



Building Sustainable Organizations for Affordable Housing and Community Development Impact

Lessons and Recommendations from the Field

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Executive Summary

Introduction

The Great Recession deeply affected the affordable housing and community development delivery system in the United States. Despite a continued, urgent — and even increased — need for affordable housing and other community development efforts during the downturn, the meltdown of financial markets, including the Low-Income Housing Tax Credit (LIHTC) market, and the decline in real estate values in many areas of the country, stalled many affordable housing projects in various stages of the predevelopment pipeline. This in turn put enormous pressure on the organizations — both nonprofit community development organizations and mission-oriented for-profit developers — that form the backbone of the nation's capacity to develop and operate affordable housing. While the delivery system has recovered to some extent over the past year as the LIHTC market improved and programs made possible by the American Recovery and Reinvestment Act allowed stalled projects to proceed, the effects are likely to persist for some time to come.

Enterprise works with nonprofit and for-profit developers across the country to build and operate affordable housing and community development projects. Our developer partners range from large organizations (nonprofit and for-profit) that develop and operate portfolios across the country, to regional developers, to organizations that work in a particular city or neighborhood. Many of these organizations have always operated on thin capitalization and margins. Given the stresses of the past several years, we have seen development partners of various sizes across the country experience significant cash shortages, close business lines, and even dissolve.

Nonprofit and mission-driven for-profit affordable housing and community development organizations are the engines that provide safety and stability for the residents they serve and their communities' resources. Building sustainable development organizations is an effective strategy for protecting and preserving these assets.

Focus of this Paper

As we work to build and preserve sustainable affordable housing and other at-risk community assets, Enterprise seeks to learn from the experience of our partners and existing portfolio. While organizational failures are still rare in the community development industry, examining them can teach us valuable lessons. Enterprise undertook a detailed look at 10 nonprofit affordable housing and community devel-

opment organizations that closed their doors or were pushed to the brink in recent years. The organizations were located across the United States, and their affordable housing portfolios ranged in size from less than 100 units to more than 3,000 units. Some partners were neighborhood based, while others served an entire state or region. All maintained an extensive array of programs, services and business lines. To fully appreciate the implications of the lessons learned, we also looked at the broader context for the stresses that strained these organizations, including dynamics in the local affordable housing development system. Based on this review, the paper outlines recommendations and issues for further discussion to help strengthen community development efforts and systems across the country.

As Enterprise analyzed the 10 stressed affordable housing and community development organizations, we sought to understand what happened and why, and to draw out common themes and lessons that might be helpful to other developers facing similar organizational issues. In Section 1, we discuss in detail our findings and recommendations.

To better understand the dynamics of affordable housing and community development organizations, Enterprise reviewed a range of factors, including the industry's systemic risks. We then focused on a particular segment of developers: nonprofit organizations that exclusively serve a specific geographic area at the neighborhood-to-metropolitan level or serve a specific population within a metropolitan area. These "place-based organizations" (PBOs) are stewards of a community's assets and have been among Enterprise's key partners. Because key funders and stakeholders are increasingly focused on comprehensive community development at the very local level, we decided to examine the unique opportunities and challenges these organizations face. This is the focus of Section 2.

In order to enhance critical infrastructure issues, we set out to make specific, practical recommendations to both community development organizations and the financial partners, funders and policy-makers that can help to address some of the themes and challenges we identified. These recommendations are discussed in more detail in Section 3.

Overall Recommendations

1. Recommendations for development organizations based on a review of stressed and failed organizations (See Section 1)

- **Strengthen financial reporting and analysis.** Maintain a capable and consistent accounting department that provides timely and accurate financial reporting to board members, senior management, financial partners, and government and philanthropic funders.
- **Beware of significant one-time cash receipts.** Though counterintuitive, pay attention to how significant one-time cash receipts mask an organization's financial difficulty and delay proportionate business decisions.
- **Grow strategically.** Grow incrementally, strategically, and sustainably — particularly if planning to add a property management arm.
- **Cast off resource-draining projects.** Be willing to cut losses before you are certain that the property will fail.
- **Maintain relationships.** Build strong, long term relationships with funders and government partners, both of whom are integral to the success of an organization and its properties.
- **Conduct forecasting and scenario planning.** Conduct realistic planning exercises with an analysis of various scenarios.
- **Diversify Revenue Streams.** Diversify revenue streams by growing strategically into new business areas with the understanding that profitability may take years to achieve.

2. Other recommendations for development organizations based on industry context (See Section 2)

- **Prioritize organizational sustainability.** Affordable housing development organizations must focus on being fairly paid for what they do; this includes fully allocating overhead costs and structuring their deals accordingly.

- **Utilize development criteria.** Create a list of development criteria to help the organization's board approve or decline future projects.
- **Adopt an early-warning system.** Organizations must create an early-warning system for detecting when a property has a problem, and seek assistance in addressing it.
- **Consider collaboration.** Where there is duplication and opportunity to collaborate, organizations should consider taking that step.

3. Recommendations for financial partners and funders (See Section 3)

- **Incentivize long-term ownership and stewardship of affordable housing assets.** In structuring housing credit transactions, public lenders should ensure that there are financial incentives for effective ownership and operation of the properties. Foremost, this includes lenders allowing cash flow to be paid to a project's sponsor.
- **Ensure fully funded workout projects and portfolios as well as ownership requirements.** When organizations take over troubled projects or portfolios, the funders involved should ensure that they are funded prior to take-over. Also, ownership requirements set by housing finance agencies must be flexible enough to allow for replacement general partners who may not meet all the nonprofit set-aside requirements.
- **Set realistic management fees and structure deals with sufficient cash flow to pay them.** Increase allowed property management, asset management and partnership management fees based on an owner's demonstration of actual, fully loaded management costs.
- **Embrace an early-warning system.** Funders have an obligation to create an environment that does not punish organizations for exposing weaknesses, but rather encourages early discussion of problems.

Mission-based developers are the heart and soul of our field. Implementing the above recommendations will: 1) build stronger organizations, 2) create viable business models, and 3) allow information to flow transparently among organizations, their leadership and funding partners. The community development industry is committed to developing safe, sustainable affordable housing, and the organizations that deliver and safeguard these assets deserve the same level of commitment to support their sustainability.