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Affordable Housing Response to Rising Energy Prices

NOTE TO READERS

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States and Local Governments should Include Energy Discussion in HUD Consolidated Plans

Every five years, state and local governments receiving money through the U.S. Department of Housing and Urban Development's (HUD) Community Development Block Grant (CDBG) program and/or HOME Investment Partnership Program must submit a planning document to HUD called a Consolidated Plan and Strategy. In the Consolidated Plan, the jurisdiction must document the affordable housing needs in the jurisdiction and set forth a five-year strategy to address those identified affordable housing needs.

Fisher, Sheehan & Colton (FSC) has submitted comments in six different states this year, on behalf of clients, urging the respective states to include a discussion of energy prices in their Consolidated Plans. In addition, in each state, FSC recommended three specific remedies for the state to include as a "strategy" to combat the adverse impacts that rising energy prices have on affordable housing programs.

The states in which FSC submitted comments included Maine, New Hampshire, Rhode Island, Massachusetts, Pennsylvania and Iowa.

HUD's Policy on Energy and Housing

HUD has an increasingly strong policy promoting an awareness of the impact that energy costs have on the affordability of housing and the need to take proactive steps to address unaffordable home energy bills. In June 2001, HUD adopted announced a policy in testimony before Congress to make "significant progress in conserving energy in housing."

HUD followed that policy statement with specific action-steps. In April 2002, HUD approved a Department-wide Action Plan with 21 items. Action Step 6 of the Energy Action Plan commits HUD to "provide technical assistance to encourage energy efficiency when using HOME and CDBG funds." In addition, HUD began to award Priority rating points for energy efficiency in the FY 2005 SuperNOFA. Energy was also included in HUD's FY 2004-2005 Annual Performance Plans.

Energy Burdens and Affordable Housing

The affordability of housing to low- and moderate-income households is generally determined based on housing cost burdens. It can safely be asserted, without citation of authority, that shelter affordability is generally measured by whether total shelter costs (including utilities[1] amongst other items) exceed 30% of household income. To the extent that a household's shelter costs exceed the 30% burden, the household is over-extended. A household with shelter costs exceeding 50% of income is considered to be extremely over-burdened.

HUD's affordable housing programs tend to address households with somewhat higher incomes than do most low-income energy assistance programs. In HUD programs, a household living at 30% of area median income is considered "very low-income." A household living at 50% of area median income is considered to be "low-income." These multiples of median income tend to be higher than incomes at 100% to 150% of the Federal Poverty Level, which are those households generally covered by low-income energy assistance programs.

Nonetheless, it is difficult for low- and moderate-income households as defined by HUD to maintain an affordable 30% shelter burden given high and increasing energy prices today. FSC found that a two-person household in Iowa living at 30% of area median income paid between 10% and 13% of his/her income for housing (looking at three jurisdictions: Des Moines, Davenport, Sioux City). Households at 50% of median income paid between 6% and 8% income for energy in the same jurisdictions.

Similarly, households in Maine living at 30% of area median income paid between 13% and 16.5% of income for energy (in three jurisdictions: Portland, Bangor, Lewiston-Auburn). Maine households with incomes at 50% of area median paid between 8% and 10% toward energy.

In both states (as well as for each state in which FSC submitted comments), FSC concluded that the data "demonstrates why it is difficult for extremely low-income (30% HUD Area Median Income—HAMFI) and very low-income (50% HAMFI) participants in * * *affordable housing programs to meet a 30% shelter burden, even given their participation in an affordable rental or homeownership program. Households cannot pay up to [13% - 16%] of their income exclusively for their home energy costs (not taking into account water/sewer costs) and expect to keep total shelter costs below 30% of income."

Energy Prices and Affordable Housing

One direct threat to the affordability of housing, FSC told the respective state affordable housing agencies, involves the spiraling price of home heating fuels today. Certainly, FSC noted, high energy prices increase the risk of default on home mortgages.[2]

Each of the six states in which comments were filed had experienced substantial fly-ups in home heating prices. In Iowa, while natural gas prices had increased 70% between 1999 and 2004, propane prices had increased 92%. In Maine, while natural gas prices had increased 90%, fuel

[1] Utilities include energy, as well as water/sewer, but not telephone, cable television or internet access.

[2] One study for the Federal Energy Administration found that in 1974 and 1975, 2.5 percent of HUD mortgages failed because of high energy prices. Metrostudy Corporation (1976). ***An Analysis of the Contribution of Energy Price Changes to HUD-Insured Mortgage Failures***. Federal Energy Administration: Washington D.C.

oil prices had increased 107%. In Rhode Island, while natural gas prices had increased 36%, fuel oil prices had increased 95%. Similar results were found in New Hampshire, Massachusetts and Pennsylvania.

