Privatization and the Social Contract:

Corporate Welfare and Low-Income Housing in the United States since 1986*

Doug Guthrie
New York University

Michael McQuarrie
New York University

ABSTRACT
This paper examines the process behind the emergence of the Low-Income Housing Tax Credit (LIHTC), a provision of the Tax Reform Act of 1986. While effectively channeling resources into inner city housing development, this policy shift created a windfall for corporations by allowing them a double tax break that individual citizens were explicitly denied. We place emphasis on the ways in which the political process is a murky world in which powerful lobbies can create hidden opportunities, and organizational actors can take advantage of these opportunities to forge new institutions and even, in some cases, new industries. A process of institutional selectivity then works to select systems that favor the powerful players and interest groups that are shaping legislation behind the scenes.

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"Conflicts over institutions lay bare interests and power relations, and their outcomes not only reflect but magnify and reinforce the interests of the winners, since broad policy trajectories can follow from institutional choices."

—Kathleen Thelen and Sven Steinmo, *Structuring Politics*

"Plato once said: When there is an income tax, the just man will pay more and the unjust man will pay less on the same amount of income."

—Senator William Cohen, Congressional Record, 1986[1]

INTRODUCTION

In the mid-1980s, a radical transformation took place in the provision of public housing in the United States. With the declining budgets of the Department of Housing and Urban Development and, specifically, the discontinuation of the budget line for Section 8 New Construction Projects, the development of federally-subsidized low-income housing in the United States had come to a virtual standstill. Direct federal subsidies were replaced by an institution that would have radical consequences for the structure of the welfare state, the Low-Income Housing Tax Credit (LIHTC). Yet, when it was originally presented to Congress as part of the Tax Reform Act of 1986, the LIHTC was to target a very small sector of the tax-paying population in exchange for a tax shelter that had become politically dangerous and many in Congress acknowledged needed to be eliminated. Within a few short years, however, the LIHTC became one of the most significant vehicles for *corporate* welfare, providing massive tax abatements for corporations at the same time as it facilitated the flow of private resources directly into the inner city areas that needed them most. More than this, the LIHTC helped give rise to an industry of community-based housing developers and intermediary organizations, as it

[1] 99th Cong. 2nd Sess., 132 Cong Rec S 8132, Vol. 132 No. 86, addressing the issues raised by a new piece of legislation, the Low-Income Housing Tax Credit, a small provision in the Tax Reform Act of 1986.

provided them with resources from the corporate sector. In relatively short order, from 1986-89, we see the explosion of an industry that rests on a set of resources and practices that simply did not exist in the years prior to 1986.

In this paper, we examine the transformation of low-income housing to illuminate a shift in power and priorities within the social contract in the United States. This case is about the leveraging of corporate resources for the funding of a public good, however, this system only works with a radical giveback to the corporate community—a giveback that was denied individuals. Within a few short years in the late 1980s, this new policy—and the industry that emerged around it—would become one of the key features of urban revitalization in the United States, quickly gaining bipartisan support as it benefited multiple constituencies. Thus, this process is not only about corporate welfare and the leveraging of corporate resources in the provision of a public good; it is also about emergence of a new logic around which community development would be framed.

Empirically, this case is important for several reasons. First, while the LIHTC is held up by constituencies on both ends of the political spectrum as an example of political compromise, the actual political history is more complicated than this. Actors in the field regularly cast this policy shift as a moment of rational bipartisan politics, where powerful interest groups and politicians came together to recast the organizations that shape inner city life in America.[2] However, this understanding is far from the reality: in fact, the political history of the LIHTC suggests a process of backroom politics, where corporations were able to receive a windfall tax abatement that Congress publicly agreed tax paying citizens could not possibly be allowed.

[2] This account comes from two sources—the in-depth interviews we conducted over the course of this research (discussed below) and the Congressional Record on discussions of the LIHTC (see, e.g., “Remarks by Jack Kemp,” Congressional Record – House, 7/11/89, 101st Cong. 1st Sess., 132 Cong Rec H 357, Vol. 135 No. 91.)

Second, in a related vein, while corporate accountants understand well the corporate welfare benefits of the LIHTC, few in the community development and policy worlds actually understand the specific ways this institution operates as a windfall for corporations. The LIHTC itself is much more than a simple tax credit; it allows corporations a "double-dip" in the tax pool, which individual citizens where explicitly denied. Third, in a more positive light, the LIHTC did accomplish something that many in Congress and in low-income communities across the country had been attempting to accomplish for years prior—it became the catalyst for an industry built around the alliance of big banks, small nonprofit organizations, and social actors with large capital interests—but the creation of this organizational field was as much an accident as it was an intended outcome. Prior, legislation like the Community Reinvestment Act of 1977 and the Passive Loss Provision in the Economic Recovery Act of 1981 had failed in their attempts to create a system that would move private resources to the development of low-income housing. With each attempt to create such a moment of change, the critical players in the field found themselves unable to capitalize on the opportunity to enhance the delivery of low-income housing. Yet, with the LIHTC, the field was suddenly transformed. Thus, this case is empirically important because of how little is known about the actual history of the institution *and* because the consequences of this change catalyzed the creation of an organizational field around critical issues of the low-income community.

Finally, this case is important because of the general trend of which it is one important example: As one of the most significant of the tax credit and other experiments around the public-private partnerships, the LIHTC is also part of a longstanding trend that has seen corporate taxes decline precipitously since World War II (McIntyre and Nguyen 2000). As Figure 1 shows, individual and corporate income taxes as percentages of the GDP were close at the middle of the century—8.2 and 7.3 percent respectively in 1945. While individual income taxes remained basically constant over the rest of the Century, at 8.3 percent of GDP in 2002, corporate contributions to the GDP fell to 1.2 percent, the lowest level since 1942. The LIHTC is one dimension of the institutional arrangements that have contributed to the privatization of the welfare state while, at the same time, allowing corporate contributions to the state to decline.

