%
REAC Financial performance score (1-100)					
Median	73.0	70.5	69.0	73.0	73.0
1-59	23.1%	35.5%	36.1%	22.2%	24.3%
60-69	17.2%	13.9%	15.1%	18.7%	17.3%
70-89	47.6%	34.2%	27.0%	45.6%	45.1%
90-100	12.1%	16.4%	21.9%	13.6%	13.3%
Total	100.0%	100.0%	100.0%	100.0%	100.0%
Expense-to-income ratio (median)	0.60	0.72	0.80	0.54	0.59
Debt-service-coverage ratio (median)	1.18	1.24	1.15	1.07	1.14
Quick ratio (median)	0.53	0.43	0.305	0.425	0.4825
Surplus cash level (median)	$89.2	$152.3	-$157.6	-$134.1	$5.2
Reserve (median)	$1,633.7	$991.1	$1,147.2	$1,979.4	$1,669.7
Vacancy rate (median)	1.5%	3.0%	3.5%	1.0%	1.5%
Administrative Expenses (median)	$102.2	$95.6	$109.0	$106.4	$103.1
Utilities Expenses (median)	$56.4	$56.2	$70.3	$57.7	$57.4
Operating & Maintenance Expenses (median)	$110.4	$121.5	$137.4	$96.9	$109.2
Taxes & Insurance Expenses (median)	$54.9	$59.3	$62.4	$41.3	$52.5
Total Operating Expenses (median)	$330.8	$341.6	$392.0	$311.3	$329.4

Source: 1998 and 1999 REAC Financial Assessment Sub-System (FASS) data.
Note: Operating expenses are per-unit-month measures.

Table 3.8 shows the following:

- Properties in foreclosure/enforcement had the lowest median physical inspection scores, as expected, although not all enforcement is related to physical condition.

- Opt-out/prepay properties had somewhat lower physical scores than those that opted in and those that did not face an opt-in/opt-out choice in the study period. This may reflect the higher incidence of Section 202/811 properties in the latter two categories, since properties serving the elderly and people with disabilities generally have higher scores than family-occupied properties. The elderly and disabled units have fewer residents, so there is less wear in those units.

- All groups had median scores above 60 and all groups had significant percentages of properties with scores below 60.

- The opt-out/prepay category had a higher percentage of properties with scores below 60 (35.5 percent) than did the opt-ins (23.1 percent), almost the same as the foreclosure/enforcement category (36.1 percent).

- Roughly 20 percent of foreclosure/enforcement category properties had very high scores (90–100) for physical inspection and financial performance.

The table also sets forth six additional indicators of relative financial strength:

- The expense-to-income ratio is a measure of expenses (other than debt service) compared to operating income. Ratios closer to or greater than 1 indicate little or no income available to pay debt. Foreclosure/enforcement and opt-out/prepay properties had the weakest ratios.

- The debt service coverage ratio is a different measure, calculating to what extent debt service could be covered with net income. All groups had adequate debt service coverage ratios (greater than 1), with those not having an opt-in/opt-out choice to make during the study period having the lowest coverage (1.07).

- The quick ratio measures liquidity. It compares cash, cash equivalents, accounts and notes receivable to current liabilities. A quick ratio equal to 1 or above indicates ample liquidity; it implies that the project has more than enough resources to meet its financial liabilities. A higher quick ratio indicates greater financial liquidity. None of the groups showed a strong ratio of liquidity to liabilities, though the opt-ins had the highest median ratio of the groups.

- Surplus cash is a HUD-defined term that measures cash on hand against trade payables and any accrued unpaid mortgage payments. Higher ratios indicate stronger financial positions. Opt-out/prepay properties had the strongest surplus cash position and foreclosure/enforcement properties had the weakest.

- Reserve levels. HUD properties are required to maintain a reserve account for replacement and may be required to maintain a residual receipts account. In Older Assisted properties these funds become the owner's at prepayment, so they measure both financial strength and a source that potentially could be used to pay off the mortgage. For most Newer Assisted properties, residual receipts resulting from Section 8 revert back to HUD. Reserves were highest in the "all other" category, followed by the opt-ins.

- Vacancy rates were low in all categories of properties, but lowest in the "all other" category, followed by the opt-ins.

Timing of Opt-outs and Prepayments

One goal for this study was to describe the timing of opt-outs relative to prepayments in properties that did both. The analysis shows whether it is common to see prepayments and opt-outs occurring at the same time and, if not, to identify which typically comes first. Table 3.9 assesses the level of coordination, if any, between owners' decisions to prepay their mortgages and to opt out of their Section 8 contracts. For purposes of this analysis, opt-outs within a 6-month window of the prepayment were considered to occur at the "same time" as the prepayment. The usual assumption is that owners will want to time the prepayment and opt-out together. By doing so, the owner can implement higher, unregulated market rents for unassisted tenants or for previously assisted tenants who receive Housing Choice Vouchers that can allow them to remain in the housing.

Table 3.9. Timing of Opt-outs and Prepayments (Number of Properties)

Reporting FY	Opt-out before Prepayment	Prepayment before Opt-out	Opt-out same as Prepayment	Total Number of Opt-outs
1992	1	.	.	1
1994	.	1	.	1
1995	.	2	.	2
1996	4	10	3	17
1997	2	53	11	66
1998	11	29	56	96
1999	16	19	30	65
2000	16	18	23	57
2001	3	9	17	29
2002	5	8	4	17
2003	1	4	1	6
2004	.	.	5	5
Number of Properties	59	153	150	362
Percent of Properties	16.30%	42.27%	41.44%	100.00%

The analysis shows that owners did not often opt out of their Section 8 contracts before prepayment and that they prepaid about as often before opt-out and at the same time as the opt-out. It is likely that owners advanced prepayments to a point before they could opt out in order to take advantage of favorable interest rates to lower the property's debt service rate and increase net income in advance of opting out.

3.2 Multivariate Analysis of Opt-out Decision

This section presents our analysis of the owners' opt-out/opt-in decisions using multivariate logistic regression analysis, described in Section 2.3, Methodology. As we noted there, such a model explains the opt-in/opt-out outcome based on an array of project, owner, program, and location variables. It allows us to examine the impact of each variable on the owners' decisions, while holding all other variables constant. The key explanatory variable yielded by the multivariate analyses appears to be the rent-to-FMR ratio: the lower the rent-to-FMR ratio, the higher the likelihood of opting out.

To construct the regression model, we chose explanatory variables from the descriptive analysis section that were found to be different between the opt-in and opt-out properties. In Table 3.10 we present the variables used in the model, and their expected direction of impacts on the probability of opting out.

The results of the regression coefficient estimates, presented in Odds Ratio format, are shown in Table 3.11. It shows that most of the variables are statistically significant with the expected sign. The correlation bears out the relationship that was suggested by the cross-tabular analysis.

Table 3.10. Regression Model Variables

Variable	Variable Specification	Expected Direction of Impact
Development size in units	Less than 50 units (reference category) 50-99 units 100-199 units 200+ units	**Unknown.** On one hand, conversion to market rate may involve fixed costs; since larger projects have lower per-unit costs, this may increase their likelihood of opting out. On the other hand, large projects tend to be associated with other physical features that are less attractive to unassisted tenants.
Density	Percent of 3-bedroom-plus units	**Negative.** It may be harder to market projects with large units to unassisted tenants because these units may not be physically suitable for higher income singles and couples who could afford market rate units.
Family occupancy type	Family = 1 Elderly/disabled = 0	**Positive.** Elderly projects face competition from amenity-rich private market projects. Also, the income distribution among elderly and disabled households may not support many market rate units. In other words, family projects are more likely to opt out.
Building type	Detached or semi-detached = 1 Other = 0	**Positive.** Detached and semi-detached projects tend to be associated with other amenities and physical characteristics that are attractive to unassisted tenants.
Older Assisted HUD program types	Older assisted = 1 Newer assisted = 0	**Positive.** The older projects often have rents that are below market rate.
Ratio of rent-to-FMR	Rent-to-FMR ratio < 80% 80% < rent-to-FMR ratio < 100% 100% < rent-to-FMR ratio < 120% (reference category) 120% < rent-to-FMR ratio < 130% 130% < rent-to-FMR ratio < 140% 140% < rent-to-FMR ratio < 160% Rent-to-FMR ratio > 160%	**Negative** for projects with rents above local FMR. Projects with rents that are low relative to the FMR may be able to raise rents with little effect on vacancy rates. In other words, as rent-to-FMR ratio increases, we expect the property owner to be less motivated to opt out.
Ownership type	Nonprofit = 1 For-profit or limited dividend = 0	**Negative.** Nonprofits are less likely to opt out. By definition, for-profit owners are motivated to increase revenues.
Not federally financed mortgage	Not federally financed = 1 Other = 0	**Negative**. This value is a proxy for projects financed by state Housing Finance Agencies (HFAs). HFAs may impose prepayment and/or opt-out restrictions.
Neighborhood poverty rate	Percent of persons in the surrounding census tract with incomes below poverty threshold in year 2000	**Negative**. Research has shown that tracts with high poverty rates typically have features that make them undesirable places to live and hence are less able to command high rents.

Table 3.10. Regression Model Variables (continued)

Variable	Variable Specification	Expected Direction of Impact
100-percent assisted	Projects with 100-percent units receiving HUD assistance =1 Other = 0	**Positive**. A project with a high percentage of unassisted tenants risks high turnover upon conversion to private market status because these tenants will not have enhanced vouchers and may not be able or willing to afford the higher rents. A high percentage of assisted tenants implies more opportunity for the owner to raise rents to market levels.
Metropolitan location	Suburb (reference category) Central city Non-metropolitan	**Negative** for central city. We expect owners in central cities to be less likely to opt out because markets may be unable to support unassisted housing. **Positive** for suburb. Suburban areas tend to have higher income renters to absorb market rate housing.
Census division	New England Mid Atlantic East North Central West North Central South Atlantic (reference category) East South Central West South Central Mountain Pacific	**Positive** for high rent regions such as New England, Mid-Atlantic, and Pacific.

In Table 3.11, the variables with odds ratio estimates larger than 1.0 imply that a positive impact on the owners' opt-out decision, while variables with odds ratio estimates less than 1.0 imply that the presence of these factors decreases the likelihood of opting out. For example, the odds ratio for the family occupancy type variable is 2.3. This means that the odds of opting out for a family-occupied property are more than 2 times of those for an elderly/disabled property with comparable property and location characteristics.[14]

As noted earlier, the key explanatory variable in Table 3.11 is the rent-to-FMR ratio. It explains the largest share of variations in the probability of opting out, suggesting that a property's pre-opt-out rent relative to the local market rent is the most important determinant of the owner's opt-out decision, controlling for all other characteristics. When the Section 8 rent is significantly below the market level (proxy by FMR), owners realize that a conversion to market rate units can increase the rental revenues (and therefore profits) with little effect on vacancy rates. The regression model indicates that, compared to properties with rent level between 100 and 120 percent of local FMR, properties with below-market rents (that is, rent-to-FMR ratio less than 100 percent) are 2.9 to 12 times more likely to opt out in terms of odds.[15]

[14] In statistics, the odds of an event are defined as the probability of the event, divided by one minus the probability of the event.

[15] To capture any nonlinear relationship between the rent-to-FMR ratio and the likelihood of opting out, the rent-to-FMR ratio is specified in the model as a series of indicator (0/1) variables. The variable for rent-to-FMR ratio between 100 and 120 percent is not used in the regression model. Properties with such characteristics serve

As the rent-to-FMR ratio increases, we expect the owners to be less motivated to opt out. This is confirmed by the monotonical
decrease in the odds ratio estimates as the rent-to-FMR ratio increases in the model. For instance, everything else being equal, the odds of opting out for a property with a rent level between 120 percent and 130 percent of local FMR are approximately half (0.53) of the odds of opting out for properties with rent-to-FMR ratio between 100 and 120 percent. When the rent level is above 140 percent of FMR, the odds of opting out for these properties drop to about 20 percent of the odds of opting out for properties with rent-to-FMR ratio between 100 and 120 percent.

