

Market Rate Affordable Rental Housing in Arlington County:

**Analysis and Recommendations
Based on a Property Owner Survey**

prepared for

The Alliance for Housing Solutions

by

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OVERVIEW

Study Objective

The Alliance for Housing Solutions (AHS) has contracted with Dr. Lisa A. Fowler of George Mason University to interview rental property owners and managers in Arlington County to assess the state of the affordable rental housing market and to discuss policies that would help owners maintain their properties as affordable. This report includes a discussion of the main findings from the interviews and concludes with a set of policy alternatives based on those interviews, as well as an earlier review of policies designed to preserve affordable rental housing in jurisdictions around the country.

The Alliance for Housing Solutions

The Alliance for Housing Solutions (AHS) is a 501 (c) (3) not-for-profit organization working to increase community knowledge and support for affordable housing through research, education and advocacy.

Introduction

The availability of rental housing that is affordable to low and moderate income households has diminished significantly over the past few years in Arlington County. This loss of affordable rental housing has occurred due to both the demolition of affordable rental properties for development of higher end housing and increases in rents at properties that were once affordable. According to a recent report by the Arlington County Housing Division, between 2000 and 2006, more than 2,400 rental units were converted to condominiums and another 400+ units were demolished, typically to build townhouses. Approximately 25 percent of these units were previously market affordable.¹ In addition, between 2000 and 2005, almost 9,900 rental units became unaffordable to low-to-moderate income households as a result of rent increases. These conversions, demolitions, and rent increases effectively removed more than 52 percent of all market rate affordable rental units from the stock.²

One of the most important sources of affordable housing in the County is market rate affordable rental housing, which can be defined as rental housing that does not make use of any government subsidies but remains affordable to low-to-moderate income households by virtue of the fact that the properties are older and have fewer amenities.

Stemming the loss of additional market rate affordable rental units should be an important part of the County's overall affordable housing strategy. However, the problem can seem daunting, as properties in desirable locations are fetching millions of dollars.³ These recent trends lead to the question: *Is there a future for unsubsidized, market rate affordable rental housing in Arlington?* The situation is not optimistic. As one property owner said, "I see a future where the draw of big bucks will eventually persuade owners (or their offspring) to sell and Arlington will become a place where you have to be really rich in order to live there." Action is needed now before it is too late.

How is Market Rate Affordable Rental Housing Different?

Market rate affordable rental properties pose a different set of challenges than do subsidized rental properties. When a rental unit is built with a subsidy (e.g. tax credit dollars), the property owner is required to keep the units affordable to households with a certain level of income (usually 50 to 60 percent of the area median income) and for a certain period of time (minimum 30 years.) Arlington County has worked diligently to provide incentives to residential developers to include committed affordable units (CAFs) as part of their projects. These CAFs are generally built at least partially with tax credit dollars. There are currently more than 5,700 rental CAFs in the County. Rental CAFs typically serve households with incomes below 60 percent of area median income. Some serve households at up to 80 percent of area median income. CAFs are guaranteed to remain affordable for 30 years or more.

Thus, Arlington County's approach to preserving and encouraging the construction of affordable housing has emphasized long-term affordability. The County has found it difficult to contact small, individual family owners of market rate affordable properties before the sale or consolidation of property. Therefore, the County tends to work with property owners at the time of the sale of

1 Interview with Fran Lunney, Arlington County Department of Community Planning, Housing and Development, 9/7/07.

2 Arlington County. *Issue Brief: Affordable Housing*. July 2006. <<http://www.arlingtonva.us/Departments/CPHD/Documents/6353aff%20hsng%20combined%20issue%20brief%2007-06.pdf>>

3 For example, ABDO Developers recently purchased five lots totaling 1.3 acres in the Fort Myer Heights neighborhood of Arlington County. The small apartment buildings on the property were demolished so that ABDO could build new condominiums. ABDO paid \$22.1 million for the properties, which means the land was valued at about \$8.5 million per acre. The new condominiums, which are nearly complete, will sell for between \$700,000 and \$2 million.



Fillmore Gardens



Magnolia Commons

a property, discussing options with the buyer and offering density bonuses for retaining and/or replacing some affordable housing.