(FIGURE 1 ABOUT HERE)

Theoretically, our analysis of this case illuminates important issues about class politics, the power of the corporate lobby, and the shift in institutional arrangements that privatize the welfare state apparatus in the United States. How does it come to pass that the funding of low-income rental housing in the United States today can only be accomplished by first allowing corporations to receive a "double-dip" tax break? Through what social and political process does this part of the social contract become linked inextricably to corporate welfare? We argue that, regardless of how this change in the tax code came about, the important point is that once this change was recognized as the windfall it was for the corporate community, interest group politics and the logic of the changing social contract worked to fix the legislation in place. The corporate lobby fought to keep it, and Congress, which is heavily dependent on the corporate sector for funding, followed suit. Thus, there was a process of selectivity at work whereby institutions of a certain logic become "locked in place" (Chibber 2003). Since the 1980s, this institutional selectivity has most often reflected the interests of capital and a general market logic.

This paper is organized as follows: first, we provide an overview of how the current system of low-income housing provision occurs. We then give an account of how this system came about and how it became institutionalized. Finally, we discuss the theoretical implications this case history has for understanding the political economy of policy formation in the United States.

DATA AND METHODS

The data for this paper come from two sources. We conducted 150 in-depth interviews with individuals working in the local development sector in three US cities.[3] Qualitative data and background information on the process we describe here come from these interviews. Interviews were semi-structured, organized around the issue of the building of low-income housing and public-private partnerships more generally. These interviews gave us insight into the pressures, practices, and views of the advocacy community working with the LIHTC. These interviews were conducted with individuals directly connected to Community Development Corporations (CDCs), intermediaries, and banks, as well as individual working in the government and the larger development community working with the LIHTC. All interviews were recorded and transcribed.

We also did historical analysis the Congressional Record for the 99th-107th Congresses (1985-2002) to track the political debate over LIHTC legislation. To gather these data, we conducted general searches on Lexis Nexis's Government Documents/Congressional Records section. Lexis Nexis allows for general and Boolean searches for document text. In order to be sure that we captured all records that refer to the LIHTC, we conducted general searches on "low-income housing tax credit." These words were entered without quotation marks, and as a

[3] The qualitative data upon which this paper is based is part of a larger study on corporate social investment in local metropolitan areas. At the core of the larger study is a national survey of 2,776 corporations with targeted oversamples in Seattle, Cleveland, and Atlanta. The qualitative data gathered were based on interviews conducted with community developers and nonprofit leaders in these cities to develop a deeper understanding of the institutional arrangements in which the corporations we surveyed are operating.

result allowed us to capture all documents that include the words “low-income,” “housing,” “tax,” and “credit,” and any combinations of these words as they were discussed in the subcommittee and floor records of both houses. In addition, we conducted searches on relevant issues that have emerged as related to the LIHTC—“passive loss,” “capital gains,” “real estate development.” This yielded over 500 pages of subcommittee and floor records, which we then pared down to the relevant information for the legislation under scrutiny. In conjunction with the relevant documents that comprise the actual legislation and its amendments, we treat this body of documents as the history of the legislation in Congress.[4]

THEORETICAL ISSUES

The conceptual framework here draws from theories in political sociology and complex organizations to examine the process behind a public policy change. From organization theory, we draw upon scholars that emphasize the ways in which individuals and organizations respond to new policy arrangements present. One important aspect of this perspective is that it focuses attention beyond the legislative process itself to the individuals and organizations that interpret and adopt practices in response to changes in the formal rules of the field (Fligstein 1990, 1997; Dobbin and Sutton 1998). DiMaggio (1988) has referred to these individuals at “institutional entrepreneurs,” emphasizing the ways in which individuals can seize upon opportunities to can take advantage of the changes in institutional arrangements. In moments of institutional change, it is often the case that key individuals innovate based on the political opportunities available to them to come up with new possibilities, new solutions, or new models of action within a given

[4] We should emphasize here that the case we describe below, comes directly from the data we gained from a combination of the interviews with actors in the field and from the Congressional Record. Thus, our data are reflected not only in the quotations from interviewees and the Congressional Record but also, more broadly, in the details of the case we describe.

social system. According to this body of research, we would expect that organizational responses to shifts in policy arise from the initiative of individuals to take advantage of new institutional arrangements.

From political sociology, we draw from the work of scholars who emphasize the larger political economy in which new policies are formed (Jenkins and Brents 1991; Pontusson 1991; Prechel 2000). These scholars have argued that the political logic of the capitalist economy has important implications for the ways in which class interests come together to shape political outcomes. Over time, the structure of the capitalist state has come to increasingly favor institutional arrangements that favor business interests. The perspective from this group of scholars is that new policies and new institutional arrangements reflect the political economic logic of this system. The policy changes that have reshaped the welfare state in recent decades are one area where these changes have been most apparent. From this perspective, we would expect that new institutional arrangements are products of political struggles between the representatives of business interests and those that represent other political constituencies.

THE CASE: THE TRANSFORMATION OF LOW-INCOME HOUSING DEVELOPMENT

Born of deep tensions between developers and growth coalitions on the one hand and those who understood housing to be a central component of social welfare, the Housing Act of 1949 eventually settled on a general vision for housing as providing a “decent home and suitable living environment” for all American families. With dual objectives of providing for low-income families and redeveloping urban areas, legislators and interest groups eventually settled on a path that addressed housing through a combination of private sector subsidy and direct public intervention (Colton 2003; Marcuse 1995; Wright 1981). For the next 30 years, federal allocations would be the primary source of funding for the building of low-income housing. However, with the end of the Section 8 New Construction program, federally-funded low-income housing development all but ground to a halt in the mid 1980s. In 1986, a new program emerged to provide funding where federally-allocated dollars left off. Figure 2 illuminates this shift: by 1986, federally funded multi-family units dropped below 20,000 for the first time in the history of HUD; by 1988, nearly all low-income multi-family units were being funded, at least in part, by the LIHTC.

