

# New PAB Eligible Uses May Threaten Affordable Housing

FEDERAL POLICY

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**The Infrastructure Investment and Jobs Act (IIJA), the bipartisan bill advancing in Washington, includes two new uses for private activity bonds, which will compete with affordable housing under state volume cap. Since federal tax-exempt private activity bonds are one of the most important financing tools to build and preserve affordable housing, Congress will need to adopt additional legislative changes to offset potentially negative impacts on affordable housing.**

**The Housing Supply Crisis:** New York State and the rest of the nation is facing an affordable housing crisis. At the root of New York's housing crisis is a severe shortage of affordable housing, particularly for low- and very low-income households. Nationally, new housing construction over the past 20 years is 5.5 million units less than long term historical production.<sup>i</sup> <sup>ii</sup> Recent analysis found that the state lacks almost 650,000 units of housing for those households, contributing to soaring rents and a homelessness emergency.<sup>iii</sup>

**Private Activity Bonds (PABs):** Tax-exempt private activity bonds are an important tool to create and preserve affordable housing. The bonds have lower interest rates and automatically generate 4% Low Income Housing Tax Credits, if 50 percent of the project is financed by private activity bonds.<sup>iv</sup> New York State's cap was \$2.1 billion in 2019 and it primarily financed affordable rental housing with \$200 million going towards homeownership in 2018.<sup>v</sup> <sup>vi</sup>

The federal government caps the amount of tax-exempt private activity bonds each state can issue, making the bonds an important but limited resource. There are over a dozen uses that are eligible for federal tax-exempt private activity bonds, including airports, sewage and solid waste facilities, public education facilities and green building projects.<sup>vii</sup> Six of the uses are exempt from the state volume cap and one use – high speed intercity rail facilities – is 75% exempt. In total, states issued \$24 billion in private activity bonds in 2018, with 91 percent of the bonds going to single and multi-family housing.<sup>viii</sup>

Demand for private activity bonds exceeds supply in many states. New York State and 13 other states are using close to or using all of their private activity bond allocations.<sup>ix</sup>

**Expanded Uses for PABs in Infrastructure Bill:** In August, the U.S. Senate passed the [Infrastructure Investment and Jobs Act \(H.R. 3684\)](#), a \$1 trillion bipartisan infrastructure bill. The U.S. House of Representatives has not yet passed the bill. The legislation fails to include affordable housing funding, which is instead found in the separate budget reconciliation bill. However, the infrastructure bill does include provisions that could impact affordable housing production. The legislation adds two new uses that would be eligible for private activity bonds: **broadband projects** and **carbon dioxide capture projects**. Both would be 75 percent exempt from volume cap, with 25% of the project costs counting towards a state's volume cap.<sup>x</sup>

**Adding more eligible uses for private activity bonds without increasing total volume cap or adopting other legislative changes to protect housing, may reduce affordable housing production.** While it is unclear exactly how new uses may impact demand for PABs, experts say 42 million<sup>xi</sup> US households lack broadband access, especially in rural areas, demonstrating significant investment needs. The potential for carbon recapture is enormous as well with a market valued at \$4.4 billion in 2017 and projected to grow to \$14.2 billion by 2025.<sup>xii</sup>

New York and other states need more private activity bonds for housing, not less. Fortunately, the federal government can take steps to mitigate impact on affordable housing production, while expanding eligible PAB uses to include important national priorities relating to broadband infrastructure and reducing carbon emissions.

## Ways to Protect and Expand Affordable Housing Production:

- **Exempt Affordable Housing from Volume Cap:** The easiest way to support robust production of affordable housing while also promoting broadband, carbon capture and other priorities, would be to exempt all or a portion of affordable housing – qualified residential rental projects – from volume cap. The law currently exempts six uses from the volume cap, only some of which have their own separate limitation. In addition, there is existing precedent for partial exemption and the two new uses are also proposed to be 75% exempt. This would allow jurisdictions

to use more tax-exempt bonds and associated 4% Low Income Housing Tax Credits for affordable housing and better meet the housing demand.