Methodology

The objective of this survey project was to get the perspective from owners of market rate affordable rental properties in Arlington County to help define new policy options to preserve affordable rental housing. Property owners and managers were selected so that a diverse set of the County's market rate affordable rental market was represented.⁴ Properties were identified through a search of the online Arlington Apartment Guide and through discussions with area property owners.⁵ Potential interviewees were identified based on rents that are affordable at about 80 percent or less of area median income.⁶

When possible, interviews were held with owners, but in two cases, interviews were conducted with property managers because owners were not available. A total of 15 owners were contacted and interviews were conducted with seven property owners and managers. Interviews were conducted in person and took between 20 and 40 minutes. The individuals interviewed for this study owned and/or managed a total of about 1,500 market rate affordable rental units in Arlington County. Most also owned and/or managed rental properties in other area jurisdictions.

From the discussions with these property owners/managers, five main themes arose:

1. Some owners of market rate affordable rental properties are *mission driven*.
2. *Control over their property* is of paramount importance.
3. The effect of rising costs depends significantly on the *duration of ownership*.
4. Most projects will need *major renovations* in the near future.
5. Tenants in these properties *may not be low or moderate income*.

1. Some owners of market rate affordable rental properties are mission driven

The property owners interviewed for this research project are business people. Owning and managing rental properties is their livelihood or a part of their livelihood and a key source of support for their families. As one owner said, “[a]s a for-profit developer, it is your neck on the chopping block. It is your money, your bottom line.” Some property owners have held on to their properties, even in the face of astronomically high offers, because the properties provide “good cash flow” and the tax ramifications of selling are too high. Other properties continue to operate as market rate affordable rental properties because they are owned by a partnership of several people, making it difficult to come to a decision about selling.

For some property owners, however, particularly those that have owned properties for 20+ years and/or who grew up in Arlington County, maintaining and managing older buildings to provide housing that is affordable is also a mission. For example, a 2004 *Washington Post* article about Fillmore Garden Apartments highlighted some of the more socially-conscious goals of rental property ownership in Arlington. While Fillmore Gardens has a good location, close to many amenities such as Columbia Pike, County library and playgrounds, the complex “has gained a reputation for affordability.”⁷ Both employees and tenants benefit from the familial atmosphere at the apartment complex. According to the 2004 *Post* article, eight Fillmore Garden employees had a

⁴ See Appendix for a description of properties included in the interviews.

⁵ <http://aptguide.arlingtonva.us/>

⁶ See Appendix for income and rent limits.

⁷ *The Washington Post*, 7/13/04, p. T05.



Allendale Gardens



Wakefield Manor

combined 164 years of service at the apartment complex and at least one 50-year resident was given a year's free rent to mark the occasion.⁸

Many other property owners interviewed said that they keep rents low because they have good tenants that they do not want to lose and they feel they are providing a service to the community. One owner who says “it’s the right thing to do” to keep rents relatively low, works not only with the Section 8 program but also with local community and church groups to help low income renters.

At least one owner interviewed has both a social and architectural interest in preserving his properties. Wakefield Manor, near the Courthouse Metro Station, is a classic example of one of the many World War II era apartment projects built in Arlington County to house new federal workers and soldiers returning from war. Wakefield Manor has been maintained because the owner “likes old buildings” and sees value in preserving architecturally significant properties in the County.

The mission driven, long-standing property owners generally indicated little interest in selling their properties now, though they did indicate there would come a time when they left the business to their children and the decision about whether or not to sell would be up to them. At least two property owners interviewed had recently sold properties in Arlington, taking advantage of lucrative offers, but they have decided not to leave the rental market altogether and retain at least one market rate affordable property in the County.

2. Control over their property is of paramount importance.

Most of the property owners interviewed for this research do not participate in any government subsidy programs. Most have not used tax credit dollars and most do not participate in the federal Section 8 program. While bureaucracy and paperwork is one reason cited for the lack of participation in these types of programs, the sentiment expressed by all of the owners surveyed was that they did not want the government telling them what they could or could not do with their properties. Subsidies or other incentives are often avoided because they come with “strings attached” and “take away the power of owners to run their property.”

Some owners and managers that have properties in other states noted how Virginia is a relatively easy state to operate in because “the rules are clear.” That is, the rules and regulations that guide a property owner’s rights and responsibilities are well established—and very favorable to owners. This environment was highly valued by property owners interviewed.

Rent control was cited as the worst mistake that a government could make by at least two different property owners interviewed. One owner unequivocally stated that rent control takes away an owner’s control and would lead him to immediately sell his property to the highest bidder.