(FIGURE 2 ABOUT HERE)

This shift marks a fundamental moment of change because it represents a transformation of the funding and development of a public good. In the case we describe here, corporations provide capital in exchange for tax credits, and this capital is then used to leverage resources from banks and private developers (who are often in partnerships with nonprofit development organizations) to build low-income housing. 'Privatization' does not capture this process, because that implies a relocation of public expenditures into private hands. What we are describing here is a fundamental transformation of funding generation and governance over housing policy. More importantly, this was one of the early experiments in the trend toward removing the federal government from the process of development and management. In the overall scheme of the federal budget, the LIHTC is a relatively small indirect expenditure. Even if we limit the field to housing policy, the largest expenditure on housing is the mortgage interest deduction—indeed this expenditure is several times as large as all other housing expenditures combined (Howard 1997). The importance of LIHTC, however, does not come from its size. Rather, the importance of this policy is that it is increasingly *replacing* direct expenditures for low-income housing. Moreover, LIHTC has provided a modular model for replacing public provision of social goods with private provision that is leveraged with public dollars. As we write, this model is increasingly being deployed in public education and commercial development. Lastly, LIHTC legislation has resulted in changing these institutional arrangements in ways that go well beyond the initial policy.

Figure 3 represents the funding process of the pre-1986 welfare state with respect to budget allocations for low-income housing. This figure shows that banks and corporations remit taxes to the federal government. A portion of these funds are allocated to the Department of Housing and Urban Development, which then contracts with a developer to build housing. Some rents flow back to developers, though some portion of these also flow from the government in the form of Section 8 subsidies. Starting in 1977, small changes began to take place within this system. Namely, with HUD budgets in decline and many cities reaching a level of urban crisis, strong evidence of redlining by banks prompted Congress to pass the Community Reinvestment Act (CRA), which mandated that banks invest resources in the local communities in which they operate. While the intent of the CRA was to channel the flow of resources into the inner cities where banks had operations, the actual effect in the 1970s and early 1980s was small. Banks generally "invested" in these communities through grants and charitable donations to local nonprofit organizations—they changed their behavior enough to get CRA credit and reduce taxable income through tax write-offs—but the legislation did nothing to change the logic of their lending practices. This is a significant point. The CRA legislation was specifically intended to influence the logic of the way banks conducted their business. Instead, as numerous bankers related in interviews, they conducted their business as before only with a new cost center to support, that of grant-making.

(FIGURE 3 ABOUT HERE)

Figure 4 represents the flow of resources under the Low-Income Housing Tax Credit regime after 1986 and currently in place. We list specific organizations here as examples of the roles that general corporate forms play in the model—Coca-Cola, Bank of America, and Fannie Mae are examples of the roles that large corporations and large commercial banks play respectively.[5] The model is considerably different from the represented in Figure 3 in terms of its the organizational players involved, the flow of resources, the role of the government, and the relationship between the government and other organizational actors. The crucial feature of this system begins with the fact that there is no connection between the corporation and the government in terms of the flow of resources, at least with respect to the portion of a corporation's taxes that are credited through investments in LIHTC. If a central feature of a welfare state system is that tax dollars are divided up and allocated by the federal government, in this system, corporate dollars flow directly into the housing development system through the purchase of tax credits. Tax credits are allocated to states by the IRS as $1.75 per person in the state population.[6] The credits are distributed through state housing agencies to developers based on a point system that reflects the priorities of state government. Corporations provide capital through a syndicator, a type of organization that arose in the 1980s as the financial institution that transforms tax credits that originate with the sponsor into capital that comes from the corporate sector.[7] In return, corporations receive a dollar-for-dollar write-off against bottom line tax liability. However, additional benefits to corporations also exist. First, corporations are

[5] While these examples are meant to represent general cases, they are concrete empirical examples that come directly from our field research.
[6] The program began as a $1.25 per capita allocation. In 2000, that figure changed to $1.75, and beginning in 2002, increases were pegged to inflation rates.
[7] The National Equity Fund (NEF) and the Enterprise Social Investment Fund (ESIC), which are the syndicate arms of the Local Initiative Support Corporation (LISC) and the Enterprise Foundation respectively, were the earliest models of these types of organizations.

permitted to buy tax credits at a "market" rate. This means they can purchase the credits for approximately 75-85 cents on the dollar (i.e., 80 cents reduces a dollar's worth of corporate taxes). Second, and most importantly, corporations receive a "passive-loss" write-off against the future depreciating value of the low-income property. In short, corporations receive a double tax break as they receive the tax credit and the write-off against future losses.[8]

(FIGURE 4 ABOUT HERE)

As we will discuss below, it is clear in the Congressional Record that, when Congress considered affording individuals the same benefit, the collective sentiment was that this type of double benefit would be "double-dipping" in tax breaks and could not be allowed. However, it is now a central feature of the flow of resources around low-income housing and a central feature of hidden corporate welfare. Corporate resources then flow into development deals, where they are put together with other financing sources, namely financing from banks, foundations, intermediaries, or public money where it is available. These deals require a sponsor, who initially applies for tax credits from the state housing finance commissions; these sponsors can be for-profit developers, nonprofit organizations, or a local housing authority. In short, these deals are extremely complex and, as a result, extremely costly in which various sources of public and private funding are stitched together to enable development that is usually initiated by CDCs. Figure 5 shows the scope of resources flowing through this system from corporations since 1986. Since that time, the LIHTC has become the primary driver behind the flow of resources into inner-city housing project development, accounting for over $5.2 billion in corporate dollars

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[8] To some extent this reflects the risk of the investment. The credits are collected incrementally over a 10 year span and the capital is put up in the first couple of years. Moreover, there is some risk of recapture though no one that we interviewed has heard of a case of complete recapture. Lastly, it seems that models of risk assessment do not really do a good job of assessing the security of the investment because of a lack of understanding of many of the institutions that are key for the investment—such as community development corporations.

invested in low-income housing and contributing to the building of over 1.3 million units for low-income families.[9]

(FIGURE 5 ABOUT HERE)

A final feature of this system—and a site of some of the most interesting institutional developments—has to do with the rise of new financial instruments in the 1990s: originally, the philosophy behind the LIHTC was to not only capture resources from the private sector but also to harness its market discipline—private or corporate investors were bound to the deals for 10 years through the recapture provisions of the tax credit, the logic being that economic actors would make more intelligent investment decisions in development projects than the government would, especially if the value of the investment was at stake. However, with the rise of mortgage-backed securities, which first emerged in 1991, these financial resources are in practice quite fluid. If a corporation has a large tax liability one year, it can buy large sums of tax credits and then also be eligible for the passive loss deduction; but if, a few years later, the tax liability is low, the same corporation can sell these tax credits on the secondary market to Fannie Mae or other types of similar institutions that deal in tax credits.[10]

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[9] It is important to note here that the figure of $5 billion only scratches the surface of what the LIHTC actually means in terms of the flow of resources. In the past, Section 8 New Construction Projects were built almost fully on government direct allocations. The LIHTC acts as initial financing that then leverages other sources—usually comprising somewhere between 15-30 percent of the total financing of a low-income housing development project—in order to make the financing by commercial institutions more attractive. As a result, the resources here provide financing that attracts financiers that heretofore had little to do with low-income development projects.