It is not surprising that these price increases adversely affect participants in affordable housing programs. FSC noted in Iowa that:

“These price changes can make dramatic differences in consumer budgets. Assuming normal weather, and an annual natural gas consumption of 100 MCF (80% of which is consumed in the winter heating season), the increase in price from $5.06/MCF to $8.59/MCF will add more than $280 to a consumer’s home heating bill. For a household with an annual income of $20,000, the *increase alone* represents 1.4% of total income.”

FSC continued: “Similarly, assuming an annual consumption of 800 gallons of propane (80% of which is consumed in the winter heating season), the increased price from $0.577 to $1.108 will result in an additional $340 in heating bills. For a household with an income of $20,000, simply the amount of *increase* in propane prices represents 1.7% of income.”

Looking at fuel oil price increases in Maine, FSC reported that, “assuming an annual consumption of 800 gallons of fuel oil (80% of which is consumed in the winter heating season), the increased price from $0.758 to $1.572 will result in an additional $520 in heating bills. For a household with an income of $20,000, simply the amount of *increase* in fuel oil prices represents 2.6% of income.”

Energy Bills and Affordable Housing

While the discussion above focuses on prices, home energy bills are also driven by weather. Extremely cold weather, matched with today’s increasing prices, presents real dangers to participants in affordable housing programs. As FSC noted for Iowa: “Given current natural gas prices, an extremely cold winter could pose substantial financial risks from the perspective of the residents of Iowa’s affordable housing. If the winter weather experienced in 2000/2001 had again been experienced at 2003/2004 prices, annual natural gas bills would have* * *reached $950. Unlike 2000/2001, however, when natural gas prices were expected to come back down (and did, in fact, do so), natural gas prices today are expected to remain high for the foreseeable future.”

Energy and Affordable Housing Production

Quite aside from the impact that increasing energy prices/bills/burdens have on low-income households is the impact that those increasing energy prices/bills have on the affordable housing programs supported by HOME and/or CDBG funds. The increase in prices not only makes “affordable housing” less affordable, but it makes it less possible to produce affordable housing units with which to begin.

FSC cited one developer description of the impacts of energy price increases in California:

“Because publicly funded low-income housing operates with legal affordability restrictions, the combination of past and anticipated utility rate hikes is dramatically limiting borrowing capacity.* * *[W]ith increasing utility rates, either tenants can pay less rent or property owners have to pay higher energy costs. Either way, net operating income declines. As a consequence, developments can afford to support less debt financing, creating a gap in the development budget .* * *[O]n a statewide level [in California], this situation is increasing the amount of scarce public funding required per project, thereby reducing the total number of affordable units that can be built.”[3]

The statement made by Mr. Herald and Mr. Shoemaker is a truism, FSC said, which is equally

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[3] Mike Herald and Doug Shoemaker, “How the Energy Crisis Affects Affordable Housing: An Overview of the Problem,” ***Property Compliance Report*** (July 2001).

applicable to other states. "[W]ith increasing utility rates, either tenants can pay less rent or property owners have to pay higher energy costs. Either way, net operating income declines." Accordingly, the total number of affordable units that can be built decreases.

FSC concluded: "As is thus evident, the proposals advanced below are not simply "energy affordability" proposals. They are also a necessary response by [each state's] affordable housing agencies, acting in their capacity as producers of affordable housing units. The proposals are, in other words, in the enlightened self-interest of [the state's] affordable housing community."

Energy in Consolidated Plans

Given the emphasis of HUD's Energy Action Plan on the promotion of energy efficiency in affordable housing developed through HUD programs (such as HOME and CDBG), and given the tremendous adverse impacts that unaffordable home energy has on the residents of affordable housing, the energy data presented above should be used as a direct input into state Consolidated Plans. Based on the above information, FSC requested, on behalf of its clients, that the development of affordable housing in each of the six states (including, as appropriate, both rental and homeownership units) using funds subject to the Consolidated Plan be made subject to the following three stipulations:

Homeownership and rental units developed either as new construction or substantial rehab by grantees or participating jurisdictions (PJs) should be developed to Energy Star standards. Energy Star is a system for achieving and verifying a certain level of performance with respect to energy efficiency. An Energy Star home is at least 30% more energy efficient than a comparable home built to meet the 1993 Model Energy Code (MEC). As HUD has noted, these savings will increase as the cost of energy continues to rise.

HUD has recommended that all grantees and participating jurisdictions (PJs) incorporate the following language into any Request for Proposals (RFP) or procurement process: "All new buildings and gut rehab shall be designed to meet the National Energy Five Star efficiency performance standard of 86. All procedures used for this rating (86) shall comply with National Home Energy Rating System guidelines."

FSC requested that each state include such a commitment in its Consolidated Plan.

Programs providing first time home buyer assistance should promote Energy Efficient Mortgages (EEMs) as a priority loan product. The Consolidated Plan should commit the state to entering into an agreement with local Home Energy Raters to provide Home Energy Ratings to each first time home buyer receiving state affordable housing assistance.