3. The effect of rising costs depends significantly on the duration of ownership.

The two biggest cost increases faced by owners of market rate affordable rental properties are (i) property taxes and (ii) insurance. Other costs mentioned include utilities (gas, electric and oil), maintenance and upgrades (e.g. windows, furnace) and health insurance for employees. In almost all cases, property owners indicated they have paid for these cost increases by raising rents. For many owners, the total amount of rent increases in recent years has gone to meeting increased costs, with no additional profit to the owners. In general, property owners anticipate that rents will increase between three and five percent annually over the next few years.

While vacancy rates are relatively low (between three and six percent), some apartment complexes do

⁸ Ibid.



Calvert Manor



Greenbrier Apartments

experience high turnover, which results in additional costs. One property owner estimated that it can cost \$5,000 per unit to do upgrades upon turnover. When there is an eviction where the tenant leaves the unit in bad shape, cleaning and repair costs can be substantial.

Property owners who have owned their properties for a long time or who have a large real estate portfolio have an easier time responding to cost increases. Some of the property owners interviewed owned their properties outright or had very low mortgages remaining. Owners that have a diverse portfolio of properties, including higher rent properties, also have the cash flow necessary to meet rising costs. The long-term and diversified property owners indicated that they have not put off maintenance or capital improvements because of rising costs and, in fact, did not seem affected by rising costs at all.

However, property taxes were the cost increase that owners were most concerned with. Every property owner stated that they had faced a significant increase in their property taxes in recent years.

4. Most projects will need major renovations in the near future.

Despite most owners indicating an ability to stay current with maintenance, it is likely that most if not all of the properties included in this survey will need major renovations in the not-too-distant future. The average age of properties in the survey is 53 years. Most are two to four story garden style buildings with relatively small units. Most buildings lack central air conditioning and the units themselves tend to have small closets and often lack dishwashers, disposals, and other amenities. Structurally, these buildings are generally sound, but they will need windows replaced and new heating and cooling systems.

Some property owners and managers state that their tenants are “hard on the properties” which accelerates the pace of building decline. Relatively high turnover in some buildings, often with lots of clean up and repairs in between tenants, is costly.

In some cases, buildings can be just too costly to renovate. In order to update systems, interiors and windows, rents would have to increase. However, some older buildings would remain difficult to rent simply because the units are small and lack amenities renters have come to expect. While the property is still income producing, the decision will usually be to just do the basic maintenance and operate it until it becomes unlivable. Thus, while it is a difficult decision to tear down, in some cases that is the only decision that makes sense to a property owner.

5. Tenants in these properties may not be low or moderate income.

The nature of unsubsidized, market rate affordable rental properties means that there are no rules guiding who can rent a particular apartment unit. In most cases, the market rate affordable rental properties have rents that are affordable at 60 or 80 percent of area median income. Some property owners and managers noted that higher income renters tend to be more desirable and are “less hard on the properties.” The unwillingness of most property owners interviewed to participate in the Section 8 program is another indication of attitudes about lower income renters. Thus, all other things equal, property owners and managers would prefer to rent to higher income tenants.

As one property owner stated, many of the people living in market rate affordable rental units are “meaningfully” over the income limits one would think of as limits for affordable housing. These higher income renters choose these properties because they may not want to pay 30 percent of their income for rent because they have other expenses, are saving to buy a home, or simply do not want to pay for amenities that they do not want. Overall, property owners and managers are happy to



Oakland Apartments



Fairfax Drive Apartments

have these higher income tenants and often do not raise rents substantially so that they can keep these good tenants.

Policy Alternatives

Many of the property owners and managers interviewed were directly involved in affordable and rental housing issues in the County, through service on community housing committees and participation in tenant-landlord meetings. Most owners and managers had given some thought to the affordable housing issue in Arlington and the role market rate affordable rental housing plays in meeting the demand for affordable housing. From these interviews, as well as with information from a recent review of policies across the nation to preserve affordable rental housing,⁹ five policy alternatives emerged. Each recommendation is specific to the goal of preserving the stock of *market rate affordable rental* housing in Arlington County.

1. Provide *property tax abatement* for owners of market rate affordable rental properties.
2. Increase opportunities for *density transfers* within a single property or between properties.
3. Require owners to sell to County if the County can *match the privately-offered price*.
4. Advocate to *improve existing programs* (such as Section 8) and *educate property owners* about them.
5. Explore options for *modifications of federal capital gains tax regulations* to encourage subsequent generations to maintain properties as affordable or sell to a non-profit.