[10] Many institutions deal in tax credits, though currently Fannie Mae is the single largest holder of LIHTC notes in the United States. Freddie Mac and Fannie Mae were not big players in developing or playing a significant role in the syndication process. However, these two GSEs became major players with respect to the LIHTC in another way: with the emergence of mortgage-backed securities in the early 1990s (commercial mortgage-backed securities for multi-family homes were first issued in August of 1991), Fannie Mae and, to a lesser extent, Freddie Mac begin purchasing LIHTCs on the secondary markets as mortgage-backed securities. This is

How did this institutional shift occur? What were the political, economic, and social pressures that brought such radical innovation about? And how did it come to be that corporations could receive a benefit of a double tax break, a benefit that individual tax payers were denied when the law was written in 1986? What was the political process behind the transfer of funding for a public good, which also became the single largest instance of corporate welfare in the last quarter century?

A POLITICAL HISTORY OF THE LOW-INCOME HOUSING TAX CREDIT

In 1986, the U.S. Congress inserted a small provision into the tax code that would have ripple effects throughout corporate and low-income communities, fundamentally altering the construction of low-income housing in the United States and the role that corporations play in this process. With the passage of the Tax Reform Act of 1986, Section 42 of the Internal Revenue Code, the Low-Income Housing Tax Credit, became one of the early experiments in the movement toward the leveraging of private funding for public goods, giving rise to an industry that ultimately helped change the face of many urban settings in America, at least in the area of low-income housing. It is a system that works well; well enough that when it was renewed in 1989 and eventually made permanent in 1993, it had gained strong bipartisan support throughout both the Houses of Congress. As one industry insider described the program's success:

> It's the largest single producer of affordable housing in this country, the low income housing tax credit. And you know the reality that people still I don't think really

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an important innovation, because it makes the market liquid, which, in turn, reduces the risk for corporations who are the holders of LIHTCs. One of the features of the LIHTC is that deals are typically structured so the benefits are graduated in over a 10-year period. The logic here was that "investors" would have incentives to maintain the property, an incentive that did not exist with the passive loss provision. When the market becomes liquid through the securitization of LIHTCs, investors begin buying and selling tax credits on the market. Over the course of the 1990s, Fannie Mae became the largest holder of LIHTCs in the country.

> understand [it]… [W]hat the tax credit for multi-family development did was level out your cost. So it allows you to produce a project that you can make economically feasible for lower rents. It's a great structure and I think it's a great way to get corporations to do part of what they ought to be doing to support the economy (Personal interview, 2002).

This confidence in the program's efficacy is echoed in Congress, as well, where the program has thrived under bipartisan support for more than 15 years. As Senator Sasser (D-TN) put it at the time of the Credit's renewal in 1989:

> In housing today, the participation of the private sector is more important than ever before. The low-income housing tax credit is an excellent incentive for private developers to build projects that provide affordable housing to low-income individuals… I have long supported the low-income housing tax credit. It helps guarantee that a steady supply of new housing will remain available to our poor. While this tax credit cannot be expected to eliminate all of our housing shortages, it is a key element in encouraging the private sector to build multi-family housing for lower income families… (U.S. Congressional Record, 1989a).

At first blush, it seems clear that those in government constructed and passed a piece of legislation that is a clear, rational answer to challenges facing the development of low-income housing in the 1970s. Yet, this institution did not arise from a transparent political process. Instead, it emerged from a process in which some of the most important decisions appear nowhere in the debated recorded within the Congressional Record. In fact, much of the debate within Congress in 1986 surrounding the LIHTC focuses on the use of the legislation by individuals and in only one obscure place in the Record is it mentioned that corporations stand to receive a potential windfall from this legislation. Yet, when the legislation was passed, a group of entrepreneurial community developers took advantage of this legislation to create a system that transformed the industry surrounding the development of low-income housing in the United States.

Background Conditions and Institutions

The conditions for this moment of change reach back well over a decade before the LIHTC came to life, setting the stage for an eventual moment of dramatic and rapid institutional change. The story begins with the housing crisis of the 1970s, a time in which many cities in the United States were suffering the long-term consequences of decaying housing projects and the immediate consequences of the budget crises of the 1970s. As one industry insider from Cleveland, Ohio recalls the evolution of these background conditions,

> You have to look at the broader environment. I think starts with an observation that [at that time] the city of Cleveland… was a dying city. It's population had plummeted from 900,000 to 500,000, massive out-migration of the middle class, lots of de-segregation, everything. The river catching fire. So early in the 1980s, City Hall adopted a policy of supporting, as a primary way to bring neighborhoods back, supporting the growth of CDCs [Community Development Corporations]. And they have had an unwavering commitment for 20 years now (Personal Interview, 2002).

Another industry insider pointed to the early attempts at institutional change that set the stage for the rapid changes in the mid-1980s:

> It really started around 1973. There was a national conference in Chicago where people came together for the first time to talk about this problem of lending discrimination and fair housing issues. It was, the organization that grew out of that was national, National People's Action, Gail Cincotta who recently, some people call here the mother of CRA… [Then] the community activists went to Congress in 1975 to get the Housing Mortgage Disclosure Act passed, so that banks would have to disclose what they're doing. Then with the information that was generated for two years by that, they went back to Congress in 1977 and said, ok, now we have some data that shows these banks are not making loans in inner-city neighborhoods. And they got Congress to pass the CRA. So those two laws are still viewed in tandem because without the HMDA, even today, you wouldn't have the data to find out what's really going on. It's sort of the teeth behind the CRA, I think. So there were a whole number of CDCs that got started in either 1979 to 1981. And this is a group of CDCs that were almost all started in response to, well, now there's a tool. Now there's the CRA and there's money that's going to be available for development. And almost all of these organizations were started by grassroots community organizations that had done the organizing around redlining (Personal Interview, 2002).

