Housing Bonds

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Administering Agency: U.S. Department of the Treasury
Year program started: 1954
Number of households served: In 2012, 36,738 with Mortgage Revenue Bonds (MRBs), 5,028 with Mortgage Credit Certificates (MCCs), and 25,740 with multifamily bonds
Population targeted: low and moderate income homebuyers
See also: *Low Income Housing Tax Credits, HOME Investment Partnerships Program*

Housing bonds are used to finance low-interest mortgages for low and moderate income homebuyers, as well as for the acquisition, construction, and rehabilitation of multifamily housing for low income renters. Investors purchase housing bonds at low interest rates because the income from them is tax-free. The interest savings made possible by the tax exemption is passed on to homebuyers and renters in reduced housing costs.

HISTORY

Private activity bonds (PABs) were established under the Tax Code of 1954. These bonds were known as Industrial Development Bonds until the Tax Reform Act of 1986 and other legislation changed their name.

PROGRAM SUMMARY

Private activity bonds, a category that includes housing bonds, are distinct from other tax-exempt bonds because they are issued for private activities as opposed to governmental activities. The private activities must fulfill public purposes, and each private activity bond issuer must hold public hearings to demonstrate such public purposes. PABs are tax-exempt for the purchaser and are issued by state and local governments to support the stated public purpose. Purchasers, or investors, of PABs can include individuals and corporations. In addition to housing, PABs can be issued for other public purposes that include student loans, infrastructure, and redevelopment activities.

State and local housing finance agencies (HFAs) have authority under the Internal Revenue Code to issue housing bonds to support affordable housing activities in their states. Issuing bonds is a way for HFAs to access private financing. HFAs sell the tax-exempt bonds to individual and corporate investors, who are willing to purchase bonds paying lower than market interest rates because of the bonds' tax-exempt status. This interest savings is passed on through private lenders to support housing purchase and development.

There are two main types of housing bonds: Mortgage Revenue Bonds (MRBs), which finance single-family home purchases for qualified low income homebuyers; and, multifamily housing bonds, which finance the acquisition, construction, and rehabilitation of multifamily developments for low income renters.

Mortgage Revenue Bonds. Proceeds from MRBs finance discount mortgages to support the purchase of single-family homes. By lowering the interest rate, MRBs make homeownership affordable for families who would not be able to meet mortgage payments on a conventional loan. Congress limits MRB mortgages to first-time homebuyers who earn no more than the greater of area or statewide median income. Families of three or more can earn up to 115% of the greater of area or statewide median income. Congress also limits the price of homes purchased with MRB mortgages to 90% of the average area purchase price.

HFAs also use their MRB authority to issue Mortgage Credit Certificates (MCCs), which provide a nonrefundable federal income tax credit for part of the mortgage interest qualified homebuyers pay each year. The MCC program is a flexible subsidy source which can be adjusted depending on the incomes of different homebuyers, and provides a relatively constant level of benefit to first-time homebuyers regardless of the spread between market and MRB rates.

Interested borrowers should contact their state or local HFA for information on obtaining an MRB loan or MCC.

Multifamily bonds. Multifamily bonds provide funding for multifamily housing development that reaches income groups the market might not otherwise serve.

Multifamily housing bonds finance the acquisition, construction, or rehabilitation of affordable rental housing. Multifamily housing developments with bond financing must set aside at least 40% of their apartments for families with income of 60% of area median income (AMI) or less, or 20% for families with income of 50% of AMI or less. The income-restricted apartments financed by those bonds must remain affordable for at least 15 years.

States increasingly combine multifamily bonds with other resources, such as Low Income Housing Tax Credits (LIHTC) and HOME Investment Partnerships (HOME) program funds, to serve even lower income families for longer periods of time than the law requires. Furthermore, many multifamily bonds finance special needs housing, such as housing for formerly homeless people, transitional housing, senior housing, assisted living housing, housing for persons with disabilities, housing for persons with AIDS, migrant worker housing, and rural housing.

ISSUE SUMMARY

In 2012, the most recent year for which data are available, state HFAs used MRBs to provide $4.6 billion to support the purchase of 36,738 homes nationwide. Some bond issuance was used to raise proceeds that were escrowed for use in future years, and to refund prior-year bonds. HFAs also issued 5,028 MCCs in 2012, an increase of over 1,000 from 2011. States issued over $3.02 billion in multifamily bonds, and those bonds financed 25,740 affordable apartments in 2012.