Each of these options has drawbacks and no one alternative will solve the problem entirely. Furthermore, these policy alternatives include recommendations that are outside the authority of the County. However, the County can be an advocate for change as it works on the problem of preserving affordable rental housing.

The one overriding element to these policy suggestions is the recommendation that the County increase its efforts to identify at-risk properties and work with current owners to maintain and preserve their affordable units.

1. Property tax abatement for owners of market rate affordable rental properties

In accordance with the Constitution of the Commonwealth of Virginia, all real estate is assessed in a uniform manner. In Arlington County, the Department of Real Estate Assessments, under the authority of the state Constitution and County code, adhere to the following legal requirements when assessing all residential and commercial property in the County:¹⁰

- Real estate assessments are required by law to be at 100 percent of fair market value. The Virginia Supreme Court has provided the following definition of fair market value: The fair market value of a property is the price which it will bring when it is offered for sale by one who desires, but is not obliged, to sell it, and is bought by one who is under no necessity of having it.
- Real property in Arlington County must be assessed annually as of January 1 of the tax year.
- Real estate assessments are also required to be uniform on the same class of property.

⁹ Fowler, Lisa A. 2006. "Policies and Programs to Preserve Affordable Housing: A Review of Incentives and Recommendations for Northern Virginia." Prepared for the Alliance for Housing Solutions.

¹⁰ Arlington County Department of Real Estate Assessments, <<http://www.arlingtonva.us/Departments/Real-Estate/RealEstateAssessmentsTaxYearInfo.aspx>>



Queens Court



Lee-Albemarle
Apartments

- The director of the Department of Real Estate Assessments assesses all real property in Arlington County, except the property of operating railroads, interstate pipelines, and public utilities.

The County’s web site states that “[a]ssessments are made according to accepted methods, techniques, and standards of the real estate appraisal and assessment profession.”¹¹ There are three methods typically used to estimate value:¹²

- Sales Comparison Approach, where an individual property is compared to other similar properties that have recently sold. When using this approach the assessor considers all available market data to arrive at an assessment. Important factors include size, quality, condition, amenities, and time of sale. The sales comparison approach has been called the most “reliable” method of determining value. However, this approach is difficult for multi-family residential properties, a category for which there are relatively few sales.
- Cost Approach, which estimates the value of the land plus the current costs of material and labor needed to replace a building (generally a single family home) with one of similar quality and function. This method is good for appraising newly constructed, special purpose and unique properties.¹³
- Income Approach values the revenue producing *capabilities* of a property (italics added.) This method determines the income, expenses, vacancy rates, and capitalization rates of an income-producing property. A net operating income is capitalized into a value which includes the value of the land (which is a major portion of these types of properties.) The income approach is used to assess commercial properties and residential properties that produce income to the owner.

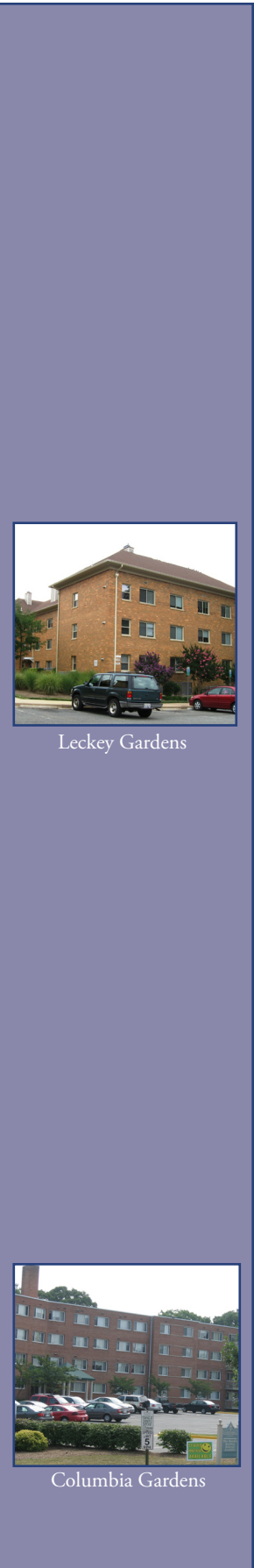
The Income Approach is the method used to assess the value of multi-family rental properties in Arlington County.¹⁴ Properties located in desirable areas that have lower rents are still valued highly because they have the *potential* to produce high income streams. Furthermore, the value of the land, which is driven by strong demand and limited supply, accounts for the majority of the assessment increases. For example, the improvement value of one property included in this analysis declined by 14 percent over the last seven years, while the land value has nearly tripled. This imbalance creates an incentive for the owner to sell.