Table 3.11 also shows that ownership type is another key determinant. As expected, nonprofit owners are significantly less likely than other owners to opt out. On average, the odds of opting out for nonprofit owners are 16 percent of the odds for other owners.

as the reference category. This means that when interpreting the odds ratio estimates associated with the set of rent-to-FMR variables, they should be compared to the reference category.

Table 3.11. Coefficient Estimates of Opt-out Logistic Regression Model

Explanatory Variable	Odds Ratio		T-statistic
Development size			
Less than 50 units (reference category)			
50-99 units	0.51	***	-6.04
100-199 units	0.38	***	-6.82
200 or more units	0.44	***	-3.06
Density			
Percent 3-bedroom-plus units in development	0.28	***	-5.88
Occupancy type			
Family occupancy type	2.30	***	6.84
Elderly/disabled (reference category)			
Building type			
Detached or semi-detached building type	1.13		0.75
Ownership type			
Nonprofit sponsor type	0.16	***	-10.65
Program characteristics			
Older Assisted Section 8	2.37	***	8.13
100% of project units are receiving HUD assistance	13.92	***	11.38
Not federally financed (proxy for HFA deals)	0.82		-1.47
Neighborhood characteristic			
Census tract poverty rate	0.97	***	-7.43
Rent-to-FMR ratio			
Rent-to-FMR ratio < 80%	11.56	***	16.55
80% < rent-to-FMR ratio < 100%	2.91	***	8.03
100% < rent-to-FMR ratio < 120% (reference category)			
120% < rent-to-FMR ratio < 130%	0.53	***	-2.65
130% < rent-to-FMR ratio < 140%	0.48	**	-2.48
140% < rent-to-FMR ratio < 160%	0.19	***	-4.17
Rent-to-FMR ratio > 160%	0.22	***	-2.86
Metropolitan location			
Central city	1.49	***	3.44
Non-metropolitan	1.29	*	1.65
Suburb (reference category)			
Census Division			
New England	0.95		-0.19
Mid Atlantic	1.32		1.17
East North Central	1.42	**	2.23
West North Central	1.44	*	2.02
East South Central	0.88		-0.57
West South Central	1.78	***	3.19
Mountain	1.50	**	2.00
Pacific	1.45	**	2.33
South Atlantic (reference category)			

Table 3.11. Coefficient Estimates of Opt-out Logistic Regression Model (continued)

Other Regression Model Information	Value
Opt-out = 1; opt-in = 0	
Total number of properties	8,992
Number of opt-out properties	763
Log-likelihood	-1701.20
Pseudo R-square	0.35
Notes: *** indicates significance at the 0.01 level; ** indicates significance at the 0.05 level; * indicates significance at the 0.10 level.	

All else being equal, properties that are 100-percent assisted have a higher likelihood of opting out compared with properties where only a few units are assisted. This may be because properties that are 100-percent assisted can receive the maximum rent increase after the conversion to market rate. The regression model indicates that the odds of such properties opting out are more than 10 times the odds for other projects. It differs somewhat, however, from the cross-tabulation findings presented in the previous section, which show that on average, opt-out properties have a smaller percentage of assisted units compared to the other categories of properties. This difference may be due to the fact that the regression includes only opt-in and opt-out Section 8 properties, while the descriptive tables include a much larger group of properties. In addition, other confounding influences, such as the rent-to-FMR ratio and ownership type, may influence the cross-tabulation results.

Other results presented in Table 3.11 yield the following findings:

- Family-occupied developments are much more likely (2.3 times in terms of odds) to opt out than elderly/disabled properties.

- Development size matters. In general, owners of larger developments are less likely to opt out of the Section 8 program than owners of comparable developments with fewer than 50 units. The magnitude of the impact, however, does not increase monotonically with property size. (The size impact on the odds of opting out appears to be larger for the range of 100–199 units than for the 50–99 or 200+ unit ranges.)

- Density of the development, as measured by the proportion of 3+ bedroom units, also matters a great deal. Holding other variables constant, properties with a high concentration of large units are less likely to opt out. For every percentage point increase in the proportion of large units, the odds of opting out decreases threefold.

- Older Assisted properties tend to be more likely to opt out, probably because their budget-based rents have been held below the market level for many years. Their odds of opting out are 2.4 times those of the Newer Assisted projects.

- Properties located in high-poverty rate census tracts are less likely to opt out, because the housing markets in those areas cannot support market-rate rents.

- One unexpected finding is that properties located in central cities and non-metropolitan areas are more likely to opt out than those in suburban areas. Being located in central cities increases the odds of opting-out by 49 percent, all else being equal. This finding may reflect a shortage of rental housing in those areas, where owners have an incentive to convert to market rate to capture the additional rental revenues. (Marketability and profitability of the units have already been controlled for by other variables such as the rent-to-FMR ratio and census-tract poverty rates in the regression model.) This finding differs, however, from the cross-tabulation results.

- Compared with properties in the South Atlantic Division, properties located in the Pacific, Mountain, and West South Central Divisions have higher odds of opting out. This pattern may be a result of the hot rental markets in those latter three regions, which have been fueled by a surge in population and a short supply of rental housing.

- Regression estimates for the building type and non-FHA mortgage insurance variables have the expected impact (direction) but they are not statistically significant. This indicates that, after controlling for other influences, these factors appear to have no impact on the owners' opt-out decision. It implies that State agency rules appear to be unimportant relative to other determinants in the model.

We also experimented with other model specifications that included tenant characteristics (percentage of minority households, percentage of single-parent households, and average household size) and REAC variables (physical inspection score and per-unit reserves). Regression estimates for those variable are either not statistically significant or with the unexpected direction of impact/sign. This probably reflects that they are highly correlated with other variables in the model and the effects of these variables have already been captured by other variables. Furthermore, because the data for these variables are missing on a large fraction of the study properties, including them would result in a substantial reduction of the sample size for the regression model. Therefore, we decided not to include these additional explanatory variables in the model.

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4. Case Study Results

This chapter describes the findings from site visits we made in August 2005 to three metropolitan statistical areas (MSAs): Sacramento, Dallas, and Cincinnati. In each of the three MSAs, we made site visits to two pairs of seemingly similar properties. One property owner in each pair had opted out of the Section 8 program, while the second owner in each pair had chosen to keep the property in the Section 8 stock. In general, we would expect owners to be more likely to opt out of their Section 8 contracts in markets where they think they could operate successfully as unassisted properties. The quantitative analysis conducted for a large number of properties found that a key driver in the decision to opt out of Section 8 is low property rent relative to FMR, indicating that property rents are below prevailing market levels. The primary goal of the case studies was to learn about the non-market factors that lead some owners to leave the Section 8 program and other owners to remain in the program.

4.1 Summary Observations

The MSAs selected for the site visits were those with a large number of properties that have opted out of the Section 8 stock.[16] Sacramento has low vacancy rates and has experienced rent increases city-wide. Thus, we are not surprised to see property owners leaving the Section 8 program with the expectation of receiving higher rents in the unsubsidized market. Similarly, Dallas was experiencing low vacancy rates and rising rents in the late 1990s when the owners of the selected properties decided to opt out (although recently the rental market in Dallas has been depressed). The question in those two cities, then, is why owners of other similar properties chose not to opt out of their Section 8 contracts. In one case in Sacramento, the owners chose to keep the Section 8 contract for a portion of a large project to avoid public opinion problems associated with removing affordable housing from the stock, and in the second case the owner has simply not gotten around to opting out yet, but plans to do so.

In Dallas, one of the properties that remained in the assisted stock is owned by a mission-driven nonprofit organization dedicated to serving low-income elderly. The sample for the case studies was intended to exclude properties owned by nonprofits. However, due to data inaccuracies this property was included. In the other Dallas property, the contract was eligible for opting out only after the market started to decline and it no longer made economic sense for the owner to take the property out of the assisted housing stock.

The situation is less straightforward in Cincinnati, which had a depressed rental market for the entire period. In Cincinnati, the owners we spoke with said that local owners often opted out because of problems with the local HUD office and with the early implementation of the Mark-to-Market program. Many properties in Cincinnati were among the first properties eligible to undergo Mark-to-Market. The sampled owners reported that in its early days, the Mark-to-Market program offered fewer benefits to participating owners. The owners

[16] For more details on the site selection procedure, see the Data Collection Appendix to this document.

claimed that the rents being offered would not cover ongoing costs. Thus, owners chose to opt out and take their chances with unassisted rents. More recently, opt-outs seem to be occurring for similar reasons. The owners we spoke with stated that HUD was not offering sufficient rents to cover operating expenses upon contract renewals. The relationship between HUD and the owners appeared to be strained.

In Dallas and Cincinnati, property owners cited difficult relations with the HUD office as a reason for opting out of the Section 8 program.

4.2 Site Summaries

Sacramento

The Local Market and Submarkets

Sacramento, the capital of California, is located in north central California, approximately 75 miles from the San Francisco/Oakland metropolitan area. Until recently, the city of Sacramento was the only major urban center in the Sacramento Valley. The Valley has been—and remains—one of the nation's most productive agricultural regions. The University of California at Davis, the "UC" system's agricultural research center, is located 20 miles west of downtown Sacramento.

Although agriculture remains the major industry in the valley, in the last several decades the Sacramento area has undergone the rapid spread of suburban communities typical of most of California. These communities have demographic characteristics significantly different from those of the urban center. For example, Placer County, which is just east of Sacramento, experienced a 43.8-percent increase in population from 1990 through 2000. The comparable figure for Sacramento County was 14.7 percent; for the city of Sacramento it was 3.0 percent.

There were also differences in the demographic characteristics of the populations of the different portions of the Sacramento area. In 2000 the city of Sacramento was about half white, with the remainder divided fairly equally between African American, Asian, and Hispanic. In contrast, Placer county was nearly 90 percent white. Similarly, in 2000 the homeownership rate in Placer County was 73 percent, with a median value of owner-occupied units of $213,900 (the state median was $211,500). In the city of Sacramento, the homeownership rate was 50 percent with a median value of $128,000. In 1999 the poverty rate in Placer County was 5.8 percent, compared to 20 percent in the city of Sacramento.

Data gathered on the site visit indicates that the "suburbanization" trend began to fade in the late 1990s. Because many individuals were "priced out" of the housing market in the newly developed suburbs, developers began to look in the city of Sacramento for single and multi-unit housing to "rehabilitate" and sell as owner-occupied dwellings. Low interest rates have facilitated this trend. As a result, there is evidence of "gentrification" in many parts of central Sacramento.

The recent gentrification of properties in the city has removed a significant number of properties from the assisted stock of affordable housing. At the same time, approximately one-fifth of the city's population has incomes at or below the poverty level. In Sacramento, as in the rest of the state, construction of rental units has fallen far below the demand. Local agencies and advocacy groups estimate that state-wide the annual short-fall in the availability of affordable rental units over the last decade has been 200,000 units per year. Both owners and agency representatives in Sacramento indicated that that this state-wide pattern accurately defined the trend in the Sacramento area during the last several years.

The American River divides Sacramento into two general areas. The area south of the American River is the "old city." It contains the State Capitol and the central commercial district. Much of the housing in this part of the city is single-family residences, many in the "California ranch style," popular in the early part of twentieth century. The long residential streets are lined by eucalyptus trees. In the 1950s and 1960s, some modest multi-unit rental properties were built in these residential neighborhoods. These are frequently two- and three-story stucco-frame structures, typical of much apartment construction in California. There are few, if any, high-rise apartment buildings in central Sacramento.

Some of the older residential neighborhoods, particularly those close to the American River, have many low-income residents (in this area mainly Hispanic), with many of the residences in obvious need of rehabilitation. Residential patterns in the rest of this part of the city are less discrete. Low-income single and multifamily units are interspersed with older single residences that have been substantially rehabilitated. In addition, there are several residential neighborhoods relatively close to the center of the city that are obviously upper income communities.

The residential patterns north of the American River are more typical of immediate post-World War II suburban development. Multi-unit and single-family residences are interspersed, without much consistency in design. The main transportation routes in this area are multi-lane boulevards characterized by a mix of retail, business, and even some manufacturing structures.

