House taxwriters offer conflicting policy prescriptions for bringing down housing costs

Debate on the role of tax policy in promoting housing affordability fell largely along party lines during a July 13 House Ways and Means Committee hearing focused on "profits, disinvestments, and the American housing crisis."

The panel's Democrats and their invited witnesses touted specific incentives in the House-passed Build Back Better Act that they contended would make rental housing and home ownership more affordable for low- and moderate-income individuals. Republicans, for their part, called for a more limited government role in the housing market and argued that, taken as a whole, the tax-increase and spending provisions in the Build Back Better legislation approved in the House (and currently stalled in the Senate) would only fuel inflation and drive up housing costs for individuals at all income levels. (See separate coverage in this issue for details on the status of Senate negotiations on a Build Back Better package.)

Democrats promote Build Back Better incentives

Democrats generally focused their tax policy discussion on two provisions in the Build Back Better Act—one that would expand and enhance the current-law low-income housing tax credit (LIHTC) and one that would create a new credit to encourage developers to rehabilitate certain abandoned or distressed single-family homes. (A detailed discussion of these and other tax provisions in the House-approved measure is available from Deloitte Tax LLP. A description of all the current-law tax incentives related to residential real estate is available from the Joint Committee on Taxation staff.)
URL: https://www2.deloitte.com/content/dam/Deloitte/us/Documents/Tax/us-tax-provisions-in-the-build-back-better-act.pdf
URL: https://www.jct.gov/publications/2022/jcx-15-22/

Low-income housing tax credit: At a high level, the House-passed Build Back Better legislation would modify the existing LIHTC by increasing state allocations of the 9 percent credit, temporarily reducing certain tax-exempt bond financing requirements, providing a basis boost for certain credit-eligible projects serving extremely low-income households, and repealing the qualified contract exception for buildings receiving allocations.

Ways and Means Democrat Bill Pascrell of New Jersey called the credit "one of our best affordability tools" but added that Congress "can make it much better." Committee Chairman Richard Neal, D-Mass., and other Democrats on the panel noted that the credit has played a key role in redeveloping certain areas in their respective districts.

One of the Democrats' invited witnesses, Audra Hamernik of Nevada HAND (a nonprofit organization focused on financing, developing, constructing, and managing affordable apartment communities) told the panel in her opening statement that the LIHTC is the "primary tool" for creating and preserving affordable housing and that LIHTC-funded projects create jobs and generate revenue for local governments.

Responding to a question from Rep. Brad Schneider, D-Ill., Hamernik explained that the credit is vital in attracting private investment in affordable housing projects, which typically offer below-market rents. But in an exchange with Rep. Suzan DelBene, D-Wash., Hamernik said that the credit program as it currently exists is "oversubscribed" and that agencies seeking awards under the program are operating in a "fiercely competitive" environment. She also noted in response to a question from Rep. Don Beyer, D-Va., that expanding the credit would increase the supply of affordable housing units and ease the competitive pressures that are contributing to spikes in rental prices generally.

Neighborhood Homes Credit: The House-passed Build Back Better legislation also would establish a new Neighborhood Homes Credit in section 42A to encourage the rehabilitation of deteriorated homes in economically distressed neighborhoods. (The credit was originally introduced in 2021 in free-standing legislation known as the Neighborhood Homes Investment Act, or "NHIA.") States would receive NHIA tax credit authority and administer and allocate credits on a competitive basis similar to the manner that states allocate low-income housing credits.

The NHIA tax credits are intended to cover the gap between development costs and sales prices after applying certain limits, including a cap of up to 35 percent of eligible development costs. Abandoned homes that have been rehabilitated must be sold to an owner-occupant for investors to receive the credits and home owners must be below certain income limitations. Sales prices are capped and qualifying neighborhoods must have elevated poverty rates, lower incomes, and modest home values. Special rules would apply to rehabilitation projects undertaken when homes are already owner-occupied before and during the rehabilitation process.

Democratic taxwriter Brian Higgins of New York, who introduced the NHIA in 2021, asked witness Akilah Watkins to discuss how the credit provides home ownership opportunities for low-income individuals.

Watkins, who heads the Center for Community Progress, a nonprofit housing advocacy organization based in Flint, Mich., explained that the credit would provide incentives for developers to rehabilitate neglected and abandoned properties in low-income communities and includes safeguards to ensure that the incentive would be available only after a transaction is complete—that is, after a developer provides a capital investment and completes work on a property and the property is sold to a qualified buyer.