As required by the Commonwealth of Virginia, the real estate tax rate is the same for commercial and residential properties. In 2007, the tax rate was set by the Arlington County Board to \$0.818 per \$100 of assessed value.

Certain individuals can receive property tax exemptions under the Code of Virginia. Persons who are 65 years old or older or permanently disabled may have real estate taxes on their home exempted or deferred. These individuals must apply for this exemption or deferral. No other exemptions are made.

Non-profit developers of affordable housing have not been able to receive a property tax reduction from the County, although the state allows these subsidized properties to appeal for a reduced assessment. The Arlington Partnership for Affordable Housing (APAH) is currently appealing the tax assessment of one of their properties. The total assessment of APAH’s properties more than doubled between 2005 and 2006.

11 Ibid.
 12 Fairfax County Real Estate Division, <http://www.fairfaxcounty.gov/dta/re_home.htm>
 13 Ibid.
 14 Arlington County Department of Real Estate Assessment.



One policy alternative is to modify the County's real estate assessment process to provide a tax reduction to owners of both subsidized and market rate affordable rental properties. This alternative would reduce the cost burden on owners and make it easier for them to maintain their properties. Under this suggestion, the property owner would pay taxes based on a reduced (i.e. less than 100 percent fair market value) assessment. The property owner would have to file for this reduction in order to certify the property as an eligible affordable rental property. "Affordable" could be defined as a property with either (i) units that have rents that are affordable to households earning 60 (or 80) percent of the area median income or (ii) units that actually *house tenants* that have incomes of 60 (or 80) percent of the area median income. This latter requirement would ensure that not only are the units affordable, but they are being occupied by lower income tenants.

There are several challenges to implementing this type of policy option. First, the Constitution of the Commonwealth of Virginia directly states that all property must be assessed at 100 percent of the fair market value. A change like the one suggested would require a change to the state constitution. One way to get around this issue is to assess the property at 100 percent of fair market value, calculate the reduced tax assessment, and then have the County provide a grant back to the property owner in the amount of the difference. The state has rules about the types of "affordable housing" grants localities can make, so the grant would have to comply with those rules, as well.

Another problem with this policy alternative is the issue of fairness. If market rate affordable rental property owners get a tax break, units that are affordable via a subsidy or units that take Section 8 tenants would also want the same tax advantage. This could create a huge expense for the County in the form of lost tax revenue.

A third problem is the increased paperwork required, both on the part of the property owner and on the part of the County. If the owner is required to determine the income of tenants, there may be other legal issues.

Finally, this option raises the issue of the length of the affordability commitment. In general, property owners would be in favor of this type of policy if it was a year-to-year tax reduction. That is, property owners would have to file annually to classify the units (or a certain share of the units) as affordable. In years when they are determined to be affordable, they would receive the tax abatement. In years when they do not meet the requirements, they would not receive the tax abatement. An annual process allows property owners to maintain control over the operation of the properties, without too much government oversight. However, a year-to-year commitment is at odds with the County's goal of pursuing long-term affordability commitments from property owners and some compromise would have to be reached on length of affordability commitment.

Another tax exemption option is an expansion of the exemption on property improvements. According to the Arlington County Department of Community Planning, Housing and Development, a partial tax exemption currently is available for property owners who do substantial rehabilitation on multi-family rental projects.¹⁵ The County ensures that developers of CAFs are aware of the program. However, this program could be more widely publicized to owners of unsubsidized units and the County could proactively seek out market rate affordable property owners who might be able to take advantage of the program. Working with Code Enforcement staff, who are aware of the condition of many multi-family buildings in the County, would be a good place to start.

Since many market rate affordable properties are going to need substantial renovations in the near future, this could be a good time to explore expanding and publicizing this exemption, both for

15 Arlington County Department of Community Planning, Housing and Development, *Creative Affordable Housing Development Tools*, <<http://www.arlingtonva.us/Departments/CPHD/Documents/4558Aff%20Hsg%20Tools%203%2028%2006.pdf>>

market rate and subsidized rental properties.

2. Increase opportunities for density transfers within a single property or between properties

One alternative to preserve market rate affordable rental properties is for the County to help property owners identify additional density potential on their properties within the County and facilitate the development of that unused density. In some cases, these properties are located in areas where the existing zoning is much lower than the density defined under the County's General Land Use Plan (GLUP.) Through the County's special exception process, owners might be allowed to build on an undeveloped portion of their property at densities much higher than allowed under the current zoning. This could allow owners to build new, market rate properties (with a portion of subsidized affordable units) that would improve their cash flow and make it easier for them to maintain their other projects.