HUD lists in Action Step 9 of its Energy Action Plan to "feature the Energy Efficient Mortgage (EEM) as a priority loan product." As HUD notes, "the EEM is an important, but underutilized, vehicle for financing energy efficiency in older homes."

Under an EEM, home buyers may borrow a minimum of $4,000 and a maximum of five percent (up to $8,000) of the home's appraised value to finance energy efficiency improvements at the time of purchase. The decreased energy bills associated with the efficiency improvements more than offset increased debt service, yielding positive cash flows from the beginning of the mortgage. FHA reports that it insures 30,000 EEMs each year.

FSC requested that each state's Consolidated Plan commit the state to promoting Energy Efficient Mortgages (EEMs) as a priority loan product for first time home buyers assisted with public funds subject to the jurisdiction of the agency submitting the Consolidated Plan and enter into the necessary agreements to allow for Home Energy Ratings to be performed for first time home purchases assisted with public funds.

All grantees or participating jurisdictions developing affordable rental housing subject to utility allowances administered by local Public Housing Authorities will certify that they have in place adequate processes to ensure that the PHA has complied with HUD regulations requiring timely adjustments to utility allowances in response to changing home energy prices. Under HUD regulations, "a PHA must review its schedule of utility allowances each year, and must revise its allowance for a utility category if there has been a change of 10 percent or more in the utility rate since the last time the utility allowance schedule was revised. The PHA must maintain information supporting its annual review of utility allowances and any revisions made in its utility allowance schedule." 24 C.F.R. §982.517(c)(1) (2004).

In addition, HUD's Public Housing Occupancy Guidebook (revised June 2003) states that: "PHAs are required to revise their schedule of allowances before the end of the year if there is a change in the utility rate of 10 percent or more from the rate on which the allowance was based. A PHA would then be required to readjust the resident payment retroactive to the first day of the month following the month in which the last rate change taken into account became effective."

These regulations can substantively affect tenants of units developed with HOME and/or CDBG dollars. For example, pursuant to federal regulations (24 C.F.R. §92.252), affordable rental housing developed with federal HOME funds is to be provided a utility allowance that mirrors the utility allowances of the public housing authority (PHA) in which the HOME-supported housing is located. So, too, are affordable housing units developed under the Low-Income Housing Tax Credit (LIHTC) to have utility allowances that reflect the local PHA's utility allowances.

Each state's Consolidated Plan should explicitly state its expectation that PHAs will be diligent in their compliance with utility allowance regulations in light of rapidly increasing energy costs and that the state's grantees/PJs relying on PHA utility allowances will be diligent in ensuring that utility allowances are adjusted as required by federal law.

Local Consolidated Plans

A commitment to build federally-assisted affordable housing units to Energy Star standards can be obtained at the local level (as well as the state level). When Belmont (MA) developed its Consolidated Plan and Strategy this year, it included the following as its discussion of an affordable energy strategy:

"Belmont commits that all homeownership and rental units developed either as new construction or substantial rehab by or on behalf of the Town (including the Housing Trust) will be developed to Energy Star standards. Energy Star is a system for achieving and verifying a certain level of performance with respect to energy efficiency. An Energy Star home is at least 30% more energy efficient than a comparable home built to meet the 1993 Model Energy Code (MEC). These savings will increase as the cost of energy continues to rise."

Belmont's Consolidated Plan continued on to state: "HUD has recommended that all grantees and participating jurisdictions incorporate the following language into any Request for Proposals (RFP) or procurement process involving HOME and/or CDBG funds: 'All new buildings and gut rehab shall be designed to meet the National Energy Five Star efficiency performance standard of 86. All procedures used for this rating (86) shall comply with National Home Energy Rating System guidelines.' Belmont agrees to incorporate this language in any future affordable housing RFP or procurement process."

Finally, Belmont's Consolidated Plan stated: "In addition to units developed under the auspices of the Town, Belmont will encourage, or to the maximum extent practicable require, affordable housing units developed pursuant to the Town's Inclusionary Housing zoning by-law, or Comprehensive Permits [Chapter 40B], to be built to Energy Star standards as well."

Availability of Materials

FSC's complete set of comments presented to any or all of the six states (Maine, New Hampshire, Massachusetts, Rhode Island, Pennsylvania, Iowa), including all data tables, can be obtained by sending a request to:

roger@fsconline.com

Belmont's Consolidated Plan can be obtained in the same manner.

Fisher, Sheehan and Colton, Public Finance and General Economics (FSC) is a research and consulting firm with offices in Belmont (MA), Scappoose (OR), and Iowa City (IA).

FSC specializes in providing economic, financial and regulatory consulting. The areas in which *FSC* has worked include infrastructure financing, public enterprise planning and development, natural resource economics, community economic development, telecommunications, public sector labor economics, planning and zoning, regulatory economics, energy law and economics, fair housing, and public welfare policy.