It is more difficult to generalize about the level of maintenance and apparent income levels for each neighborhood in this area. It appears that the income level of residents and the quality of housing stock changes sharply almost on a block-by-block basis. However, several of the areas adjacent to the main boulevards are clearly low-income, and the city and several nonprofit organizations have initiated redevelopment programs for several portions of this city sector.

The Properties and their Tenants

The Sacramento case studies focused on two sets of properties, both located in the north sector of the city. One property was at the western edge of the city, and another group of properties was in the north and eastern part of the city.

North Western Properties
The case study property in the north sector is an apartment complex near the western edge of the city where the American and Sacramento rivers meet. It borders a wide boulevard, one of the city thoroughfares. The immediate area around the complex consists of a mix of relatively new multi-unit properties, single-family residences, and several "strip" retail malls along the main thoroughfare. All of the surrounding neighborhoods are moderately to well-maintained. As in many parts of California, it appears that most residents have access to vehicles and there is very little foot traffic.

The property is a community complex of slightly more than 800 units located in more than 20 two- and three-story multi-unit structures. The development's amenities include four swimming pools, tennis courts, at least three large community centers, and large gardens surrounding the apartments. At the time of the visit all structures and community areas appeared to be well maintained. The property was constructed in the early 1980s and was purchased by its current owner in 1991. The ownership entity is a major owner/developer in California. Located in Menlo Park, it owns and manages more than 20,000 units from the Sacramento region down to San Jose. The firm currently has more than 1,000 units under development.

As originally developed, the property was a "mixed" complex, with 160 out of the 800 units assisted under multiple Section 8 contracts, and the remainder of the units rented at market rate. The owner began opting out of the Section 8 program in the 1990s, and now only one 26-unit structure remains assisted.

The owner's representatives indicated that there were two key factors in their decision to leave the program:

- *The burden placed on their administrative staff.* In their view, operating Section 8 properties requires personnel who can devote their attention to program requirements, and this is too much to expect of administrative staff members who must manage the market-rate units as well. They considered it a financial burden to hire staff solely devoted to the Section 8 units.

- *The resale value of the property.* Since the property was always essentially a market rate complex, the presence of the Section 8 units made the property less attractive to prospective private-sector purchasers.

Comments from management and several other informants indicated that an additional factor may have been concern about income and lifestyle differences between the Section 8 and market-rate residents.

The owner has kept one of the structures in the Section 8 program. Several individuals in the Sacramento area suggested this may have been done for public relations reasons since the "opt-outs" at the property garnered considerable local newspaper and TV coverage.

North Eastern Properties

The properties visited here included four properties, three of which opted out, and one that remained in the Section 8 program.

The four properties are similar three-story stucco multi-unit structures. The properties are not part of a single complex, but are located in different parts of central Sacramento immediately north and east of the central commercial district and the State Capitol complex. All of the structures appear to have replaced traditional single-family ranch-style residences. None has major amenities such as a swimming pool.

The neighborhoods immediately surrounding the properties vary considerably. Closer to the American River (north of downtown), the neighborhoods appear to be lower income. Most of the neighboring structures are poorly maintained, and there are few retail outlets in the commercial strips of the neighborhoods.

The properties located directly east of downtown are in neighborhoods undergoing gentrification. Although some homes in these areas still appear poorly maintained, many of the residences show evidence of considerable recent investment. “Boutique-style” retail outlets have opened on the main traffic arteries. One of the properties is located only a few blocks from a very expensive residential neighborhood.

The property that remains in the Section 8 portfolio is located just south of the American River. The single-family residences in the immediate area are not well maintained, and there are few retail outlets on the blocks close to the property (mainly a few bodegas). In terms of general appearance and apparent level of maintenance, however, this property does not differ significantly from the other three properties.

Ownership of these properties resides in the type of limited partnership entities common to the Section 8 portfolio. However, a single management company has continuously managed all four properties. This is one of the largest property management firms in the Sacramento region, and only a small percentage of its portfolio is in the Section 8 program. Senior partners at the firm are part or complete owners of some properties as well as property managers.

The key factors associated with the opt-out decision for the three properties that opted out were:

- The tight rental market caused by the gentrification of central Sacramento.

- Lack of direct involvement on the part of the ownership entities. Original partners retired or died. New owners saw continued participation in the Section 8 program as an unnecessary complication.

The opt-in decision among one of the four properties appears to have occurred almost inadvertently. The partners in the ownership entity have not shown much interest in the property, either to remove it from the program or to sell it. Recently, however, representatives of the property management group responsible for the property have begun proactively seeking a nonprofit purchaser for this property, because they see a need to maintain affordable housing in central Sacramento.

Lessons Learned

The first and most obvious conclusion to be drawn from the Sacramento case is that a tight rental market can influence owners to take properties out of the Section 8 program. In the period from 1998 through 2004, the Sacramento real estate market was characterized by rising prices for single-family homes, low interest rates, gentrification in areas of the central city, and a low rate of construction of new rental units. This was an environment in which owners saw an opportunity to take properties out of the Section 8 program with very low risk in terms of future occupancy rates and rent levels.

In the case of the properties visited, however, these factors served as a background to the decisions on the part of owners and owner/managers. In both cases, the owners or managers had portfolios consisting primarily of market-rate units and wanted to convert the remaining properties to market rate to make them consistent with the rest of their portfolios. Neither group had major complaints about the operation of the Section 8 program in Sacramento (the Sacramento HUD office received positive comments from all categories of respondents). Yet because Section 8 was only a small part of their operations, they stated that the administrative burden placed on their staff by a program run on totally different principles was not justified. Because of the tight rental market, these owners with significant market rate portfolios were able to successfully opt out of the Section 8 program.

At the time of the site visit, no subsidized residents remained in the “opted-out” portions of the northwest sector property. Reportedly fewer than half of the formerly subsidized residents remained in the properties in the northeast sector structures 3 to 4 years after they left the program. Local advocacy groups have had some difficulty in tracking where these low-income individuals are going once they have left these properties. It is clear that the removal of properties from the Section 8 program has had a major impact on where low-income residents can find affordable housing in the metropolitan Sacramento area.

Local restrictions were not mentioned as a major factor in keeping properties in the program. This is perhaps surprising, given the level of tenant advocacy in California. However, owner representatives did claim that requirements for affordable units in new complexes were having a negative impact on the rate of construction of new rental units.

Dallas

The Local Market and Submarkets

Interstate 30 divides the city of Dallas into two distinct economic regions: North Dallas and South Dallas. There is a great deal of economic disparity between the two halves. Poverty and crime rates in South Dallas are twice those in North Dallas. In North Dallas, the median home price is $150,000 compared with just $58,000 in the Southern sector. The majority of affordable housing is located in South Dallas. During the “dotcom” boom, several major technology companies took up residence in North Dallas. As a result, a significant number of new houses were built in the area.

City officials now believe that the area north of Interstate 30 is overbuilt, and officials are beginning to focus on developing additional housing units in South Dallas. The Dallas City Council recently contracted with McKinsey and Company to examine the suitability of South Dallas for such development. Approximately 17 percent of Dallas’s land mass is developable, a rare circumstance among large cities. Most of the developable land lies in South Dallas. Following the national trend of promoting homeownership, combined with low interest rates, the Mayor and City Council have supported the building of single-family homes in South Dallas. For the first time ever, more single-family home permits were issued in 2004 in South Dallas than in North Dallas.

New multifamily developments are being built as replacements for the current older housing projects. A large number of properties have been funded by the Low Income Housing Tax Credit in South Dallas over the past few years. This may change in the near future, given that a member of the Dallas City Council is under investigation by the FBI for profiting from a development venture to which the Council awarded tax credits. A HUD representative reports that this investigation may lead the city to be more conservative in its issuance of tax credits.

Dallas is currently experiencing an increase in housing vacancy rates as a result of the loss of jobs in the area during the past several years. Throughout the city, landlords are offering incentives such as low security deposits and a free month’s rent to entice renters. The increase in development of homeownership opportunities in the city further depresses the rental market. Rental vacancy rates are currently above 11 percent citywide, up from a low of 7 percent in 1999. Recent private market studies suggest that a stronger economy during the next 2 years in Dallas should produce more jobs and a decrease in vacancy rates. This should allow property owners to raise rents and reduce concessions.

The need for affordable housing in Dallas remains significant. The Dallas Housing Authority (DHA) administers 16,000 Section 8 Housing Choice Vouchers, but there are approximately 34,000 additional families on the voucher waiting list. The wait for a voucher is 18 to 24 months, and the waiting list is currently closed. Dallas Housing Authority’s waiting list for public housing is open only for elderly applicants and families needing four- or five-bedroom units. Officials from the HUD Regional Office in Dallas estimate that the City has approximately 30,000 fewer affordable housing units than are needed.

The Study Properties

The site visit focused on two neighborhoods in South Dallas: Cockrell Hill and Pleasant Grove/Balch Springs. Both areas historically are economically depressed; there is little business or industry. The majority of businesses that do exist cater to the low-income population, providing services such as fast food, rental furniture, and payday loans. Most of the jobs and stores are outside of the neighborhoods. However, because of the focus by the city on developing South Dallas, there has been a recent flurry of residential construction activity in both neighborhoods.

Cockrell Hill

In Cockrell Hill, several tax credit properties have opened in the past 2 to 3 years. In addition, an entire community of new single-family homes has arisen on the main thoroughfare through the neighborhood. The single-family homes across the street from the opt-out property were offering $500 move-in specials for their units, leading to competition for the opt-out property. The Cockrell Hill neighborhood is home to Mountainview College, one of the Dallas County community colleges.

The opt-out property is 30 years old and owned by a limited partnership. The partnership owns 9 other multifamily rental developments and manages all 10 through its own management division. Seven of the developments are in the Dallas area, one is in Abilene, and one is in San Antonio. All of the developments were formerly Section 8 project-based; in all but one, the owners have opted out of the program. The final Section 8 property has only been under the ownership of the limited partnership for 7 months. Otherwise, this property likely would have been converted to unsubsidized rental units.

The owners opted out of the program in 1998, when the property first became eligible. The decision to opt out of Section 8 was an easy one. At the time, the Dallas rental market had been enjoying increasing rents for several years, and the owners believed the trend would continue. In addition to the prospective profitability of receiving market rents for the development, they were happy not to have to abide by what they considered to be HUD’s increasingly rigorous regulations. At the program’s inception, property owners were allowed to put in place their own procedures, with the exception of eligibility requirements. One of the owners stated that it had become progressively more difficult to hire and train property managers with adequate knowledge of the program’s vast requirements.

The opt-out property was one of the first Section 8 project-based properties in the state. One of the owners reported that when the program began, the owners’ organization and HUD were partners in providing housing opportunities to low-income tenants and received great support from the local office in administering the program. She reported, however, that the relationship became adversarial over time. She said that HUD believed the owners had become too profit-driven or were trying to cheat the system somehow.

Following the opt-out, the rents at the property initially increased and then leveled off. Because management is currently offering a free month’s rent as an incentive, the overall rent roll effectively has decreased. Prior to the opt-out, the vacancy rate was about 5 percent. The property is currently experiencing a 10-percent vacancy rate, similar to the rest of Dallas.

Six months after the opt-out occurred, the owners had to advertise for the property, something they never needed to do previously. Although vacancies increased at this property following the opt-out, the owner stated that she remains interested in opting out of other Section 8 project-based developments because of the increased regulations and the perceived unfavorable relationship with HUD.

The owner stated that the limited partnership had lost some residents to new properties that have been developed in the neighborhood, both tax credit rental apartments and owner-occupied single-family homes. The residents were lured away with greater amenities, such as remodeled kitchens and baths and washers and dryers in the units. Several of the newer properties offered lower initial move-in specials and later increased the rent. According to the owner, some families who took advantage of $500 downpayment homeownership opportunities have since determined they could not afford a house, or it was foreclosed, so they moved back to the property. The majority of residents stayed at the property following the opt-out. Many of them could not afford the newer tax credit properties or homeownership opportunities.

Since the opt-out, the owners have invested some money into rehabilitating the development. They made most of the improvements to the exterior of the buildings. They painted and re-sided the entire development, and installed a pool, playground, and carports. The owner's representative stated she would have liked to install new kitchens and baths but lacked enough funds to do so.

