Reprinted from:

The

Multifamily Advisor

National Housing & Rehabilitation Association Fall 1997

Assisted Living Facilities Offer Opportunities But Require Careful Planning, Speakers Say

Growth in the elderly population and political pressure to reduce costs of subsidizing their care are fostering greater opportunities for development of assisted living facilities affordable to low-income residents.

At the same time, states are lowering regulatory barriers that previously left assisted living projects in a gray area between conventional elderly rental properties and licensed nursing homes, making it easier now to utilize low-income housing tax credits for such properties.

"Roughly two-thirds of the market cannot afford the type of assisted living facilities that have been built on a wide scale today. That creates the demand," said attorney David Abromowitz, of Goulston & Storrs, P.C., Boston, MA.

Abromowitz was one of four speakers on a panel about assisted living and elderly housing at NH&RA's 1997 Summer Institute in Beaver Creek, CO.

Definition of Assisted Living

Defining the product, Abromowitz noted: "Assisted living is a mix of rental housing and health care. The balance of that mix is what raises a lot of (housing tax credit) issues that just don't have answers."

Assisted living facilities offer private living quarters and basic personal services — meals, housekeeping, laundry, etc. — in exchange for a standard monthly payment. Residents also can have an option to pay for additional services such as transportation, physical therapy, medical services, or help with dressing, bathing, and medication.

Syndicator Bernie Husser, of First Financial Management Corp., Boston, MA, said the target market for assisted living facilities is generally individuals 75 to 85 years old. Most are single, and they are primarily female.

Abromowitz said assisted living residents typically pay 75 percent or more of their income for housing and services. The level is high because residents usually have most of their needs fulfilled by services provided through the property.

The speakers indicated that demographics and other trends are creating greater demand for assisted living. The 1990 census, Abromowitz said, identified 30 million Americans 65 or older, including 4 million over 85.

Meanwhile, federal and state agencies see assisted living as a less expensive alternative to nursing homes. Federal and state governments are less willing to subsidize – through Medicare, Medicaid, and other programs – high-cost nursing home care for individuals who don't need such a high level of services. Studies have shown that many seniors don't need the care level of nursing homes. At the same time, though, many are physically unable to live alone in their house or apartment.

Said Abromowitz: "As people begin to live longer, aging in place appears as a good option to staying in their homes. But as people get older, they get frail and need assistance. And frankly the children of those people...are not really willing, able, or close enough to provide the kind of assistance they need. Assisted living offers them an option."

Abromowitz said the current opportunity is for development of assisted living facilities affordable to lower-income Americans.

State Statutes, Credit Rules

The speakers indicated that structuring affordable assisted living projects can be tricky because of the complications posed by housing tax credit rules, the need to find ways to reduce or subsidize costs, and the special management skills needed to assure a successful project.

Abromowitz suggested that more states have adopted statutes and regulations clarifying the status of assisted living facilities, thereby making it more certain for developers to proceed. He said until a few years ago many states didn't have a law defining assisted living. The consequence was that in some such states, new elderly housing projects providing services had to be licensed as a nursing home or fall under some other heavily regulated area.

He noted the regulatory uncertainties about as-

(Continued on page 4)

Assisted Living Facilities

(Continued from page 3)

sisted living facilities are now gone in large measure. But Abromowitz added that state statutes governing assisted living facilities vary widely. He said in some states, assisted living is just a certification process relating to the standard of the housing. In other states, such as New Jersey, assisted living is much more regulated, with greater emphasis on nursing care and other services.

State requirements for assisted living facilities are critical because unfavorable standards may jeopardize the ability of a property to qualify for housing tax credits.

Under federal tax rules, units must be residential rental units to qualify for housing tax credits. Accordingly, credits aren't available for nursing homes, lifecare facilities, or retirement homes providing significant services other than housing. As a result, one issue with assisted living facilities is to avoid having a level of medical care that rises to the level that would disqualify the project for housing tax credits.

In addition, credits are limited to residential rental units that are rent-restricted throughout the housing tax credit compliance period. To be rent-restricted, the gross rent charged for a unit can't exceed 30 percent of the maximum income for a qualified low-income household (50 percent or 60 percent of area median income).

In general, gross rent includes the rent charged for the unit plus fees for additional services that aren't optional (i.e., are mandatory). Accordingly, Abromowitz noted that the services offered must be optional to qualify for housing credits. To be prudent, he advised using lease agreements with two parts: one component imposing just a rental charge, and the second relating to the services.

He said there is only a small risk that new residents moving into an assisted living facility will decline to sign up for the services.

The speakers also said that assisted living facilities are faring better now under state low-income housing tax credit programs, even receiving preference in funding cycles in some cases. For instance, Husser noted that in one 1997 application cycle in Massachusetts, 3 of the 16 projects awarded housing tax credits were assisted living facilities.