- **Lower the 50% Test:** As mentioned above, affordable housing projects qualify for 4% LIHTC if 50% of their project is funded with tax-exempt private activity bonds. However, many projects do not need to finance 50 percent of their project with private activity bonds to make the financing work but have to use that much to generate the tax credits. If projects could generate tax credits with a smaller share of tax-exempt bonds, it would allow the bonds to be more efficient. It would support more projects by freeing up tax-exempt bonds for other projects and generate tax credits, generating more affordable housing each year. The [Affordable Housing Credit Improvement Act \(S. 1136, H.R. 2573\)](#) would lower the threshold to require a minimum of 25% of the project covered by private activity bonds. This change could double housing production with the same amount of bonds in New York City.<sup>xiii</sup> See NYHC impact [analysis](#) of reducing the 50% text.

## Conclusion

While Washington balances priorities for traditional infrastructure and new needs around connectivity and climate change, solutions must not be at the expense of affordable housing, the primary use of PABS for many states. New York and other states across the country desperately need more affordable housing. Further changes are necessary to protect current production levels and expand them to meet the current housing crisis.

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<sup>i</sup> U.S. Housing Market Needs 5.5 Million More Units, Says New Report, Nicole Friedman. Wall Street Journal, June 16, 2021.

<sup>ii</sup> Housing is Critical Infrastructure: Social and Economic Benefits of Building More Housing. Rosen Consulting Group for National Association of Realtors, June 2021. <https://cdn.nar.realtor/sites/default/files/documents/Housing-is-Critical-Infrastructure-Social-and-Economic-Benefits-of-Building-More-Housing-6-15-2021.pdf>

<sup>iii</sup> The Gap: A Shortage of Affordable Rental Homes – New York. NLIHC, 2021. <https://reports.nlihc.org/gap/2019/ny>

<sup>iv</sup> [https://www.novoco.com/sites/default/files/atoms/files/2020\\_novogradac\\_ncsha\\_50\\_test.pdf](https://www.novoco.com/sites/default/files/atoms/files/2020_novogradac_ncsha_50_test.pdf)

<sup>v</sup> 2019 IDB Cap Carryforward Summary. NYS Division of the Budget. <https://www.budget.ny.gov/pubs/supporting/idbcap/2019-idbcap-cf-summary.pdf>

<sup>vi</sup> CDFA Annual Volume Cap Report, 2018. Council of Development Finance Agencies.

[https://www.novoco.com/sites/default/files/atoms/files/cdfa\\_annual\\_bond\\_volume\\_cap\\_2018\\_report\\_102319.pdf](https://www.novoco.com/sites/default/files/atoms/files/cdfa_annual_bond_volume_cap_2018_report_102319.pdf)

<sup>vii</sup> 26 U.S. Code § 142 - Exempt facility bond: <https://www.law.cornell.edu/uscode/text/26/142>

<sup>viii</sup> CDFA Annual Volume Cap Report, Council of Development Finance Agencies. October 2019.

<https://www.cdfa.net/r/VolumeCapReport2018.html>

<sup>ix</sup> Analyzing the impact of Lowering the 50% Test for 4% Tax-Exempt Bond Financed Properties. Novogradac.

[https://www.novoco.com/sites/default/files/atoms/files/analyzing\\_the\\_impact\\_of\\_lowering\\_the\\_50\\_percent\\_test\\_051520.pdf](https://www.novoco.com/sites/default/files/atoms/files/analyzing_the_impact_of_lowering_the_50_percent_test_051520.pdf)

States include: California, Colorado, Connecticut, Kansas, Massachusetts, Minnesota, Nebraska, New Jersey, New Mexico, New York, North Dakota, Tennessee, Washington, and Wisconsin.

<sup>x</sup> H.R.3684 - Infrastructure Investment and Jobs Act: <https://www.congress.gov/bill/117th-congress/house-bill/3684/actions>

<sup>xi</sup> <https://www.bloomberg.com/news/articles/2020-02-19/where-the-u-s-underestimates-the-digital-divide>

<sup>xii</sup> <https://www.marketwatch.com/press-release/carbon-capture-and-sequestration-market-size-to-surpass-us-9107-million-by-2027-2021-07-13>

<sup>xiii</sup> 4 Ways the Affordable Housing Credit Improvement Act Will Help NYC. NYC HDC. May 2021.