In an exchange with Democratic taxwriter Gwen Moore of Wisconsin, Watkins noted that the credit is also available to developers who work on owner-occupied properties, a feature that promotes neighborhood stability by enabling individuals who live in aging properties but lack the equity to pay for the cost of needed upgrades to remain in their homes.

Another witness, Christopher Herbert of the Joint Center for Housing Studies at Harvard University, explained in response to a question from Del. Stacey Plaskett, D-V.I., that the NHIA would attract capital to help close the gap that occurs when the cost of acquiring and renovating a property exceeds the property's likely post-renovation sales price. Herbert cited the gap as an example of a situation in which "government intervention is necessary because market forces won't turn [it] around."

Republicans cite inflationary concerns

For their part, Republicans on the panel did not engage in extended discussions of the specific real estate-focused incentives in the House-approved Build Back Better legislation, although there were two notable exceptions. Rep. Tom Rice, R-S.C., commented during an exchange with witness Audra Hamernik that the federal government already provides substantial support for low-income housing developers through the LIHTC and questioned the need for it to provide more. For his part, Rep. Mike Kelly, R-Pa., expressed support for the Neighborhood Homes Credit, calling it an example of what the government can do "when it gets out of the way and lets private investors do what they do best, and that's picking good investments to invest their money in." (Kelly co-sponsored the Neighborhood Homes Investment Act with Democrat Brian Higgins, although he joined the rest of the House Republican Conference in voting against the larger Build Back Better Act, which includes the Neighborhood Homes Credit, when it came to the chamber floor last November.)

Otherwise, Republican taxwriters advanced a more general argument that proposed spending programs and revenue-raising provisions in the Build Back Better legislation writ large would exacerbate the recent rise in inflation and continue to drive up prices across all sectors of the economy, including housing.

" . . . [W]hen this committee marked up the Build Back Better bill, I and my Republican colleagues expressed our deep-seated concerns that the White House was spending so much to kill so many American jobs," ranking member Kevin Brady, R-Texas, said in his opening statement. "We warned that under that bill, inflation would spin out of control, and would raise taxes on the middle class and small businesses. Now, we hear rumors of a "slimmed-down" version of this bill and we still see over a trillion dollars of tax increases that will drive prices higher."

Net investment income tax: Several Republicans on the panel singled out a possible expansion of the 3.8 percent net investment income tax as something that would be particularly detrimental to the housing sector if it were to become law. The House-passed Build Back Better legislation generally would expand that tax to include, in addition to all investment income, all trade or business income for individuals with more than $500,000 in modified adjusted gross income (for joint filers), $250,000 (married filing separately), or $400,000 (all other individual taxpayers). A similar provision reportedly was slated for inclusion in a narrower Senate alternative package being negotiated by Senate Majority Leader Charles Schumer, D-N.Y., and Sen. Joe Manchin, D-W. Va., but negotiations over that emerging package abruptly broke down on July 14.

House taxwriter Adrian Smith, R-Neb., asked witness Edward J. Pinto of the American Enterprise Institute Housing Center about the possible effects of such a proposal on new home prices.

Pinto replied that any provision that increases marginal tax rates would be "counterproductive," especially for small businesses. This particular provision, he said, would hit home builders and contractors and would "decimate" the housing industry.

In a similar exchange with Rep. Gregory Murphy, R-N.C., Pinto contended that the provision would lead to increases in construction costs that would in turn drive up rental prices as well as the purchase price of new homes.

Pinto characterized the proposal as “going in the wrong direction.”

Opportunity Zones: A few Republicans argued in general terms that Congress could more effectively address the nation’s current economic concerns by focusing on Trump-era tax policies. Pennsylvania Republican Mike Kelly specifically touted Opportunity Zone program, enacted in the Tax Cuts and Jobs Act of 2017 (P.L. 115-97), which provides tax relief on capital gains rolled over into investments in designated geographic areas.

Democratic taxwriter Ron Kind of Wisconsin noted that the program has had some success in his district and asked Akilah Watkins of the Center for Community Progress whether the incentive would be effective in boosting the affordable housing stock.

Watkins replied that Opportunity Zones tend to work best in communities that are “on the cusp” of redeveloping and need an additional infusion of cash, but they are less effective in areas that are “persistently poor.” Those communities, she said, “need a different set of tools”—including government subsidies—because the profit margins otherwise are unlikely to attract significant private investment.

— Michael DeHoff
Tax Policy Group
Deloitte Tax LLP