Many owners of market rate affordable rental properties in Arlington County own multiple properties in the County. In some cases, there may be an opportunity for transferring density rights from one parcel to another, which would allow sufficient density for development. The County could help property owners identify these opportunities and facilitate the density transfers.

In February 2006, Arlington County established authority for transfer of development rights (TDRs). Based on this authority, TDRs would be considered by the County for historic preservation, affordable housing, open space, and community facilities. The receiving site must be subject to a site plan and must be located in the Rosslyn-Ballston or Jefferson Davis corridor. The sending site does not have to be part of a site plan and can be located in any part of the County.

The County is currently working on a full ordinance to allow TDRs. Recent TDRs include the shifting of excess density from an urban park to an adjacent portion of the Rosslyn Ridge II site by Arlington Partnership for Affordable Housing (APAH), which resulted in a 238-unit mixed income project with 95 new affordable units. TDR was also used in 1984 to preserve the 41-unit Key Blvd. Apartments, involving a density shift to The Atrium condominium.¹⁶

In a massive undertaking, the Arlington County Board in 2004 approved the transfer of development rights from 28 acres termed the "North Tract," which was acquired by the County, to the "South Tract" in a site plan project in South Arlington from Crystal City to the Alexandria border. This allowed the North Tract area to be preserved for recreational facilities while allowing higher density in the southern portion of the site. Several high rise office and residential buildings are nearing completion in the south tract.

Despite these examples, the County does not yet have a formal ordinance in place to facilitate transfer of development rights from one property within the County to another for a *private* owner. Allowing—and even encouraging this transfer—could promote additional affordable housing, not only by persuading property owners to maintain their market rate affordable properties with the new income stream, but also by requiring that the new development have a certain percentage of units as committed affordable units. At the same time, Arlington County could continue working towards its vision of the County that is outlined by the GLUP.

Some entrepreneurial property owners have identified unused density on their property and have begun to work with the County on development plans. However, in many cases, property owners are not aware of the development possibilities or they are not equipped to take on a large-scale

¹⁶ Arlington County Department of Community Planning, Housing and Development, *Creative Affordable Housing Development Tools*, <http://www.arlingtonva.us/Departments/CPHD/Documents/4558Aff%20Hsg%20Tools%203%2028%2006.pdf>

redevelopment process. In these instances, the County and non-profits could better inform property owners about the assistance available to facilitate the development process.

One of the main obstacles to implementing this alternative is the difficulty the County seems to have in identifying and contacting properties that might be ripe for sale and/or redevelopment. In some cases, the potential return for reaching out to small properties is limited. However, more outreach could be done. Much of the County's current activities related to market rate and other affordable properties happen at the time of the sale, when they work with the new owner to try to save some of the existing affordable units or encourage them to include affordable units in the new project through use of density bonuses. Key to making this strategy work is to be able to identify properties at risk of being lost. The County Housing Division currently maintains a list of market rate affordable rental properties in the County and could use this list to start a dialogue with owners. Planning staff could do an analysis of allowable densities and existing densities on these properties to identify where excess density remains. (According to the Arlington County Department of Community Planning, Housing and Development, this analysis is currently underway.) Then, County staff could approach owners proactively to discuss development opportunities. The County could partner with non-profit or for-profit developers to help property owners without development experience navigate the process.

Another obstacle appears to be the lack of awareness on the part of property owners of the County's TDR policies. Based on this review, it appears as though TDRs are allowed between sites. That is, a property owner who owns two properties in the County might be able to petition the County to transfer rights from one parcel to another and capitalize on that excess density. Most property owners interviewed were not aware of this policy.

The County's current TDR policies limit the development of transferred density to sites with the Rosslyn-Ballston and Jefferson Davis corridors. It would be advisable for the County to encourage TDRs to sites along Columbia Pike, Lee Highway and in the Shirlington/Nauck areas. These are areas that are beginning to get increasing development attention, and are also the locations of many market rate affordable rental properties.

3. Require owner to sell to County if the County can match the privately-offered price

In most cases, when an owner makes the decision to sell his or her property, the most important factor is the price. If the County (in partnership with a non-profit) could match the price offered by a private developer, a market rate affordable rental property owner could be required to sell to the County. In some cases, the owner would actually prefer to sell to the County, knowing the property would be preserved instead of torn down.