The opt-in property in Cockrell Hill is an all-elderly development originally built with Section 202 funds. The owner of the property is a nonprofit organization whose mission is to assist those in need.[17] The property is managed by a company that manages 15 other subsidized properties in Texas and New Mexico. Of the 15 properties, one is a Section 236 property, one is a combination of Section 8 and Section 236, and the remaining properties are Section 8 project-based developments. Only two of the properties, located in Laredo and Albuquerque, have opted out of the program, with location being the major factor (and one of the two continues to accept Section 8 vouchers). The owners expressed no interest in getting out of the Section 8 program for their remaining properties. The manager did state, however, that they discuss opting out of the program every year for three of their properties, because they do not receive requested rent increases from HUD and believe they can charge more rent in the private market.

The property for elderly tenants in Cockrell Hill was built in 1981. After years of poor management by the nonprofit organization, the management company was hired to oversee the operations. The management company invested some of its own funds to improve the physical appearance of the premises. Today the property is considered well-managed. The building and grounds are in very good condition, and the management contracts with several agencies to provide a wide array of social, meal, and health services to its residents.

[17] As noted, the goal of the site visits was to see only properties owned by for-profit owners.

For this specific property, there was never any discussion by the owners to remove it from the Section 8 program. It is the mission of the nonprofit owners to help the low-income community, and they state that this mission will not change. Also, there is a significant need in the area for elderly developments. The property has only a 2-percent vacancy rate. The managers were successful in getting small rent increases at the property based on their budget. However, they have not been as successful at some of their other properties. The property management company is currently appealing two denials for rent increases at two other properties. Although the owners and managers have no intention to remove the property from the program, they expressed frustration with the contract renewal process, saying that it took about 18 months to complete and that the relationship with the staff at HUD was adversarial.

The owner stated that there have been no major changes to the property, tenants, or administration since deciding to remain in the Section 8 program. The resident population is static. Residents usually move out only upon admission to nursing homes or passing away. There have been no physical changes to the building or units, and aside from small rent increases, they run the program exactly as they did prior to contract renewal.

Pleasant Grove

The Pleasant Grove neighborhood is similar to Cockrell Hill in that it is a mostly residential, low-income community. There is some commercial activity, including distribution centers, car dealerships, and the Southeast Dallas Health Center. The neighborhood includes a grocery store, although it had recently been converted from a national grocery store chain to a regional discount store. There are several shopping plazas that appeared to be vacant. There did appear to be some construction activity occurring in neighborhoods adjacent to Pleasant Grove, including new single-family home development and a new Wal-Mart Super Center.

The owners of the opt-out property located in Pleasant Grove prepaid their mortgage and opted out of the Section 8 program in 2000. The ownership entity is a limited partnership made up of a construction company and a development company.[18] Most of the owners' experience is in the construction of military housing. They have some tax credit developments, but they have limited experience with the Section 8 program. One of the owners stated that the main reason for opting out was the belief that they could obtain higher rents in the private market.

Since the opt-out, the Texas Department of Housing and Community Affairs has given the owners a loan based on a tax-exempt multifamily bond issue. The owners have spent approximately $1 million on renovating the 200-unit property. The exteriors of all the buildings have been repainted and the interiors renovated. The buildings and the grounds appeared very well maintained, although it was obvious that this development was one of the older ones in the neighborhood.

[18] The property owner of the opt-out property in Pleasant Grove was unavailable during the site visit. We still conducted a physical inspection of the property and gathered additional information by telephone.

The Pleasant Grove site visit also included a property that remained in the Section 8 program. In 2001, at a time when the local real estate market was soft, the 20-year Section 8 project-based contract expired. The owners of the property entered the Mark-to-Market program and subsequently renewed their Section 8 contract at 1-year intervals. They decided to remain in the program primarily because they believed that the low-income population would not be able to pay market rents and that the property would need the Section 8 rental subsidy to continue to operate. The owner is a limited partnership that owns several other Section 8 project-based properties in El Paso, Lubbock, and Childress. All of their properties remained in the program when their contracts expired, primarily because the rents in the areas in which the properties were located were low.

The development was constructed in 1972 and still has the original kitchens and baths. There have been no major renovations to the property since the contract renewal. The management is trying, however, to install new carpets, cabinetry, light fixtures, and appliances upon unit turnover.

The residents are mainly low-income families. The manager estimates that only 20 percent of the tenants are working, while the remainder receives income from Social Security and Temporary Aid for Needy Families (TANF). The manager describes the majority of families as in “survival mode.” The tenants pay for their own utilities and she often comes across families who are faced with having the utilities turned off for nonpayment. The residents are largely the same since the contract was renewed. There is routinely a very low vacancy rate, and management maintains a waiting list with estimated waiting periods of 6 months to a year. In the previous year, the waiting period had increased to more than a year, either because the number of opt-out properties in recent years had increased or because rents were relatively higher in the competing housing developments.

As in Cockrell Hill, there has been construction of new tax credit multifamily developments in the neighborhood. In fact, there is a new development adjacent to the Section 8 property. The development has just opened and is accepting Section 8 vouchers. Although the neighboring development would provide greater amenities and newer kitchen and baths, the property owner did not think she would lose many residents to the newer property. She stated that the stricter eligibility criteria of the new development would prevent many of her residents from being accepted.

The property manager stated that her relationship with HUD has been improving since she took the job in 2003. At the start of her tenure, she found it difficult to learn and abide by all of the Section 8 program regulations, and it was challenging to get the needed assistance from HUD. She has since developed a positive relationship with her Section 8 asset manager, and says that she now has adequate support.

The company that owns the opt-in property has been successful in obtaining incremental rent adjustments for their properties. The owner is a large company and has staff members who assist property managers in understanding the regulations and in dealings with the federal government. The company also employs a grant manager who helps the properties apply for any eligible sources of funding for which they may be eligible.

Lessons Learned

In Dallas, property owners apparently opted out of the Section 8 program when they were able to do so. One property kept in the program is owned by a nonprofit organization for which providing low-income housing is central to its mission. The owners of the second property that remained in the program renewed the contract, because the property housed mainly very low-income households, and the owners said the neighborhood market would not bear much higher rents. With new tax credit properties and single-family homes in the area, the second property's owner did not see a potential market for its units in the private rental market. Additionally, the owner was successful in securing incremental contract rent increases from HUD. These increases allowed the property owner to increase its revenues to some extent while still remaining in the Section 8 program.

All of the property owners, except for the elderly opt-in development, owned other Section 8 properties. Where the market would bear it, the owners opted out of the program for their other properties. In many of these cases, the owner had requested rent increases that had been denied.

Another common reason stated for the decision to opt out was that it was becoming increasing difficult to work with HUD. Owners thought that the program's regulations were overly burdensome and restrictive. They welcomed an opportunity to have more input into how their developments were administered. Owners also stated that there was little support from HUD and that there was an air of distrust of their motives.

In both opt-out properties in Dallas, the majority of assisted tenants remained in the property following the opt-out.

The owners of properties that remained in the program were successful in obtaining rent increases and seemed to have better working relationships with representatives at HUD.

Cincinnati

The Local Market and Submarkets

The Cincinnati metropolitan area encompasses 13 counties in southwest Ohio, northern Kentucky, and southeast Indiana. The city of Cincinnati itself had a population of 330,000 people in 2000, reflecting about a 9-percent decline since the 1990 census. The metropolitan area has had a rental vacancy rate of more than 10 percent for the past several years. The city's population has not been growing, and low interest rates and low housing prices mean that more low-income households can move into homeownership (although the homeownership rate of 39 percent in 2000 was still well below the statewide rate of 69 percent).[19] There has also been a significant amount of new construction in the city, including high-end units that are tapping into the "back to the city movement," as well as lower rent HOPE VI an1d tax credit units. (For example, approximately 1,200 assisted and 600 market-rate units were recently completed through the HOPE VI program.) These trends have lead to increasingly high rental vacancy rates, particularly at the low end of the market. Renters are reportedly able to move up to higher quality rental units, leaving particularly high vacancy rates in the lower rent properties.

A large fraction of the affordable housing in the city is located in three neighborhoods: Over the Rhine, Avondale, and Walnut Hill. Two of these neighborhoods, Over the Rhine and Avondale, are very distressed areas with significant drug and crime activity.

Over the Rhine is a neighborhood that includes many low-rise buildings built primarily in the years 1850–1880, as well as large public housing projects that were built more recently. The properties are somewhat rundown, and the neighborhood has a very high vacancy rate.

The Avondale neighborhood was built primarily in the 1900–1930 period and includes many brick multifamily properties. The properties appear to be in reasonable condition, although the public and outside spaces are not very well maintained. Nearly every residential building on the main street of the Avondale neighborhood is either owned by the housing authority, is a Section 8 property, or is occupied by a voucher holder. There are many churches in the neighborhood, as well as some commercial activity, including some small stores.

The Walnut Hill neighborhood also has drug and crime activity, but is located near a city park and is more mixed in terms of quality and tenancy. There are some large older homes. Over time, many were converted to multifamily properties, but recently some have been re-converted to single family. There are also some smaller multifamily properties, including some new construction (including both market-rate and tax credit properties). There are some streets with offices, nicer houses, and condominiums that are occupied by market-rate tenants

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[19] For population, homeownerships rates and other data about the city, see Web site http://quickfacts.census.gov/qfd/states/39/3915000.html.
For median house prices, see Web site
http://www.realtor.org/Research.nsf/files/REL05Q2T.pdf/$FILE/REL05Q2T.pdf.
Median house prices in Cincinnati were $134,000, $139,000, and $143,000 in 2002, 2003, and 2004 respectively, compared with national medians of $158,000, $170,000, and $180,000.

and other streets with deteriorated properties that are reportedly primarily assisted or inhabited by voucher holders. The neighborhood also has some grocery stores and restaurants.

There are reportedly five large owners of affordable housing in Cincinnati. The Cincinnati Metropolitan Housing Authority is the largest owner in the city with about 8,000 units, including two newly redeveloped HOPE VI projects. Another large owner owns about 4,000 units of project-based Section 8 housing. A third company has owned as many as 1,000 Section 8 units at one time. This third company has opted out of its Section 8 contracts for many units, and as of mid-2005 the company still owned about 600 Section 8 units. Many of the company's current developments are supported through the Low Income Housing Tax Credit program. Another large owner owned several thousand Section 8 units until recently. Because of difficulties we discuss below, he sold off many properties, and his company is now bankrupt. The fifth company is a family-owned business that reportedly can do well in the low-margin market for low-income rentals, because family members perform most of the work at the properties. This company purchased many of the bankrupt owner's properties, as well as a large number of other units throughout the city, and appears to be a large and growing player in the affordable housing market in Cincinnati. Its portfolio includes Section 8 properties as well as other affordable rental units.

The Properties and their Tenants

The site visit focused on two pairs of properties located in two of the three low-income areas in the city. One pair was located in Avondale, and one pair in Walnut Hill.

Avondale Properties

The two properties in Avondale were on the main street a few blocks away from each other. Both were owned by the same company. The property that opted out was an 18-unit family property, and the property that remained in the assisted stock was a 24-unit family property. The properties appeared to be in similar physical condition, both in solid, brick buildings built in the early part of the 20th century. Both were reasonably well maintained, although the owner says that the tenants do not maintain the interiors of the units well.

The owner reported that most of the tenants in both buildings are low-income, although in the opt-out building, more are likely to be working. Most of the tenants who lived in the property at the time of the opt-out are no longer there, although the new tenants have similar incomes and some use vouchers.

The owner of these two properties is part of a family-owned business. He said he decides on opting out on a case-by-case basis. He determines whether his company can withstand the cash flow shock that would occur as a given opt-out property moves from Section 8 to market rate. Because of the high vacancy rate in the city, the owner expects that upon opting out most residents will use their vouchers to move to other properties and it could take 3–6 months to re-fill the property. Whenever the owner thinks this is financially possible, however, he does opt out, because he said he prefers not to have to deal with HUD in order to set rents.