Housing bonds have been an unqualified success in providing lower income Americans a unique and otherwise unavailable chance to own a decent and affordable home and to access quality rental opportunities. Using MRBs, HFAs have made homeownership possible for more than 3 million low and moderate income families. They help another approximately 100,000 families buy their first homes with MRB mortgages in a typical year. In 2012, 79% of MRB borrowers earned less than the area median income. The median MRB borrower income was $46,444, 90% of the national median income.

HFAs have also provided nearly 175,000 lower and moderate income homeowners with critical tax relief through the MCC program. Thirty-eight percent of all MCC borrowers in 2012 earned less than 80% of the area median income.

HFAs have financed an additional 1 million affordable rental apartments with Multifamily Bonds. About 40% of all annual LIHTC rental home production includes Housing Bond financing. HFAs have used the LIHTC to produce more than 2.5 million rental apartments for families earning 60% of AMI or less. They add another 100,000 LIHTC apartments every year.

FUNDING

By law, the annual issuance of PABs, including MRBs and multifamily bonds, is capped based on population and indexed to inflation. The 2014 cap is $100 per capita, with a minimum of $296,830,000 in private activity bonding authority allowed each state.

FORECAST FOR 2014

As Congress continues to consider comprehensive tax reform, the tax exemption for housing bonds, and all municipal bonds, may face its biggest threat since Congress last considered tax reform in 1986.

Throughout the last year, Representative Dave Camp (R-MI), Chair of the House Ways and Means Committee, and Senator Max Baucus (D-MT), the former Chair of the Senate Finance Committee, held a series of hearings examining the tax code and exploring options for reform. Both have expressed support for adopting reform legislation that would substantially lower marginal tax rates, which would require them to eliminate and scale back many tax credits and deductions. Tax reform could include eliminating PABs or limiting the ability of taxpayers to deduct from their income interest earned on municipal bonds.

On February 26, 2014, Camp released his discussion draft of legislation to reform the tax code. The discussion draft proposes to terminate PABs by making interest on PABs issued after 2014 taxable. Camp's draft would also prohibit borrowers from using MCCs issued after 2014 to claim a federal tax credit.

President Obama has several times advanced a proposal to cap the value of income deductions and exemptions for high income taxpayers by limiting the tax value of those deductions and exemptions to 28%. This proposal was included in the President's fiscal year (FY) 2015 Budget request. In addition, the President's National Commission on Fiscal Responsibility and Reform proposed eliminating PABs in its December 2010 report.

Eliminating or capping the tax exemption for municipal bonds would have a significant negative impact on municipal bond investment, directly increasing borrowing costs for HFAs and detracting from their ability to provide affordable housing opportunities to lower income and Americans with special needs. It is estimated that the President's proposal would cause issuers to pay yields of up to half a percent higher to continue attracting investors, resulting in an additional $10 billion annually in debt payments. The ultimate impact, however, would likely fall not on bond issuers and investors but on the bond programs' ultimate beneficiaries, including homebuyers and renters, who would bear the cost of higher interest rates demanded by investors. Further, lower and middle income taxpayers could face increases in taxes if state and local governments are forced to increase revenue to cover higher borrowing costs.

WHAT TO SAY TO LEGISLATORS

Advocates should tell legislators to preserve the tax exemption for housing bonds and other municipal bonds.

Advocates should ask legislators to express their support for the tax exemption for all municipal and private activity bonds, including housing bonds, directly to the leaders of the Senate Finance Committee or House Ways and Means Committee.

Advocates should speak with staff in their Members' offices responsible for housing or tax policy and deliver the message that support is needed for housing bonds in any tax reform or deficit reduction proposal.

Specifically, lawmakers should:

- Preserve the tax exemption for municipal and housing bonds.
- Maintain and strengthen the Mortgage Credit Certificate program.
- Increase the Mortgage Revenue Bond home improvement loan limit by an amount at least adequate to reflect the rise in construction costs since it was first established, and index it for construction cost inflation annually thereafter.

FOR MORE INFORMATION

National Council of State Housing Agencies, 202-624-7710, www.ncsha.org