Finding Other Subsidies

Sponsors of assisted living facilities with low-income tenants will need to find subsidies or lower-cost financing to help offset the losses on the services provided to such residents.

CPA John Mackey, of Ziner & Company, P.C. in Boston, urged developers to determine if the state where they might build an assisted living project has any subsidy programs like adult foster care, or whether the state instead hopes the sponsor will get tax-exempt financing and subsidize costs for the low-income residents with service payments from the market-rate tenants. The speakers indicated that the services rendered can be quite profitable.

Mackey warned developers to be careful if they plan to rent more than 20 percent of the units in a project to low-income residents. In such projects, he said sponsors should make sure their service component won't "blow up" if any state reimbursement payments are ended or reduced.

Abromowitz said the two most common types of assisted living facilities he has seen are so-called "80/20" deals and properties sponsored by mission-oriented nursing home providers.

80/20 projects are developments occupied 20 percent by low-income residents; the term usually refers to projects financed by tax-exempt private activity bonds.

Panelist Mike Henderson, of Newman & Associates, Denver, CO, said that in financing affordable housing, the sponsor "who has the lowest cost of capital wins." He recommended tax-exempt financing as the way to achieve a lower cost of capital. Henderson said bond financing can also help a developer get housing tax credits for the project – though 4 percent rather than 9 percent credits – without having to compete for an allocation from the state's annual credit volume cap.

Using tax-exempt financing can reduce debt service costs for an assisted living project through a below-market mortgage rate. Other ways that can be used to reduce debt service costs and/or subsidize a project include raising housing tax credit equity (thereby reducing the size of the debt), obtaining soft second debt financing, or obtaining foundation monies or other assistance.

Abromowitz cited a Massachusetts project, spon-

Progress Slow on HOPE VI Activity, But Apt to Speed Up

In the first three fiscal years of HUD's Hope VI program, for redevelopment of distressed public housing properties, more than $1.5 billion was appropriated.

But revitalization of public housing is a slow moving process. As of the end of FY 1996 – or September 30, 1996 – less than half the appropriated funds for three years had been earmarked by HUD for expenditures for specific projects.

"Public housing authorities have had a very charmed life, and this is a culture shock for many of them — the whole concept of privatization and having economic risk in their transactions," said CPA John Mackey, of Ziner & Company, P.C., Boston. "I think that's one of the reasons it has progressed slowly."

Mackey was one of three speakers on a panel on HOPE VI and public housing redevelopment at NH&RA's 1997 Summer Institute in Beaver Creek, CO.

The goal of HOPE VI — the popular name for HUD's Urban Revitalization Demonstration program — is to help fund the demolition of obsolete public housing and rebuild public housing projects as successful mixed-income communities. HOPE VI funds are awarded as grants to public housing authorities (PHAs) by competition.

Despite the slow progress of projects already approved, Mackey said the trend with the new round of HOPE VI funds is to provide opportunities to smaller city PHAs, as opposed to the mega-developments funded so far that have been in the nation's largest cities.

This shift means more opportunity for the private sector, Mackey said.This is because the award of more -- but smaller grants -- to smaller PHAs will mean more total redevelopment jobs.

HUD in April announced the availability of $488 million in FY 1997 HOPE VI grants in a new funding round. The maximum award was $35 million to any single PHA. Awards were just announced. *(See box on next page.)*

Another speaker, attorney Ben Applegate, a partner with Schiff Hardin & Waite, Chicago, said that in recent HUD notices announcing the availability of

(Continued on page 6)

---

sored by a nursing home provider, where the total development cost was financed 40 percent by mortgage debt through a state housing finance agency program, 40 percent by housing tax credit equity, and 20 percent by federal HOME funds and assorted soft loans.

Husser described an assisted living property his company syndicated, Longwood, located in an upper middle-class town of Reading, north of Boston. The property has 86 units, of which 18 (20 percent) are for low-income tenants and the rest for market-rate tenants.

The project received debt financing through the state's Elder Choice program, which provides below-market construction and permanent loans funded by tax-exempt bond proceeds for development of elderly rental housing projects occupied at least 20 percent by low-income residents.

The project has qualified for the 4 percent housing tax credit ($80,000 per year), and $1 million in historic rehabilitation tax credits. The development involved rehabilitation of an existing 2-1/2 story school house plus construction of a new three-story building.

Costs for the 18 low-income units are also offset by state payments from the Group Adult Foster Care program of about $1,000 per resident per month.

Mackey said the developer also obtained a commitment of HUD Section 8 certificates, to make it possible that at least half of the low-income residents are from Reading.

Husser noted that Longwood, as of mid-August, was 80 percent occupied after being open nine months. While the project lease-up rate for assisted living facilities is typically four units per month, Longwood has rented eight a month, said Husser. "It is doing very, very well."

Abromowitz predicted that as more of the tax credit issues are worked out, and states regulate the business, more and more developers will be entering the assisted living arena and targeting a portion of it at the affordable end.☐