Walnut Hill Properties

The second two properties were located in the Walnut Hill neighborhood. The opt-out property had 28 units, and was converted to condominiums following the opt-out. It was on one of the better streets in the neighborhood. The former owner said he sold the property purely for financial reasons. He expected a better financial return for selling the property than from maintaining it as affordable rental housing. This owner has opted out of about half of his portfolio to date.

The opt-in property in the Walnut Hill neighborhood was a scattered site 26-unit property: one building was in the Walnut Hill neighborhood, and a second building was in the Over the Rhine neighborhood. The owner of the opt-in property reports that both buildings are covered by the same mortgage. For the property located in the Walnut Hill neighborhood, he may well have been able to opt out, but given the location of the second building, there was no choice but to stay in the program. (There are no market-rate options for the property in Over the Rhine.) In fact, this owner, whose company owns about 4,000 units, has not opted out of any of his Section 8 mortgages. Although he reported that he is increasingly frustrated with his dealings with HUD primarily in terms of rent-setting policy, he said that he stays in the program because he is too old to learn a new way of doing business.

Lessons Learned

In Cincinnati, whether owners have in fact opted out or not, the dominant theme is that because of difficult relations with HUD, owners who can legally opt out often may do so, even if does not appear to make economic sense. As one long-time owner said, when he started in the program, HUD and owners were partners in providing low-income households with decent affordable housing. He now feels that HUD assumes owners are trying to cheat, while at the same time, owners are not receiving adequate funds to provide adequate housing.

We met with three of the four major private owners of Section 8 properties in the city as well as with field office and PHA staff. Respondents described the experience of the fourth owner as well as their own. This owner at one time owned a lot of properties in the city, particularly in the Over the Rhine neighborhood. He was the general partner in a partnership that developed many units 20 years ago. When the Section 8 contracts were up for renewal, the contract rents were well above market level. This was early in the Mark-to-Market program, and the limited partners did not want to enter the Mark-to-Market program. At that time the owners said that the program would not provide sufficient rents to cover ongoing costs. In addition, they reportedly did not want to invest the required 20-percent equity for repairs. The owner stated that he had no choice but to opt out, because the rents HUD offered him would be too low. Because of the soft rental market in the city, however, many tenants used the vouchers to leave the properties. Ultimately, the company went bankrupt and another owner has purchased several of the properties.

Two of the large owners we interviewed had elected to opt out of some of their Section 8 properties, but remained in the program for others. The decision depended on the location of the property. In one case, the owner noted that it also depended on whether at the time he had the cash on hand to accept the 3 to 6 months it takes for the property to re-stabilize following the opt-out.

The final owner had not opted out of any of his properties. He is an older man, and said he was hesitant to enter a new segment of the market in spite of his frustration dealing with HUD. He has dealt with the lower rents offered by HUD by refinancing some properties, and by entering Mark-to-Market with others. He was looking for a nonprofit buyer for one large property, because he believed that was the only way to obtain the financing needed to rehabilitate the property.

5. Results from the Affordability Analysis

Policymakers will be more concerned about properties leaving the assisted stock if rents at these properties become unaffordable to low-income households, than they would be if these properties can continue to provide affordable housing to low-income households after opting out. To address this issue, we looked at the post-opt-out affordability in a sample of units that left the assisted stock. We found that at the end of 2004, nearly 60 percent of the sample of units had rents that were below the FMR after leaving the assisted stock, indicating that they would be affordable to voucher holders. An additional 31 percent had rents that were between 100 and 125 percent of FMR, indicating that they might still be affordable to voucher holders, depending on the payment standards chosen by voucher program administrators and families' ability to pay more than 30 percent of their income for housing. However, only 6 percent of units would be affordable to unassisted households earning 30 percent of the local area median income. Sixty-four percent would be affordable to unassisted households earning 50 percent of the local area median income.[20]

HUD does not track rents in properties after they leave the stock, thus we could not obtain rental data for all such properties. As an alternative, we used HUD's PIC/MTCS system to obtain rents for a sample of units in these properties. When properties leave the stock, assisted tenants in the properties often receive Section 8 vouchers that can be used to remain at the property (or to move to a different property). Some tenants receive enhanced vouchers, which can be used to pay above-payment-standard rents at the opt-out property if HUD determines that the rent is reasonable. In addition, once the property leaves the stock, additional voucher holders can use them to rent units at the property.

HUD does not have a file that contains addresses of all buildings in assisted properties. It is thus not possible to identify all voucher recipients who live in opt-out properties. With assistance from HUD, we were able to link a group of voucher recipients (using an extract of MTCS/PIC from late 2004) to the opt-out properties (from REMS) using the property owners' Tax Identification Number (TIN), which is common across both database systems. Because TIN is owner-specific rather than property-specific, however, multiple properties belonging to the same owner can have the same TIN. Thus, we used a matching algorithm to further ensure that the MTCS/PIC addresses of the voucher recipients found in the TIN matching are in the projects with address locations of the opt-out properties identified in REMS. This check yielded a final study sample of 9,012 voucher recipients. Gross rent information was available on the MTCS/PIC file for 8,956 of the housing units occupied by these voucher recipients. Together, they represent housing units from 449 opt-out properties. These units are 34 percent of the total 26,691 units. A total of 2,267 units that received enhanced vouchers were identified, as were 6,689 that received regular vouchers.

[20] We cannot determine whether the rents for those units are now higher than the contract rents on the basis of which HUD paid subsidies when the units were part of the assisted stock, because we do not have rent data for that period.

For study purposes, affordability is measured by comparing gross rent divided by FMR. Units with gross rents below the FMR are considered affordable, while units with rents above the FMR are considered not affordable. We further divide the affordable units into very affordable (rent less than 75 percent of FMR) and moderately affordable (rent between 75 and 100 percent of FMR). Similarly, we divide the unaffordable units into moderately unaffordable (rent between 100 and 125 percent of FMR) and very unaffordable (rent greater than 125 percent of FMR). We use the FMR as a measure of affordability because it is based on the 40th percentile (and in some places the 50th percentile) in the rent distribution.

As can be seen from Table 5.1, more than half of the units that opted out were affordable at the end of 2004. These include 8 percent of units that were very affordable (rent less than 75 percent of FMR) and 51 percent of units that were moderately affordable (rent between 75 and 100 percent of FMR). Among the units that had rents above the local FMR, the vast majority were moderately unaffordable (rents were between 100 and 125 percent of FMR).[21] Only 10 percent of units were very unaffordable (rents were above 125 percent of FMR).

Table 5.1. Post-opt-out Rent Affordability of Opt-out/Prepay Units

	Rent Affordability Category	Number of Units	Percent
All Voucher Units			
Affordable units	Rent/FMR less than or equal to 0.75	735	8%
	Rent/FMR greater than 0.75 but less than or equal to 1	4,571	51%
Not affordable units	Rent/FMR greater than 1 but less than or equal to 1.25	2,730	31%
	Rent/FMR greater than 1.25	920	10%
Total		8,956	100%
Regular Voucher Units			
Affordable units	Rent/FMR less than or equal to 0.75	616	9%
	Rent/FMR greater than 0.75 but less than or equal to 1	3,383	51%
Not affordable units	Rent/FMR greater than 1 but less than or equal to 1.25	1,934	29%
	Rent/FMR greater than 1.25	756	11%
Total		6,689	100%
Enhanced Voucher Units			
Affordable units	Rent/FMR less than or equal to 0.75	119	5%
	Rent/FMR greater than 0.75 but less than or equal to 1	1,188	52%
Not affordable units	Rent/FMR greater than 1 but less than or equal to 1.25	796	35%
	Rent/FMR greater than 1.25	164	7%
Total		2,267	100%

[21] Program rents can be well above the FMR for several reasons. First, the PHA can set the payment standard up to 110 percent of FMR, or up to 120 percent with approval from the field office. In addition, current program rules allow households to spend more than the payment standard on rent, if the rent is above the payment standard. Households can spend up to 40 percent of income on rent at the start of a new lease to go above the payment standard, and they can spend even more upon contract renewal.

The table also shows that the share of affordable units among those that received enhanced vouchers was similar to affordable share among units that received regular vouchers. Interestingly, units with regular vouchers were more likely to be very unaffordable than units that received enhanced vouchers. This may be because regular vouchers are more common in the higher rent areas of the country, including the New England, Mid-Atlantic, and Pacific regions, while enhanced vouchers are more common in the lower rent East North Central and West North Central regions. Furthermore, as can be seen in Table 5.2, in some regions, rents in enhanced voucher units are actually below rents in regular voucher units.[22]

Another possible reason for the lower rents in enhanced voucher units may be that in these properties rents increased more sharply after the opt-out/prepay, so that the only voucher holders living in the property have enhanced vouchers. In other properties, it may be that rents did not go up as high, so that regular voucher holders can afford to live in the units at rents just slightly above the FMR. Table 5.2 shows the number of units and median gross rent by region.

Table 5.2. Number of Units and Median Gross Rent by Region

Region	Regular Voucher		Enhanced Voucher	
	Number of Units	Median Gross Rent	Number of Units	Median Gross Rent
New England	455	$1,080	27	$925
Mid Atlantic	1,017	$1,311	101	$1,085
East North Central	837	$549	711	$562
West North Central	321	$538	364	$680
South Atlantic	776	$645	304	$675
East South Central	289	$495	38	$432
West South Central	805	$574	148	$662
Mountain	552	$547	197	$650
Pacific	1,637	$871	377	$920

Table 5.3 shows additional characteristics of properties by post-opt-out/prepay affordability categories. The table shows that:

- Most very unaffordable units (64 percent) opted out/prepaid in 1999. Over 25 percent of the moderately unaffordable opt-outs/prepays did so also in 1999. The largest group of very affordable units (38 percent) opted out/prepaid in 2000, and nearly half the group of moderately affordable units opted out/prepaid in 2000 and 2001.

- Half of the very affordable units were located in the South; more than a third were in the West. Only 6 percent of all affordable units were in the Northeast. Nearly three-

[22] For example, 7 percent of regular vouchers were in the New England region, 15 percent were in the Mid-Atlantic region, and 24 percent were in the Pacific region. The comparable percentages for enhanced vouchers were 1, 4, and 17 percent respectively. In contrast, 31 percent of enhanced vouchers were in the East North Central region and 16 percent were in the West North Central region. The comparable percentages for regular vouchers were 13 and 5 percent.

quarters (72 percent) of the most unaffordable units were in the Northeast, and virtually none (1 percent) were in the South.

- Unaffordable units were concentrated in suburban locations.

- Family-occupied units were among the most and least affordable. Of the most affordable group, 87 percent were family units, as was 82 percent of the least affordable group. In contrast, about two-thirds of each of the two other groups were family units.

- Nearly all (96 percent) of the very affordable units had been Older Assisted, compared with about two-thirds of the very unaffordable units.

- Affordable units are distributed across all property-size categories. In contrast, few unaffordable units were in properties with more than 200 units, and no very unaffordable properties had more than 200 units.

- The more affordable units tended to be in neighborhoods that had higher concentrations of poverty and higher concentrations of minority households compared with less affordable units. In contrast, the most unaffordable units were in neighborhoods with the lowest poverty rates and the lowest concentrations of minority households.