In both of these statements we find common elements that are echoed throughout the oral history of the community development industry today: urban crises and specifically housing crises in the

1970s; the emergence of a neighborhood-based activist community to begin to deal with these issues; new institutions such as the Community Reinvestment Act, the Housing Mortgage Disclosure Act, and federal legislation attempting to force banks to change their business relationships with low-income communities.

The mid-1980s marked a crucial shift in the structure of the welfare state. With a conservative in the White House and, for two years, a Republican-controlled Senate, the Democrat-controlled House was, for much of the 1980s on the defensive. The Tax Reform Act of 1981 marked a period of dramatic cutbacks that affected many programs, including those that funded the construction of low-income housing. Many in Congress blamed the Reagan administration directly for this shift (though HUD budgets had actually been in decline in the late 1970s as well): As Senator Kerry (D-MA) put it in 1986, “The crisis we feel today has been brought about in part as a result of the Reagan Administration’s rejection of the federal government’s historic role in stimulating the production of multifamily housing directly through federal spending programs. Since 1981, budget authority for housing has declined by 60 percent…” (U.S. Congressional Record, 1986d).

One of the items of that 1981 tax bill, however, the “passive loss” provision, was set up to create incentives for wealthy individuals to invest in low-income housing. The main idea behind the passive loss provision is that individuals could receive write-offs against the depreciating value of property. By the mid-1980s, many in Congress recognized the host of problems that were associated with this provision, problems that would be addressed in the Tax Reform Act of 1986. For one thing, many wealthy individuals were finding ways to avoid taxes entirely, simply through investments in cheap property. Even more significantly, the passive loss provision was actually contributing to urban blight: because the provision hinged on depreciating value, the incentives were for individuals to intentionally allow property to become rundown. As a result, the Tax Reform Act, which was the second major overhaul of the tax code under Reagan sought to close this loophole for individuals. As Senator Packwood (R-OR), then Chair of the Senate Finance Committee, testified in introducing the bill,

> On the individual tax, the principal thing we did was severely limit the benefit of so-called tax shelters… What very wealthy individuals would do is invest in properties, usually real estate but not always, that generated paper losses. They would offset the paper losses against their regular income. This would reduce their regular income, their taxable income, down to zero. They paid no taxes. Everyone in this Chamber has gone home and had this question put to them—these are people making $15 or $16,000 a year. "Senator, I don't mind paying my fair share, but why don't they pay something?"… Every year, the story is printed in the papers – and I paraphrase – 844 Americans last year made over $1 million and paid no taxes. That, justifiably, galls the average taxpayer who is making $15,000 a year and paying $1,000 in taxes. This bill closes those loopholes (U.S. Congressional Record, 1986b).[11]

Senator Cohen (R-ME) expressed the widespread support for dealing with the passive loss tax shelter problem, saying,

> Mr. President, I want to express my support for the tax reform bill that is now being considered by the Senate… For too long, our Federal income tax system has been too complex and filled with esoteric provisions benefiting special interests. Over and over I have heard my constituents say that the tax system is unfair, that the wealthy are not paying taxes… While they dutifully pay their fair share of taxes, others use exotic write-offs, creative tax shelters, and investment schemes, the vast majority of which are legal, to reduce their tax liabilities… (U.S. Congressional Record, 1986a).

The Emergence of the LIHTC

The passive loss provision would be replaced by a new financial mechanism, the LIHTC. According to the official debate that took place in Congress at the time, the LIHTC was originally intended for individual investors—the same wealthy individuals who had benefited from the passive loss provision tax incentives to invest in low-income housing. Thus, the official

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[11] Legislative day of Wednesday, September 24, 1986, 99th, Cong. 2nd Sess., 132 Cong Rec S 13782, Vol. 132 No. 129, though submitted to the Senate Congressional Record on 9/26/86.

proposal that emerged in the 99th Congress (1985-86) was to take away the passive loss provision and replace it with a tax credit. Congress clearly acknowledged at that time that creating such an incentive required they close the passive loss loophole; the Congressional record is clear on this point—that investors should not have both the credit and the passive loss. Such a scenario was referred to as "double-dipping" (U.S. Congressional Record, 1986a).

At the time, there was an animated debate in both houses of Congress over removing the passive loss provision, as some members argued that it was unfair to the individuals who had invested in the tax shelters with the understanding of ongoing depreciation benefits. For example, as Senator Mitchell (D-ME) argued:

> As I believe Senator Packwood is aware, low-income housing is different from other real estate. Low-income housing does not provide cash-flow from rents, or the promise of appreciation on sale. Investors are attracted instead by the return they can receive by offsetting their tax liabilities from other income. This was the understanding they had when they undertook, the investment. Many thousands of investors throughout the country are now in the position of having entered into commitments to provide equity payments in limited partnerships for low income housing on which they will not be able to take their anticipated losses under the committee amendment (U.S. Congressional Record, 1986a).

Senator Cranston (D-CA) echoed this sentiment, linking the issue to confidence in Congressional legislation:

> In 1981 the tax laws were changed to require the use of 15-year depreciation schedules for real estate. Investors responded to that incentive and bought land, erected buildings, and provided housing and jobs. They created low-income apartments, small shopping centers, office buildings and factories. In calculating the return on their investments, they counted on receiving the allowance of depreciation contained in the law at the time. The Senate Finance Committee bill will eliminate a substantial part of those depreciation benefits – wiping out deductions that were pivotal to the economic benefit of the investment… Can we get meaningful tax reform without breaking promises made by Congress earlier? (U.S. Congressional Record, 1986b).

In the end, however, the arguments against allowing for both a tax credit *and* the passive loss provision prevailed, with the clear understanding that it would be simply too much of a giveback to the wealthy. If there was already grumbling among constituents about tax shelters, allowing for the double-dip tax break could become a political bombshell.