There is little precedence in Virginia for giving local government the opportunity to match a private offer. One recent example, however, is the Gunston Hall project in the City of Alexandria. In 2005, the City of Alexandria Housing Development Corp. offered \$12.3 million to buy Gunston Hall, a 68-year old garden apartment building in south Alexandria. This offer matched an offer made by a private developer who planned to demolish the complex and put in luxury townhouses. A judge recently upheld the ruling that the owner of Gunston Hall must sell to the City.¹⁷ The owner plans to appeal but for now the 56-unit project remains saved. The City was able to stop the sale and demolition by classifying the Gunston Hall apartments as historic.

Historic preservation is a technique that also has been used in Arlington County to negotiate the preservation of affordable units.

17 Bahrapour, Tara. "Judge Upholds Offer to Buy Gunston Hall," *The Washington Post* 21 June 2007, VA03.

Other states and localities have “rights of first refusal” laws, including Illinois, Maryland, California, Maine, Texas, Rhode Island, District of Columbia, San Francisco and Portland, Oregon. These policies are designed to create opportunities for tenants, local governments, and/or non-profit organizations to make an offer to purchase a subsidized or assisted multi-family rental property. Property owners are required to notify a specified group of interested parties when they plan to either sell the property or otherwise terminate the subsidy. Generally, the notification requirement is triggered by the intention to sell or dispose of the property or to take other action that would terminate the subsidy. Notification is required anywhere from 90 days to two years prior to the sale, disposition or other action. The right of first refusal can go to the tenants’ association, local or state housing authority, non-profit organizations or some combination of these groups. In all cases, these rights of first refusal policies apply only to federally-subsidized and state-subsidized housing with expiring contracts. However, this option could be expanded to include privately-owned properties.

There are two big challenges to this policy alternative: (i) opposition from property rights advocates and (ii) money. Because Virginia is a Dillon Rule state, localities have very limited powers that are specified explicitly by the state. In real estate, in particular, local jurisdictions are restricted to what the state authorizes to do them. Thus, in general, Arlington County’s hands are tied when it comes to telling property owners what they can do with their property. This includes who they can and cannot sell their property to. If the Gunston Hall case provides any example, it shows that requiring the owner to sell to the City has resulted in years of legal battles. It is very likely that the County would face these challenges, as well, unless it crafted a very strict and specific set of rules regarding sales of these properties and worked closely with the state to ensure it was within its authority. For example, would all property owners be required to sell first to the County? How much notice would the owners have to give the County? Would there be a substantial increase in paperwork or a significant increase in the amount of time to complete the sale? What if the owner disagrees with the proposed use of the property if it is sold to the County?

The second big challenge is money. Even if the County could require owners to sell to it (or a non-profit), generating the resources needed to meet the market price is very difficult. In many cases, the amount would total \$10 million, \$20 million, or more to save one 60-year old property. The Arlington County Affordable Housing Investment Fund is the County’s main program for the financing of affordable housing projects. The fund includes both local and federal money. The County’s fiscal year 2007 budget included \$5.4 million to the fund. Other sources of funding for affordable housing include developer contributions, loan repayments, and Community Development Block Grant (CDBG) funds. However, aside from CDBG money, none of these sources is guaranteed. The County needs to figure out how to generate more *guaranteed* resources for affordable housing before it can compete with private offers.

4. Advocate to improve existing programs (such as Section 8) and educate property owners about them.

One important recommendation that emerged from these discussions is to take a hard look at existing affordable housing programs available in the County to determine how they could be improved *and* how market rate affordable property owners could be better educated about the benefits of program participation.

Two programs that were mentioned by property owners and managers interviewed were the federal Section 8 and affordable housing tax credit programs. Nearly all of the property owners and managers interviewed are currently *not* participating in these programs. Some of them used to participate in Section 8 but have decided to discontinue their participation. The main issue cited is the bureaucracy. To participate in Section 8, not only must the tenant be screened and qualified

but the unit must also be visited and qualified. If there is one thing wrong with the apartment unit, the owner must schedule a follow-up visit by a Section 8 representative which delays renting up of the unit. Another perceived problem cited with Section 8 is the inability to evict a tenant for reasons other than non-payment. Property owners indicated they believe that the rules related to evictions of Section 8 tenants are very strict and in many cases, they cannot evict a Section 8 tenant when they would evict another tenant for the same reason. Finally, property owners are allowed to increase rents only once per year under Section 8. Many market rate affordable rental units are rented month-to-month and owners sometimes increase rents every three or six months.