Table 5.3. Units across Post-opt-out Rent Affordability Categories

	Affordable Units		Not Affordable Units		
	Rent/FMR ≤ 0.75	0.75 < Rent/FMR ≤ 1	1 < Rent/FMR ≤ 1.25	Rent/FMR > 1.25	Total
All Voucher Units					
Number of units	735	4,571	2,730	920	8,956
Percent of units	8%	51%	31%	10%	100%
Voucher Characteristic					
Enhanced voucher	16%	26%	29%	18%	25%
Not enhanced voucher	84%	74%	71%	82%	75%
Total	100%	100%	100%	100%	100%
Opt-out/Prepay Fiscal Year					
1997 or before	6%	5%	1%	0%	3%
1998	18%	17%	5%	0%	11%
1999	7%	14%	27%	64%	23%
2000	38%	22%	14%	5%	19%
2001	12%	23%	15%	12%	18%
2002	8%	5%	15%	15%	10%
2003	9%	12%	14%	2%	11%
2004	1%	3%	8%	0%	4%
Total	100%	100%	100%	100%	100%
Census Division					
New England	2%	2%	9%	14%	5%
Mid Atlantic	3%	5%	13%	58%	12%
East North Central	4%	25%	11%	8%	17%
West North Central	7%	7%	10%	6%	8%
South Atlantic	21%	12%	13%	1%	12%
East South Central	2%	4%	5%	0%	4%
West South Central	26%	14%	4%	0%	11%
Mountain	16%	9%	7%	0%	8%
Pacific	18%	23%	27%	13%	22%
Total	100%	100%	100%	100%	100%
Census Region					
Northeast	5%	6%	23%	72%	18%
Midwest	11%	32%	20%	14%	25%
South	50%	30%	23%	1%	26%
West	35%	32%	34%	13%	31%
Total	100%	100%	100%	100%	100%
Metropolitan Location					
Metropolitan/suburb	35%	40%	34%	66%	41%
Metropolitan/central city	59%	48%	51%	28%	48%
Non-metropolitan	7%	12%	14%	6%	12%
Total	100%	100%	100%	100%	100%
Occupancy Type					
Family	87%	66%	65%	82%	69%

Table 5.3. Units across Post-opt-out Rent Affordability Categories (continued)

	Affordable Units		Not Affordable Units		
	Rent/FMR ≤ 0.75	0.75 < Rent/FMR ≤ 1	1 < Rent/FMR ≤ 1.25	Rent/FMR > 1.25	Total
Elderly/Disabled	13%	34%	35%	18%	31%
Total	100%	100%	100%	100%	100%
HUD Assistance Type					
Older assisted	96%	70%	55%	66%	67%
Newer assisted	4%	30%	45%	34%	33%
Total	100%	100%	100%	100%	100%
Development Size					
< 50 units	37%	24%	32%	12%	26%
50-99 units	23%	32%	24%	38%	29%
100-199 units	17%	28%	36%	51%	32%
200+ units	23%	17%	8%	0%	13%
Total	100%	100%	100%	100%	100%
Neighborhood Characteristics					
Average poverty rate	20%	18%	18%	10%	17%
Average percentage of racial/ethnic minorities	60%	44%	38%	26%	42%

A second way to look at affordability is to compare rents with local incomes to assess whether units are affordable to households at various income levels relative to the local area median. A unit is considered affordable if a household with a specific income relative to the median can afford to rent the unit spending no more than 30 percent of income on gross rent.

Table 5.4 gives a distribution of rent affordability at various income levels. In particular, this table shows that, overall, 6 percent of the sample units had rents that would be affordable to *unassisted* households with incomes at 30 percent of area median income (AMI). In other words, only 6 percent of the sample units have rents that are affordable at or below 30 percent of the relevant AMI, if the household did not have a voucher. Similarly, 64 percent of units would be affordable to households with incomes at 50 percent of AMI, 88 percent would be affordable to those with incomes at 80 percent of AMI, and 94 percent would be affordable to those with incomes at 100 percent of AMI.

Table 5.4. Post-opt-out/prepay Rent Affordability of Units by Income Group

Rent Affordability Category	Number of Units	Percent
All Voucher Units		
Rents affordable at income = 30% of AMI	551	6%
Rents affordable at income = 50% of AMI	5,732	64%
Rents affordable at income = 80% of AMI	7,864	88%
Rents affordable at income = 100% of AMI	8,404	94%
Total	8,956	100%
Regular Voucher Units		
Rents affordable at income = 30% of AMI	396	6%
Rents affordable at income = 50% of AMI	3,981	60%
Rents affordable at income = 80% of AMI	5,726	86%
Rents affordable at income = 100% of AMI	6,198	93%
Total	6,689	100%
Enhanced Voucher Units		
Rents affordable at income = 30% of AMI	155	7%
Rents affordable at income = 50% of AMI	1,751	77%
Rents affordable at income = 80% of AMI	2,138	94%
Rents affordable at income = 100% of AMI	2,206	97%
Total	2,267	100%

Results differ for regular and enhanced voucher holders. Table 5.4 shows that a higher fraction of units with enhanced vouchers are affordable at the various income groupings. For example, 6 percent of units with regular vouchers would be affordable to unassisted households with incomes at 30 percent of area median, compared with 7 percent of enhanced voucher units. Similarly, 60 percent of units with regular voucher holders would be affordable to unassisted households with incomes at 50 percent of area median, compared with 77 percent of enhanced voucher units.

Table 5.5 shows other features of note:

- The majority of units that are affordable to households with incomes at 30 percent of area median are in the East North Central and West North Central divisions. Only 7 percent of these units are in the Pacific region. Nearly one-quarter of units that are affordable with incomes at 80 percent of area median and at 100 percent of area median are in the Pacific division.

- The majority of units that are affordable at all income levels are in central cities. As the income range rises, however, the percent of affordable units in suburban areas increases. Only 25 percent of units that are affordable to households with incomes at 30 percent of area median are in suburbs, compared with 38 percent of units that are affordable with incomes at 100 percent of area median.

- Half the units that are affordable to households with incomes at 30 percent of area median are family-occupied units, compared with 68 percent of units that are affordable with incomes at 100 percent of area median.

- Three-quarters of the units that are affordable to households with incomes at 30 percent of area median were assisted under the older assistance programs, compared with 66 percent of units that are affordable with incomes at 100 percent of area median.

- Units that were affordable to the lowest income group tend to be in smaller properties. Over half (55 percent) of the units that were affordable to households with incomes at 30 percent of area median were in properties with fewer than 50 units, and only 20 percent were in properties with more than 100 units. Properties that are affordable to all other income groups were more evenly distributed across size categories, although few had more than 200 units.

- Neighborhood poverty rates are similar across all affordability categories.

Table 5.5. Units Affordable by Income Groups

	Rents affordable at 30% of AMI	Rents affordable at 50% of AMI	Rents affordable at 80% of AMI	Rents affordable at 100% of AMI	Total
All Voucher Units					
Number of units	551	5,732	7,864	8,404	8,956
Percent of units	6%	64%	88%	94%	100%
Voucher Characteristic					
Enhanced voucher	28%	31%	27%	26%	25%
Not enhanced voucher	72%	69%	73%	74%	75%
Total	100%	100%	100%	100%	100%
Opt-out/prepay Fiscal Year					
1997 or before	3%	3%	4%	3%	3%
1998	9%	15%	13%	12%	11%
1999	15%	16%	17%	19%	23%
2000	35%	21%	21%	20%	19%
2001	24%	20%	19%	19%	18%
2002	10%	8%	10%	10%	10%
2003	4%	11%	12%	12%	11%
2004	1%	5%	5%	4%	4%
Total	100%	100%	100%	100%	100%
Census Division					
New England	2%	4%	5%	5%	5%
Mid Atlantic	2%	2%	4%	8%	12%
East North Central	30%	24%	19%	18%	17%
West North Central	22%	12%	9%	8%	8%
South Atlantic	11%	16%	14%	13%	12%
East South Central	3%	5%	4%	4%	4%
West South Central	3%	14%	12%	11%	11%
Mountain	20%	11%	10%	9%	8%
Pacific	7%	12%	24%	23%	22%
Total	100%	100%	100%	100%	100%
Census Region					
Northeast	4%	6%	9%	13%	18%
Midwest	52%	36%	28%	26%	25%
South	17%	35%	30%	28%	26%
West	27%	23%	33%	32%	31%
Total	100%	100%	100%	100%	100%
Metropolitan Location					
Metropolitan/suburb	25%	32%	36%	38%	41%
Metropolitan/central city	55%	52%	50%	50%	48%
Non-metropolitan	20%	16%	13%	12%	12%
Total	100%	100%	100%	100%	100%
Occupancy Type					
Family	50%	60%	66%	68%	69%
Elderly/Disabled	50%	40%	34%	32%	31%
Total	100%	100%	100%	100%	100%
HUD Assistance Type					
Older assisted	77%	67%	66%	66%	67%
Newer assisted	23%	33%	34%	34%	33%
Total	100%	100%	100%	100%	100%
Development Size					
< 50 units	55%	31%	28%	27%	26%
50-99 units	24%	25%	29%	29%	29%
100-199 units	17%	25%	28%	30%	32%
200+ units	3%	18%	15%	14%	13%
Total	100%	100%	100%	100%	100%
Neighborhood Characteristics					
Average poverty rate	19%	19%	18%	18%	17%
Average percentage of racial/ethnic minorities	33%	39%	43%	43%	42%

In summary, this analysis shows that well over half (59 percent) of the sample of opt-out/prepay units were affordable in 2004, in the sense that they had rents below the FMR. Without rents from the time before the opt-outs or prepayments, it was not possible to estimate whether rents in these units are higher or lower relative to the FMR than they were at the time of the opt-out.

Even with rents at or below FMR, however, only 6 percent of units could be rented by unassisted households with incomes under 30 percent of the local AMI, assuming they spent no more than 30 percent of income on rent. Sixty-four percent of these units could be rented by unassisted households with incomes at 50 percent of the local AMI.

6. Conclusions and Policy Recommendations

In this chapter we summarize our key findings in the three study areas: the quantitative analysis (including both cross-tabulation and regression analyses), the case studies, and the affordability analysis. We conclude by offering policy recommendations based on those findings.

6.1 Key Findings

Quantitative Analysis

The main finding of the quantitative analysis is that property characteristics *are* associated with the owners' decision to leave the Section 8 program or prepay their subsidized mortgages. We made additional findings of significance and summarize those across five key areas: property location, type and level of program assistance, unit size and age, specialized housing status, and physical and financial characteristics. In some cases, the results produced by the regression analyses differ slightly from those produced by the cross-tabulation analyses. We make note of the differences where they occur.

Property location matters

Properties with rents below the local FMR are more likely to leave the assisted stock. This result is confirmed by both the cross-tabular and regression analyses. These properties are located in areas where the owners apparently believe that they can obtain higher rents for their properties in the unassisted market than they can charge under the assisted programs. Additional findings include the following:

- Opt-out/prepayment properties are located in neighborhoods with higher median incomes, higher median rents, and lower poverty and vacancy rates than properties that remain in the stock.

- The cross-tabulation analysis shows that the Pacific Census Division, with 13 percent of the properties, has 21 percent of the opt-outs/prepayments. The Mountain and West South Central regions are also highly represented in opt-outs/prepayments relative to the total number of properties in those regions. The regression results support this finding and also indicate that properties in the Mid-Atlantic, East, and West North Central regions are more likely to opt out than those in the New England and East South Central regions.

- Opt-outs/prepayments occur more frequently in suburban and metropolitan/central city locations and less frequently in non-metropolitan locations, according to cross-tabulation results. The regression analysis supports the finding regarding central city locations, but indicates that non-metropolitan properties have a higher likelihood of opting out relative to suburban locations. (The Section 8/515 program is focused in non-metropolitan locations, and properties in this program are very likely to opt in.)

Type and level of program assistance affect opt-out decisions

Older Assisted properties are significantly more likely than Newer Assisted properties to be at the extremes in terms of outcomes. They are more likely to either opt out/prepay (possibly an indicator of financial success) or to be in foreclosure/enforcement (which is an indicator of failure). Another significant finding from the regression analysis is that, all else equal, properties that are 100-percent assisted have a higher likelihood of opting out compared with properties where only a few units are assisted. This may be because properties that are 100-percent assisted can receive the maximum rent increase after the conversion to market rate.

Occupancy type, unit size and age make a difference in the opt-out decision

Family-occupied properties are more likely than elderly/disabled to opt out. They are also more likely to be in foreclosure or to be referred to the Enforcement Center. Cross tabulation results also indicate the following:

- Opt-in properties are more likely to have zero- and one-bedroom units; this frequently means the property houses elderly people or people with disabilities.
- Opt-out/prepay and foreclosure/enforcement properties are more likely to have two- and three-bedroom (family) units.
- Units for large families (four or more bedrooms), occur more frequently in foreclosure/enforcement properties.
- Buildings constructed before 1975 were prevalent in both the opt-out/prepay and the foreclosure/enforcement categories.

Specialized housing may influence the opt-in and opt-out decision

Properties designated for the elderly and/or disabled represent more than 49 percent of the opt-in properties, but represent only 12.9 percent of opt-out/prepay and 8.9 percent of the foreclosure/enforcement category. Conversely, 91.1 percent of the properties in foreclosure/enforcement are family-designated properties, and 87.2 percent of opt-out/prepays are family-designated.