Before further discussion of this moment of institutional innovation, it is important to reiterate a crucial point here: when the Tax Reform Act of 1986 was passed, the LIHTC was, at least according to the debate in the Congressional Record, intended for *individuals*. In the record of the 99th Congress (1985-86), the entire passive loss debate centered solely around how to move wealthy individuals from investments that rely on depreciation to those that would use the tax credit. And in our interviews with individuals who were working in the community development industry in the mid-1980s, the general consensus was that this legislation was set up to provide incentives for individual investors. As one of our interviewees who was working in the industry at the time put it, "Nobody thought about corporations [for the LIHTC]" (Personal Interview, 2002).

Actually, despite this perception among community developers, it is not quite accurate that *nobody* was thinking about potential benefits for corporations; at least one individual in Congress was thinking about such issues. There is an oddly out-of-place entry into the Congressional Record of the 99th Congress: one of the very last entries into the Record is a statement by Democratic Senator Bennett Johnston (D-LA) that raises some very interesting issues, especially given that nothing is ever mentioned about the corporations buying tax credits under the LIHTC regime in the hundreds of hours of floor debate recorded before. As if to simply put on public record what no one else in the entire debate over the LIHTC seemed to be willing to say, Senator Johnston begins:

> Mr. President, I wish to confirm my understanding of the application of the new so-called passive activity loss and credit rule that is embodied in section 501(a) of the conference report to accompany H.R. 3838, the Tax Reform Act of 1986. As I understand the conference agreement: First, rental activity is per se classified as passive activity; second,

> income derived from the investment of working capital is characterized as portfolio income; third, C corporations may offset losses from passive activities against income from an active trade or business but not against portfolio income; and fourth, losses from an active trade or business may be offset against income derived from the investment of working capital and vice versa. To assure that my interpretation is correct, I would like to ask the distinguished chairman of the Finance Committee to confirm the accuracy of a number of examples of this rule (U.S. Congressional Record, 1986e, emphasis in original).

The discussion goes on in this fashion for several pages of the Congressional Record, finally ending with Senator Johnston saying "I thank the distinguished chairman for his assurances."[12] There are a couple of things that are noteworthy in this exchange. First, in the debate over whether individuals could receive *both* tax credits *and* the passive losses, which took place in June of 1986, corporations are never mentioned. And the perception taken from this debate, as noted above, is that the legislation was only intended for individuals. However, it is clear that at least one Senator was willing to go on record explicitly reminding the public that, while passive losses had been eliminated for individuals, corporations would continue to be

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[12] Senator Johnston then goes on for several pages of testimony giving example after example of corporate benefits from the LIHTC (though, notably, without ever mentioning the provision itself), after each statement eliciting a response of affirmation from Senator Packwood:

> SENATOR JOHNSTON: First, do I understand that if a closely held C corporation has $400 in losses from passive activities – such as equipment leasing and/or real estate transactions, $500 in income from an active trade or business – which is not a passive activity – and $100 of portfolio income, the company may offset the $400 in passive losses against the $500 of active trade or business income, leaving taxable income of $200, $100 or which is attributable to the active trade or business and $100 of which is attributable to working capital – portfolio income.
> SENATOR PACKWOOD: The Senator from Louisiana's understanding is correct.
> SENATOR JOHNSTON: If a closely held C corporation had $400 in losses from passive activities, $500 in losses from an active trade or business and $100 in portfolio income, its $100 in portfolio income can partially offset the $500 in losses from an active trade or business, leaving a $400 loss carry forward from the active trade or business and a $400 passive loss carry forward.
> SENATOR PACKWOOD: The Senator is correct (U.S. Congressional Record, 1986e).

allowed these benefits under the new provisions.[13] Given that this was a recording of a floor presentation that was entered into the Record, we can safely assume that many others in the Senate understood this as well. Second, although the Democratic Senator does not mention the LIHTC, the repeated references to real estate indicate that this exchange is obviously lodged to register a statement about the so-called "double-dip" tax break that was eliminated for individuals. Third, the repeated questions of scenario after scenario yield a dialogue that appears, at least on paper seem to register his distaste for the fact that "C-corporations" stand to benefit dramatically from this particular shift in the tax code. It is crucial that Johnston's testimony emphasizes "C-corporations" (with the record placing emphasis on this term). C-corporations are large-scale corporations that can have an unlimited number of shareholders (as opposed to S-corporations, which have a limit of 75 shareholders) and have no limits on passive loss income. Thus, it is clear from Johnston's testimony that he is addressing an issue that is quite different from the animated passive loss-LIHTC debate that took place in Congress earlier in 1986.

Interest Groups

Given the debate and subsequent decision in Congress to eliminate the passive loss provision and replace it with the LIHTC, how was it that corporations would come to benefit from the same double-dip tax break that Congress debated and decided to eliminate? How did a small provision in the tax code established to close one loophole facilitate the flow of billions of

[13] Corporations have long benefited from passive losses, as it is critical to corporate calculations of depreciation values of operating equipment. When the passive loss provision was set up in 1981, the notion was (1) that real estate would then be eligible for passive loss write-offs, and (2) that individuals would be able to take passive loss write-offs the way corporations could. What changed in 1986 was that this possibility was eliminated for individuals but not for corporations. It is also important to note here that the Senator's reference to "C-Corporations" is singling out the opportunity that exists here for large-scale corporations.

dollars into the development of low-income housing across the country? The answer lies, in part, in the fact that a few key interest groups working within the emerging field of community development saw the opportunity for corporations that was hidden within the legislation. By capitalizing on the opportunity before them, these institutional entrepreneurs stumbled upon a system that would provide an astounding set of resources for social change.

In the years prior to the Tax Reform Act of 1986, an organizational field had begun to take shape around the issues of community development and, specifically, low-income housing. In 1979, the Ford Foundation set aside $10 million to fund a nonprofit organization that would have as its mission the development of communities through the development of low-income housing. Specifically, this created the Local Initiative Support Corporation (LISC), which would work with local nonprofit organizations in a variety of targeted cities in order to develop a network of local Community Development Corporations (CDCs). These organizations, in turn, would serve as the initiator of local development projects with technical, training, project, and operating support from LISC in addition to their usual sources of funding: other foundations grants, occasionally dues, fees of various kinds. LISC's role was to serve as an intermediary between these CDCs and various funders—a role that would become much more important with the enactment of the LIHTC because the amount of dollars under consideration would multiply several times with its enactment. LISC grew quickly in its scope and mission, working as an intermediary between the corporate community, and the CDCs representing local neighborhoods and communities. Today, though largely hidden from public view, LISC is the largest community building nonprofit organization in the United States.