Property owners who do work with Section 8 believe that the problem of limited participation in Section 8 is due to a lack of knowledge on the part of other property owners. In their opinion, while there are sometimes problems with Section 8 tenants, they are no more prevalent than among other tenants. Section 8 tenants provide a guaranteed source of rent, compared with other tenants who can often be delinquent with rent. Furthermore, participating with Section 8 allows property owners to fulfill a mission of giving back to the community. Despite County efforts to increase landlord participation in Section 8, there remains many misconceptions about the program. Property owners who work successfully with Section 8 could be called upon by the County to share their positive experiences with other property owners.

Because Section 8 is a federally-regulated program, the County probably has little ability to make changes. However, if advocating for change was possible, one suggestion is to make the qualification process easier by simply qualifying the prospective tenant and eliminating the requirement of inspection of each participating unit. Qualified households would be provided a rental voucher and they would be allowed to use the Section 8 money at any apartment they want. They would not be limited to units that were inspected and qualified by the government. Under this process, Section 8 tenants would be subject to the leasing and eviction rules of the apartment complex. Prospective tenants would be able to visit apartments and make their own decision about the suitability of a particular unit.

5. Explore options for modifications of federal capital gains tax regulations to encourage subsequent generations to maintain properties as affordable or sell to a non-profit

One of the biggest challenges to preserving market rate affordable rental housing is figuring out how to coordinate preservation efforts when property is passed down from owner to his or her children. Many of these market rate affordable rental properties have been held by the same owner for years or even decades. In most cases, the properties have no or very little remaining debt. One important reason that current owners do not sell is the capital gain tax they would incur on the profits. For example, if a property owner sold a property for \$20 million that was purchased 20 years ago for \$1 million, that property owner would have to pay taxes on the difference between the amount it sold for and the basis, or what was paid originally. Thus, in this case the owner would be responsible for paying capital gains tax on \$19 million in profits.

However, if the property is inherited, the tax ramifications change significantly. The beneficiary would be responsible only for the capital gains on the difference between the \$20 million sale price and the fair market value at the time of the parent's death. Assuming the fair market value was \$19 million and the property sold for \$20 million, the owner's descendent would be responsible for capital gains tax on only \$1 million.

These IRS rules make it very likely that current property owners will be discouraged from selling, but if they pass the property onto their children, the incentive will be much different. It may be impossible to create incentives for the children to hold onto the property, but it is important to be aware that this transfer will happen over the next decade or two for many market rate affordable rental properties in the County.

APPENDIX

Table 1. 2007 Incomes by Percent of Area Median Income

Household Size	80%	60%	50%
1	\$52,960	\$39,720	\$33,100
2	\$60,480	\$45,360	\$37,800
3	\$68,080	\$51,060	\$42,550
4	\$75,600	\$56,700	\$47,250
5	\$81,680	\$61,260	\$51,050
6	\$87,680	\$65,760	\$54,800

Table 2. 2007 Rents by Percent of Median Income for Committed Affordable Units

Unit Size	80%	60%	50%
Efficiency	\$1,324	\$993	\$827
1	\$1,418	\$1,063	\$886
2	\$1,702	\$1,276	\$1,063
3	\$1,966	\$1,474	\$1,228
4	\$2,192	\$1,644	\$1,370

Source: Arlington County Housing Division.

Interviews with Property Owners/Managers

Elliott Burka

Fillmore Garden Apartments

Monica Bush (manager)

Oakland Apartments

John Fitzgerald (manager/owner)

Allendale Gardens

Upton House

Fairfax Drive Apartments

Eva Garcia (manager)

Magnolia Commons

Columbia Gardens

Greenbrier Apartments

Ralph Johnson

Wakefield Manor

Lee-Albemarle Apartments

11th Street Apartments/Westover

Boulevard Courts

Columbia Courts

Rhodes Street Apartments

Paul Kenschaw

Carydale Enterprises

Rolfe Street Apartments

Heather Garden Apartments

Stan Sloter

Paradigm

Courthouse Crossing

Columbia Grove

Leckey Gardens

Calvert Manor

Buckingham Village

Queens Court

South Ballston Place

Interviews with County Staff

David Cristeal

Fran Lunney

Sarah Pizzo

Arlington County Housing Division