Physical and financial characteristics are correlated with the opt-in and opt-out decision

- As expected, properties in foreclosure/enforcement had the lowest average REAC physical inspection scores (although not all enforcement actions are related to physical condition).

- Opt-out/prepay properties had somewhat lower physical inspection scores than those that opted in and those that did not face a choice during the study period.

- Owners generally did not opt out of their Section 8 contract before prepayment.

- Prepayment occurred about equally before and at the same time as the opt-out.

Case Studies

The case studies, based on observations made at the site visits, provide additional information on owners' motivation to opt out or remain in the Section 8 program. Although these factors are both economic and non-economic in nature, economic factors generally appear to be the key drivers in the opt-out decision**.**

Economic factors are key drivers in opt-out decision

Two of the case study locations—Sacramento and Dallas—support the quantitative analysis finding that properties located in growing markets with increasing rents and opportunities for market-rate rentals are more likely to leave the stock. Owners of opt-outs in both of these markets reported that they chose to remove their housing from the assisted stock when they believed it was in their economic interest to do so. On the other hand, opt-out owners in Cincinnati, the third case-study site, may have been motivated by more than just economic factors, citing non-economic reasons to justify their decision (see below).

Another interesting economic factor is that a program with no expansion opportunities may lessen the incentive for ongoing participation by owners. Project-based Section 8 is not being funded for new units, with minor exceptions for property-disposition activities. One Sacramento owner said he opted out because, with no new opportunities/incentives in the program, he is reluctant to maintain specialized skills necessary to participate. In this case, an owner who was primarily market-oriented wanted to streamline operations, and seeing no opportunities to expand in the program, decided to opt out. By opting out, the landlord transfers the need for specialized skills to the voucher administrator.

Non-economic factors can also affect the opt-out decision

At the same time, the case studies yield insights into non-economic factors that are not able to be determined through the quantitative analysis, but which can also affect an owner's decision to opt out. Some of the non-economic factors to emerge from our site visits were the following:

- Consistent with the quantitative analysis, which found that nonprofit-owned properties comprise only a small portion of properties opting out/prepaying, one case study property was owned by a nonprofit owner who was mission-driven and chose to keep properties in the assisted stock, regardless of economic incentives.

- The owners interviewed in Dallas and Cincinnati spoke about their sense that they were no longer viewed as partners with HUD in providing low-income housing, and that HUD was increasingly rigorous in its requirements of owners. During the relevant opt-out time period, HUD improved its oversight of properties and Section 8 contracts through a new property inspection protocol and a requirement for electronic submission of annual financial statements. Both imposed a greater burden on owners.

- One Sacramento owner retained a portion of his portfolio as Section 8 rentals as a result of public pressure.

- A second Sacramento owner did not opt out of the Section 8 program, apparently due to inertia (although the owner is now pursuing the sale of the property to a nonprofit owner who will maintain it as low-income housing).

- A Cincinnati owner cited fear of change and his own age as a reason not to opt out, even though he owned some properties in locations that he thought could command higher rents in the unassisted market.

- One Dallas opt-in property owner cited an improving working relationship with HUD as making the job easier, as well as being affiliated with an owner with enough Section 8 units to have specialized support staff, including a grants specialist.

Affordability Analysis

The affordability analysis indicates that opt-out does not always mean a loss of affordable housing, if housing vouchers are available. The affordability analysis indicates that:

- Well over half (59 percent) of the sample of opt-out/prepay units were affordable to voucher holders in 2004—that is, they had rents below the local FMR. (Without rent data from the time of the opt-outs it is not possible to determine whether rents in these units rose or fell following the opt-out or prepayment).

- Most of the remaining units had rents that were between 100 and 125 percent of FMR. Depending on how high the payment standards were set by the voucher administrator, this could mean that households with vouchers were spending more than 40 percent of income for rent.

- However, if households do not have any rental assistance such as vouchers, the number of units affordable to very-low-income households drops. Even with rents at or below FMR, only 6 percent of units could be rented by unassisted households with incomes at 30 percent of the local AMI, assuming they spent 30 percent of income on rent. In contrast, 64 percent of units could be rented by unassisted households earning 50 percent of the local AMI.

The case studies supported the findings of the affordability analysis, showing that:

- One of the Sacramento properties retained a significant number of voucher holders in the property.
- In one of the Dallas properties the majority of tenants stayed, and rents have leveled or decreased.
- The second Dallas opt-out property remained affordable through tax-exempt bond restrictions.
- A large opt-out owner in Cincinnati has an affordable portfolio that is now largely supported by tax credits.
- One of the opt-out properties in Cincinnati is still occupied by similar income tenants as before, some of whom use vouchers.
- Only one of the opt-out properties in the case studies was converted to non-rental (condominium) use.

6.2 Recommendations

Based on the study, we make the following policy recommendations to HUD. If the policy goal is to keep properties in the assisted housing stock, we suggest that HUD consider policies to offset both the economic and the non-economic incentives to opt out. We have two recommendations for policies bearing on economic factors. First, consider whether the Section 8 project-based program rules can be made less complex or supported more fully through software to reduce the burden on owners. Second, target resources and incentives that encourage staying in the assisted housing programs to areas where rents after opt-out are less affordable.

With respect to non-economic factors, we suggest that HUD establish better communication regarding rent-setting policies, not only within the Mark-to-Market program, but also for the Mark-up-to-Market policy affecting regular renewals.

In summary, this study examined the characteristics of properties that have left the HUD-assisted stock either through prepayment or through opting out, and compared them with characteristics of properties that have remained in the HUD programs. As expected, markets matter. Properties with assisted rents below prevailing market levels are more likely to leave the stock than are properties with rents closer to market levels. Non-economic factors such as local community pressures to preserve affordable housing or difficult relations with local HUD offices, however, also influence owner decisions to either stay in the stock or leave. Once properties leave the assisted stock, some owners do reposition properties and raise rents, but at least a portion of the properties that leave the stock remain rented and affordable to low-income households.

Appendix—Data Collection Guides for Case Studies

1. Discussion Guide for HUD Asset Manager

Name of Respondent: ____
Phone Number: ____
Email: ____
Position of Respondent: ____
Date of interview: ____
Econometrica/Abt Interviewer: _____________________________________
Phone/Onsite? ____

Econometrica Inc. and Abt Associates are research companies in the Bethesda, Maryland area. We are conducting a study for the US Department of Housing and Urban Development comparing HUD assisted multifamily properties that have terminated their assistance relationship with HUD to those that continue to receive HUD subsidies. The study will examine why owners decided to opt out or stay in the program and what outcome that has had on the properties and communities.

Thank you for agreeing to speak with me today. Your opinions and ideas are important for our study. The information you provide will be summarized in the research reports but we will not identify you personally in any of our reports. I have a set of topics that I would like to discuss today, but please feel free to raise any other issues that you think are important.

Interviewee Information

[*The goal is to interview the actual asset managers for the four properties or, if it seems to make more sense, the chief of the asset management branch within the MF division or even the chief of MF. The research team will search for the best candidate to interview.]*

1. How long have you been the asset manager for each of the properties? (If it is the asset manager that is interviewed.)
2. If it is the chief of the multifamily division, ask what is the involvement he/she has had with the subject properties?

Sampled Projects

We are studying four projects in the X metropolitan area. Two have opted out and two have chosen to remain subsidized.

Discuss one property at a time. *I'd like to talk [first] about [name the property*.]

3. What can you tell about its history over the past 10 years that may explain why it [opted out/did not opt out]?
4. How does this property differ from other properties for which you are the asset manger? Is it well located/poorly located? Are any in an area where market rents are increasing?
5. What can you tell me about the location of the property, amenities, rents vs. market rents, its history of rent increases [e.g., *constrained by statutory limitations on Section 8 rents compared to FMRs? Tried to get rent increases based on comparability studies? With or without success (i.e., was this a "mark up to market"? Eligible for M2M and, if so, made any moves down that path*).]
6. Can you tell me about other aspects of the property? *[Mention the REAC physical and financial scores and ask the asset manager to comment. Try to figure out whether the asset manager thinks this is or was a problem owner or a problem property.]*
7. What do you think about the owner's decision process?
8. How was the decision to opt out or stay in made and who made it?
9. Was it a straightforward economic calculation or were there other considerations?
10. Were there legal impediments or community/political pressure that may have influenced the decision?
11. Are you familiar with the market in the neighborhood of any of these projects? What can you tell us about trends in these sub-markets?

Policies and Procedures

12. In your opinion what are the strengths and weaknesses of the Section 8 contract renewal process?
13. *[If it is an opt- out establish whether in these cases the owner would opt out because the process didn't permit him to get the rent increases he should have gotten or to figure out what was going to happen if he stayed in the program in a timely way].* In your opinion did the owner encounter problems in getting market rent-renewals? Did any group besides the owner want the property to leave the Section 8 inventory (e.g., as part of a redevelopment plan for the neighborhood)?
14. *[If it is an opt-in establish if opt-ins had an easy time making a commitment to stay in the program. Try to establish whether the owner got an above market rent renewal or was allowed to access the*

property's residual receipts.] In your opinion what prompted the owner to remain in the program? Were there other influences on the owner's decision? Was the owner able to find additional resources for the property that made him decide to stay in (e.g., LIHTC or HOME or other local funds)?

15. About how many Section 8 contract renewals does the field office process a year?
16. Is the process difficult to administer? If so, what are the difficulties?
17. What are the most important considerations?
18. Drawing on your experience with owners of Section 8 properties, why do you think owners choose to opt-out? Alternately, why do owners choose to opt-in?

Impact of Opt-Outs

19. What happened to the tenants? Did they get vouchers? Were they enhanced vouchers? If they got regular vouchers, did they use the vouchers to stay in the property or to go elsewhere?
20. Are you familiar with the tenants in the property after the opt-out? If so, can you give me information on incomes ranges, type household, what is the property's market niche post opt-out? Have any new households moved in with vouchers?
21. What is the future of the property? Is the use likely to change over time (e.g., no longer rental housing, redeveloped as luxury housing? Or are the rent levels and occupancy patterns likely to remain the way they are now?)
22. From your experience, are some properties more likely to opt out than others? What makes them more likely to opt-out or stay in the program (e.g., is the local rental market, how well the property is maintained or neighborhood conditions influential in the outcome)?

Impact of Opt-Ins

23. Has anything changed since the owner's decision to renew the contract?
24. Is the property providing the same type of housing to the same group of tenants?
25. How likely is it that the decision to opt-in was temporary and that the owner will opt out in the future? If not likely, is it because of barriers [e.g., the property has LIHTC restrictions—or because there are no real market opportunities for the property?]
26. Are there problems with the property that will cause it not to provide good quality housing over time or is it likely to leave the Section 8 program through default?
27. Does the property have a positive or negative impact on its neighborhood? Can you tell me why?

28. Does the property provide any special opportunities or amenities for its residents (e.g., near jobs, near services, have service programs on site?
29. Were there any negative impacts?

Ask for any available documents relating to the property such as:

- *Monitoring reports.*
- *Any comparability studies submitted by property owners when they chose to opt-out of the Section 8 program.*
- *Independent appraisals of rental housing properties in neighborhoods proximate to the sample properties*.

2. Discussion Guide for HUD Regional Economist

Name of Respondent: ____
Phone Number: ____
Email: ____
Position of Respondent: ____
Date of interview: ____
Econometrica/Abt Interviewer: _______________________________________
Phone/onsite? ____

Econometrica Inc. and Abt Associates are research companies in the Bethesda, Maryland area. We are conducting a study for the US Department of Housing and Urban Development comparing HUD assisted multifamily properties that have terminated their assistance relationship with HUD to those that continue to receive HUD subsidies. The study will examine why owners decided to opt out or stay in the program and what outcome that has had on the properties and communities.

Thank you for agreeing to speak with me today. Your opinions and ideas are important for our study. The information you provide will be summarized in the research reports but we will not identify you personally in any of our reports. I have a set of topics that I would like to discuss today, but please feel free to raise any other issues that you think are important.