In 1982, a similar organization was founded by developer Jim Rouse, The Enterprise Foundation, which also had at its core mission the economic development of local communities.

Slightly smaller than LISC and slightly broader in mission—community development through housing *and* workforce development as opposed to only housing—Enterprise was the other major player working with local CDCs in cities across America. These two organizations and the local development organizations they worked with were very much attuned to the legislative changes coming about (they were lobbying for it), as they sought ways to take advantage of changes in the tax code to develop in inner city communities. When the time was ripe, they would also spawn two new organizations—National Equity Fund and Enterprise Social Investment Corporation—which would become the "syndicators", the clearing houses for processing the massive amounts of resources that would eventually flow from the LIHTC. As a result of these and other organizations like them, there was an organizational field in place that was prepared to consume any new political opportunities for the development of low-income housing that emerged from the Tax Reform Act of 1986.

But the shift that occurred in 1986 would also require a few key individuals who would take the new legislation that came out of this shift in the tax code and innovate within this new political context. It is clear from the Congressional Record that both Rouse and LISC president, Mitchell Sviridoff, had lobbied Congress in an effort to get this legislation passed.[14] Clearly Rouse and Sviridoff represented an important interest group in the area of community development (i.e., those community development organizations that had deep ties to both the nonprofit *and* the corporate community), and Rouse, especially, having been an immensely successful real estate mogul before turning to philanthropy and community development certainly had significant ties to the corporate community. With an emerging field of

[14] For reference to Rouse and his lobbying efforts, see, e.g., 99th Cong. 2nd Sess., 132 Cong Rec S 8132, Vol. 132 No. 86. For reference to Sviridoff, see "Comprehensive Tax Reform: Hearings Before the Commission of Ways and Means House of Representatives," 99th Cong. 99-45. pt. 5 of 9, 3769 (Statement of Mitchell Sviridoff, President of LISC).

organizational actors that were increasingly focused on community development through the development of low-income housing, there were a number of players, who were actively seeking out opportunities to shift resources into low-income housing development. The LIHTC was a piece of legislation these individuals were interested in. However, at the time, the appropriate institutions that were necessary for the complex process that would channel corporate dollars into the low-income housing (see Figure 4) did not exist. Even if corporate accountants were aware of the opportunity the LIHTC presented in terms of a double tax break, corporations were not about to get into the business of low-income housing development and management, which was a necessary part of the process of capturing these tax credits.[15] As such, following its inception in 1986, community developers like Rouse, Sviridoff, and others, working with CDCs, turned to individuals to raise money for the LIHTC. However, raising money by convincing individuals to buy tax credits proved very difficult, and it looked like the legislation that was the LIHTC would go nowhere. For one thing, according to individuals working in the community development arena at the time, many were angry at Congress for changing the rules after they had made the investments to take advantage of the passive loss provision. As one industry insider recounted the early years of the legislation,

> I remember everybody was very, very skeptical. Mainly because most of the [wealthy people] had just gotten burned… As part of the '86 act, they changed things so you couldn't take advantage of [passive losses] anymore. So now, what happened is a lot of these people had made investments… that would never make money, but they could take tax losses on them. And now they couldn't take tax losses anymore. So they're sitting

[15] One of the key features of the LIHTC is that the credits graduate in over a 10-year period. The legislation was passed in this way to tie the "investors" (i.e., the holders of the credits) to the property. This was a direct response to the perverse incentives that had emerged when individual invested in low-income property to take advantage of the passive loss provision. It was also based on the logic that the property would stay available for low-income households (60/40 or 50/30—i.e., 40% of units restricted to tenants with 60% of median income or 30% at 50% of median income). The problem for corporations is that, in order to receive the credits, they would need to be in the business of development and monitoring of the property.

> there with this piece of shit building that doesn't yield any money, and they just threw away 100,000 bucks… They were the ones who bought into these limited partnerships—mostly doctors, dentists, CFOs, CEOs. And they're telling me, "Bullshit. You're telling me to invest again? And I'm going to get burned again by the changes in the law by Congress?"… I mean I had one guy that just was so ticked off, he says, "I got burned, and I'm not doing it again…" (Personal Interview, 2002).

There were some examples of attempts by financial institutions to raise capital through individual funds, but, without exception, all of these experiments failed.[16]

In early 1987, a group of individuals working in the community development industry in Cleveland began to examine this legislation and realized that corporations would be much better suited for investment in this type of tax credit than individuals for a variety of reasons. First, corporate tax liability is much greater than individual liability so the pool of potential resources that could be channeled into low-income housing was much greater. Second, and more importantly, while Congress closed the passive loss loophole for individuals, *it did not do the same for corporations*, which meant that corporations could receive a double tax break, with the first part coming through the buying of tax credits (a one-for-one write off) and the second, by virtue of this "investment", coming from the passive loss tax break against the future depreciation of the low-income property. One industry insider recalled this moment of realization, saying, "Well, that's the beauty [of what we did], because if I'm an individual and I buy credits, I only can take the credits. I can't take the losses. And they were thinking that the market for this were individuals. And then when the corporations started taking it, they had this added other benefit, of taking these losses. Because as a corporation you're able to take the passive losses associated with the development" (Personal Interview, 2002). As Joe Hagan, now President of the National Equity Fund, who brokered the first tax credit deal, explained:

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[16] The highest profile case of this was a fund that was set up by Boston Capital. This attempt, as with others like it, was abandoned before it got off the ground due to difficulties raising funds.

