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Kill the Loopholes, Including the One for 'Low-Income Housing'

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As tax reform begins to wind its way through the legislative process, President Trump should not forget his call last month to get "rid of the loopholes and complexity that primarily benefit the wealthiest Americans and special interests." Resistance to eliminating these features of the tax code will be stiff, but the more such unjustified breaks are eliminated, the more tax rates can be cut.

Consider the Low Income Housing Tax Credit, created by the 1986 tax reform. This $9 billion credit masquerades as an antipoverty program, but it mainly subsidizes developers, investors and the financial industry.

To stimulate low-income housing construction, the federal government allots a share of tax credits to the states, which dole them out to selected developers. The credits cover part of the construction costs of multifamily housing projects. The developers must cap rents for a share of the units, so the benefits of the tax credit are meant to flow to tenants in the form of lower rents. Yet the developers usually sell the credits to banks and investors, often using syndication companies as intermediaries. The investors, developers and middlemen—not poor families—end up grabbing most of the benefits.

Gregory Burge of the University of Oklahoma estimated in a 2010 study that the value of the rent savings for tenants was a mere 35% of the value of the tax benefits going to developers. Economists Edward Glaeser and Joseph Gyourko concluded two years earlier that the low-income housing credit "is not very effective along any important dimension—other than to benefit developers and their investors."

Although the credit subsidizes a lot of construction, it mainly displaces private building that would have occurred without the program. A 2005 study in the Journal of Public Economics by Todd Sinai and Joel Waldfogel found that half or more of housing would have been produced even without the credit. And a 2010 study for the Journal of Public Economics by Michael Eriksen and Stuart Rosenthal found that as much as 100% of development subsidized by the credit is offset by declines in private development.

The housing credit is also a prime target for abuse. Earlier this year a National Public Radio reporter profiled a Miami-area business that stole $34 million from 14 low-income-credit housing projects by submitting inflated construction cost data to the government. Another Miami company discussed by NPR stole $4 million from four projects by the same method.

The NPR report concluded that “little public accounting of the costs exists, even among government officials and regulators charged with monitoring the program.” This is consistent with a 2015 Government Accountability Office report, which concluded that federal oversight of the credit is “minimal.” The federal government has audited the low-income credit activities of less than 20% of state housing agencies.

This credit is the exact sort of corporate tax loophole that Congress should repeal in exchange for a lower corporate tax rate. Instead the Senate Finance Committee held a hearing this summer to explore *expanding* the credit. Members are swayed by lobbyists such as the chairman of the National Association of Home Builders, who claimed at the hearing: “If we want to provide affordable rental housing for lower-income households, it is financially impossible to do so without a subsidy.”

That is not true. To increase supply, Americans need fewer local zoning regulations that inflate housing costs, not more federal subsidies. A 2005 study found that restrictive regulations have doubled the price of housing in cities such as San Jose and San Francisco, as well as in the New York City borough of Manhattan. Numerous academic studies suggest that zoning reduces the supply of multifamily housing, which hits low-income families the hardest.

Housing affordability is a serious problem in many cities, but the low-income credit is a misdirected federal solution for a local problem. GOP tax reformers should put it—and other loopholes like it—on the chopping block.

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