We are studying four projects in the __ metropolitan area. Two have opted out and two have chosen to remain subsidized.

Interviewee Information

1. Please tell me what your current position is and how long you have been in that position.
2. Were you in there during the period when the opt-outs/opt-ins for the four properties occurred?

Sampled Projects

3. How familiar are you conditions in the rental market in this metropolitan area over the last 10 years? Could you describe trends in the overall market?
4. What can you tell about me about history of the four properties as far as marketability goes? Were their program rents out of line with the local market and their specific sub-market?
5. Are you familiar with the market in the neighborhood of any of these properties? What can you tell me about trends in these sub-markets?

6. Do you have any information on the spread between current rent and market rent in the properties that we are looking at which opted-out of the program?
7. Do the “opt-out” properties represent a trend in their local housing market or are they in some sense outliers?
8. What are the impacts of opt-outs? For the subject properties, what were the negative or positive impacts on the housing market? On the tenants? On the community?
9. What are the impacts of opt-ins? For the subject properties, what were the negative or positive impacts on the housing market? On the tenants? On the neighborhood?

Affordability Issues

10. How affordable do rents remain in areas where the conversions occurred?
11. How affordable have the rents remained in the subject properties?
12. How easy/hard it is to use vouchers, especially in the neighborhoods where the four properties are located?
13. Do costs vary widely from one neighborhood to another?
14. Finally, do you know or can recommend local experts who we can interview about what is happening in the housing market in general and in the sub-markets where the four properties are located?

Ask the Field Economist to provide us with any available documents relating to the property such as:

- *Independent appraisals of rental housing properties in neighborhoods proximate to the sample properties.*
- *Market studies of the neighborhoods where the four properties are located.*

3. Discussion Guide for Property Owners Who Have Opted Out

Name of Respondent: ____
Phone Number: ____
Email: ____
Property Name/location: _____________________________________
Date of interview: ____
Econometrica/Abt Interviewer: ________________________________
Phone/onsite? ____

Econometrica Inc. and Abt Associates are research companies in the Bethesda, Maryland area. We are conducting a study for the US Department of Housing and Urban Development comparing HUD assisted multifamily properties that have terminated their assistance relationship with HUD to those that continue to receive HUD subsidies. The study will examine why owners decided to opt out or stay in the program and what outcome that has had on the properties and communities.

Thank you for agreeing to speak with me today. Your opinions and ideas are important for our study. The information you provide will be summarized in the research reports but we will not identify you personally in any of our reports. I have a set of topics that I would like to discuss today, but please feel free to raise any other issues that you think are important.

Interviewee Background

1. How long have you owned or been involved with this property?
2. In what form is the ownership entity organized (e.g., sole owner, limited partnership, partnership, etc.)?
3. Who makes the decisions and how are those decisions made?
4. Do you own other HUD-subsidized housing properties?
5. Has you or your organization removed any of these properties from Section 8, or is it considering doing so in the future

Reasons for Opting Out

We use the term "opting out" to cover the process of terminating the assistance relationship with HUD and making the property a market property.

6. When was the project eligible to opt out?
7. Why did the ownership decide to opt out?
8. What did you believe was the alternative use of the property and why?

9. How did the ownership arrive at the decision? What were the most important factors encouraging you to opt-out? Were there any considerations that discouraged you from opting out?
10. Did you do market studies?
11. Why did you decide to opt-out?
12. Were rents below market rate at the time of the opt-out?
13. Do owners of HUD-subsidized housing properties tend to “opt-out” in your local housing market or was your decision unusual for the local market?
14. Are there any circumstances in which you would have remained in the program?
15. What was the ownership’s contractual relationship with HUD while the property was *in* the program? Did that relationship influence the decision to opt out?

Outcomes

16. What was the property like at the time of the opt-out?
17. What is the property like now?
18. Have you made any major physical changes?
19. Are you fully leased up?
20. How is the property financed?
21. Are there any emerging issues or circumstances that you think could affect the financial viability of the property? If so, please describe.
22. In your opinion, what was the impact of the opt-out on your organization?

Affordability Issues

23. Do you know to what extent previous residents continue to live in the property?
24. Is the local rental market above HUD’s FMRs?
25. Have rent levels changed much?
26. Are rent levels competitive with the rent levels in the immediate area?
27. What are the current rents in the building?
28. If rent is not thought affordable for tenants, ask how long it has been a problem and how serious is the problem.

Other topics may be discussed depending on how the conversation unfolds.

4. Discussion Guide for Property Owners of Opt-In Properties

Name of Respondent: ____
Phone Number: ____
Email: ____
Property Name/location: ____
Date of interview: ____
Econometrica/Abt Interviewer: ____________________________________
Phone/Onsite? ____

Econometrica Inc. and Abt Associates are research companies in the Bethesda, Maryland area. We are conducting a study for the US Department of Housing and Urban Development comparing HUD assisted multifamily properties that have terminated their assistance relationship with HUD to those that continue to receive HUD subsidies. The study will examine why owners decided to opt out or stay in the program and what outcome that has had on the properties and communities.

Thank you for agreeing to speak with me today. Your opinions and ideas are important for our study. The information you provide will be summarized in the research reports but we will not identify you personally in any of our reports. I have a set of topics that I would like to discuss today, but please feel free to raise any other issues that you think are important.

Interviewee Background

1. How long have you owned/or been involved with this property?
2. In what form is the ownership entity organized (e.g., sole owner, limited partnership, partnership, etc.)?
3. Who makes the decisions and how are those decisions made?
4. Do you own other HUD-subsidized housing properties?
5. Have you or your organization removed any of these properties from Section 8, or is it considering doing so in the future?

Reasons for Staying in the Program (Opting-in)

6. When the opportunity arose to remove this property from the Section 8 program, did you or your organization consider taking the property out?
7. [*Whether they answer yes or no to the previous question ask*] What were the primary factors influencing the decision to keep the property in the program?
8. Were any legal or contractual restrictions important in the decision to keep this program in Section 8? If so, if the restrictions had not been in

place would the organization considered taking the property out of Sectiion8?

9. Were there financial, commercial, market-driven, business-related or other economic motivations for keeping the property in the program?
10. Were there communal (charitable), socially driven, motivations for keeping the property in the program?
11. When will the property next be eligible to opt out? Have you made any preliminary decisions about opting-out in the future? What factors do you see influencing that decision? (e.g., local imposed restrictions, restrictions based on original ownership, special zoning requirements, etc.)
12. Does this organization own any other Section 8 properties? Has the organization removed any of these properties from Section 8, or is it considering doing so in the future? What factors have been or are influential in these decisions?

Tenant Characteristics

13. What are the demographic characteristics of tenants (e.g., income levels, families, elderly) of the tenants currently resident at the sample property?
14. Are tenants likely to stay in the property, if it were removed from the program?
15. If the sample property were removed from Section 8 could the tenants use vouchers to find housing they can rent in the same neighborhood?

5. Discussion Guide for Property Site Managers of Opt-Out Properties

Name of Respondent: ____
Phone Number: ____
Email: ____
Property Name/location: ____
Date of interview: ____
Econometrica/Abt Interviewer: ____
Site/Location: ____

Econometrica Inc. and Abt Associates are research companies in the Bethesda, Maryland area. We are conducting a study for the US Department of Housing and Urban Development comparing HUD assisted multifamily properties that have terminated their assistance relationship with HUD to those that continue to receive HUD subsidies. The study will examine why owners decided to opt out or stay in the program and what outcome that has had on the properties and communities.

Thank you for agreeing to speak with me today. Your opinions and ideas are important for our study. The information you provide will be summarized in the research reports but we will not identify you personally in any of our reports. I have a set of topics that I would like to discuss today, but please feel free to raise any other issues that you think are important.

Interviewee and Property Background

1. How long have you managed this property? Were you the property manager when this property was in HUD's Section 8 program?
2. If yes, do you know any of the reasons why the owners took the property of Section 8? If yes, could you tell me what were the most important reasons?

Recent History of the Property

3. Have the owners made any significant upgrades or investments in the property since it has been out of Section 8? (Just tell me about the period of time you know about.) If yes, could you tell me what these upgrades were?
4. What are the current rent levels for different size units? How regularly have these rates been raised? Do you think that these rates are "in sync" with others in the neighborhood? Are they higher? Are they lower?

5. What is your view about the economic trends in you neighborhood? Does it seem to be on the upgrade? If yes, what are the indicators of improvement?
6. How will this property function in the market post opt-out?
7. Is the property still affordable for families/people with vouchers?
8. Could you tell us what proportion of the residents remained at the property after it was taken out of Section 8? Did these residents receive enhanced vouchers to cover their rent payments?
9. In your opinion could residents at this property use a HUD voucher to find a comparable unit in this neighborhood?
10. Is the property still affordable for people without vouchers?
11. Do you think that the owners intend to keep it as an affordable property?
12. Who has moved in since the property opted out?
13. What are their income ranges? What types of households? Do the new residents tend to have the same characteristics as the households who are still there using vouchers or different?
14. Have any new residents with vouchers moved into to property? Are the current rents within the PHA's payment standard? Are there exception payment standards for this neighborhood?

Thank you for all that information. Now, I would like to take a brief tour around the grounds. Please point out any major recent improvements that have been made.

6. Discussion Guide for Property Site Managers of Opt-In Properties

Name of Respondent: ____
Phone Number: ____
Email: ____
Property Name/location: ____
Date of interview: ____
Econometrica/Abt Interviewer: _______________________________________
Site/Location: ____

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Interviewee and Property Characteristics

[Before going onsite, ask the owner or manager to send you occupancy reports that provide this information regarding vacancy rates, waiting lists, occupancy problems.]

1. How long have you managed this property?
2. Do you know if the owners have ever considered taking this property out of Section8? If yes, do you know any of the reasons they chose to keep the property in the program?
3. Have there been any changes in income levels or household types over the past few years, both before and after the owner made the decision to stay in the program?
4. In your opinion could residents at this property use a HUD voucher to find a comparable unit in this neighborhood??

Recent History of the Property

5. Have the owners made any significant upgrades or investments in the property within the last year? If yes, could you tell me what these upgrades were?
6. What are your current rent levels for different size units? Do you think that your rates are "in sync" with others in the neighborhood? Are they higher? Are they lower?
7. What is your view about the economic trends in you neighborhood? Does it seem to be on the upgrade? If yes, what are the indicators of improvement?
8. If this property were taken out of Section 8, could your residents get into a comparable Section 8 property in the neighborhood?

Thank you for all that information. Now, I would like to take a brief tour around the grounds. Please point out any major recent improvements that have been made.

7. Discussion Guide for Expert Informants

Name of Respondent: ____
Phone Number: ____
Email: ____
Position of Respondent: ____
Date of interview: ____
Econometrica/Abt Interviewer: _______________________________________
Phone/onsite? ____

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Interviewee Information

1. Please tell me what your current position is, how long you have been in that position, when and where you become involved with housing in the community.

Policies and Procedures

[There will not be time for many such interviews. While it is good to use them to find out in general how opt-outs are affecting housing affordability in the community, the respondents should be chosen and the interviews focused on finding out 1) why the 4 particular properties in particular neighborhoods opted out or stayed in and 2) what the role of the 4 properties now is in the housing market.]

Community Issues

2. Do the "opt-out" properties represent a trend in your local housing market or are they in some sense outliers?
3. Are there unique characteristics/circumstances of this housing market that influenced the owners of the subject properties to opt-in or opt-out of Section 8?

Affordability Issues

4. How are opt-outs and opt-ins affecting the housing market in your community?
5. Is there a shortage of affordable housing in your community?
6. Do you believe that residents can find affordable housing?
7. What happens to families that cannot absorb the rent increase?
8. How does the community continue preserving affordable housing?
9. Do laws, statutes, zoning incentives, ordinances, policies, and programs, to encourage the creation of new affordable housing or the preserve affordable housing in your community? Are there inclusionary zoning provisions in this area that can help create housing opportunities for people at a variety of income levels?
10. Are public subsidies, such as Tax Exempt Bonds, CDBG funds, HOME funds, Tax Credits, etc. to encourage the development of affordable housing units.