> So the ‘86 act was passed, everyone said this tax credit program is something to look at, but most people were convinced that it wasn’t going to go that far. And it was very, very complicated. We do it now like it’s nothing, but at that point in time it was really hard to structure deals. It was Cleveland Tomorrow[17] that said, let’s put together a Cleveland equity fund, and let’s figure out how to get some of our corporations to invest in tax credit deals. And, so, I’m at the state housing finance agency, and I work closely with Enterprise [Jim Rouse’s organization]. And Enterprise kept telling us, “listen, the credits come in over 10 years. If there’s a way for us to structure a payment, or structure the payment from the investors over 10 years, we’d get them a better return. But what we need is a bridge loan. We need somebody that’s willing to provide us the money up front, and take corporate investor, take the investor notes and finance those…” So we had access to this huge pot of money. And so, I went to our counsel and said, “listen, can we use this?” and they’re saying, “well, we don’t see why you can’t.” So, what I did is I contacted Enterprise [Foundation], worked with them, and developed a bridge loan program, called the Corporate Local Development Loan Program. And we were able to charge an interest rate that was ½ of prime. It could actually go down to 0%, but for the most part it was ½ of prime. And we would lend the money in, up front; we would take as collateral the investor notes from major corporations. And that really got the first couple of investors interested in doing this type of deal (Personal Interview, 2002).

With large tax liabilities, the tax credit made sense for corporations, but on its own, it is basically an even tradeoff with paying taxes to the government (a dollar-for-dollar write-off of tax liabilities). However, by combining the credits with book value depreciation of the property meant that corporations could receive the double-dip Congress had explicitly argued against individual receiving: with the passive loss provision still in place for corporations, the opportunity existed to take the tax liability and turn it into an investment for corporations. Over a 10-year period, beyond the credit corporations could yield an additional graduated write-off against future taxes. Hagan estimated that many of the early deals he put together yielded an additional 15 percent return for corporations in unpaid taxes over the next decade. In other words, rather than simply paying taxes, corporations could basically take that tax liability,

[17] Cleveland Tomorrow is a membership organization of the most important local corporations. Participation is limited as much as possible to CEOs. The result of this format is an extremely effective local business organization. When they decide to create an equity fund for housing it happens quickly and is well-funded. The organization has spun off further housing funds as well as organizations that address industrial retention and downtown development and planning.

"invest" it in low-income housing, and generate something on the order of a 15 percent return over the next decade.

The deal that Hagan describes above is the first LIHTC deal that channeled corporate dollars into the development of low-income housing. It is important to note that the institutions that would eventually become central to development of corporate LIHTC deals largely did not exist in 1987. As Hagan points out above, because the credits are graduated in over a ten-year period, in order to make the deals happen, the money must be guaranteed up front by some type of "bridge loan" (as Hagan puts it) or syndication by some type of intermediary organization. In the case of the first deal, Hagan and Rouse figure out a way to use unclaimed money from Ohio Capital (which was underwritten by Standard Oil's Corporate Foundation). However, once Hagan and Rouse figured out a way to syndicate the credits to capture corporate dollars, the credits became very enticing for large corporations.

In sum, the social actors who were a part of lobbying for the legislation also played a key role in pointing the way toward a new logic around which the organizational field would be constituted. Joe Hagan of Ohio Capital and Jim Rouse of Enterprise, among others, figured out how to build the intermediary institutions that would allow corporations to receive a windfall tax abatement that was explicitly denied individuals when the legislation was passed. In that sense, these individuals played a central role in building the institutions that allow the LIHTC to deliver resources for the building of low-income housing while at the same time providing a windfall for corporations. Hagan and Rouse had feet in both communities: Hagan was working for Ohio Capital at the time on the development of affordable housing but shortly thereafter went on to Banc One to head the bank's community development division; Rouse was a real estate mogul who had made a huge amount of money in development.[18] While these individuals represented interests on both sides of the process, other forces were necessary for the solidification of this new innovation. We turn now to the issue of institutional selectivity and the ways that innovations that favor powerful corporate actors become locked in place within the political system.

Institutional Selectivity and the LIHTC

The first tax credit deal was brokered by Ohio Capital in 1987, with corporate purchases by Exxon, Bank One and Standard Oil, and backing from Standard Oil's Corporate Foundation. Out of this innovation sprang an industry. Similar models were successfully set in place by the Enterprise Foundation, LISC, and Fannie Mae, and as the resources began to flow, the CDC movement became the other major beneficiary of this provision in the tax code. By the time the then-temporary Credit was up for renewal in 1989, the emerging industry had significant momentum, and powerful interest-groups—from corporations to nonprofit community developers—arose to protect it. Legislators seemed eager to claim that this model of innovation was what they had in mind all along. Indeed, some seemed to go out of their way to state that current practices matched their original intent. As Senator Heinz stated on the Senate floor in the Fall of 1987:

> Mr. President, on September 28, the National Temple Nonprofit Corporation of Philadelphia held a ribbon-cutting and ground-breaking ceremony to mark the completion

[18] Though Sviridoff was lobbying and operating alongside these two, he was, to some extent, further removed from the corporate community than Hagan and Rouse. A former president of Connecticut's AFL-CIO and professor of social policy at the New School for Social Research, Sviridoff came to the field with fewer ties and fewer interests in the corporate community. However, Sviridoff was a former officer of the Ford Foundation and was the first president of LISC, which was largely established to be an intermediary between the corporate and nonprofit communities.

of construction of 20 units of housing for low-income families in north Philadelphia and the beginning of rehabilitation on 12 additional units. This project was financed by Fannie Mae, which invested $570,000 in the housing, and by the Enterprise Social Investment Corporation, CIGNA, Mellon Bank, the Ford Foundation, the William Penn Foundation, and the National Trust for Historic Preservation, as well as the City of Philadelphia. This project utilized provisions of the 1986 Tax Reform Act and it is precisely the kind of low-income housing initiative the Congress contemplated in enacting these tax provisions… At a time when federal housing funds are particularly limited and our nation faces a continuing erosion of its low-income housing stock, *it is important for corporations to step up and use those tools Congress has provided* (U.S. Congressional Record, 1987, emphasis added).

The legislative discussion at this point quickly became a model of bipartisan support. This happened for a variety of reasons many of which have been pointed out by Christopher Howard (1997) in his analysis of the "hidden welfare state".[19] First, conservatives in Congress who had been pushing to all for the double tax break for wealthy individuals found that they had appeased a much wealthier and much more powerful constituency—the corporate community. At this point, the debate over passive losses quickly fell away, as Republicans realized they had gotten even more than they were originally asking for in their desire to reinstate the passive loss

[19] As Howard (1997) argues, the hidden welfare state is composed of indirect tax expenditures. These expenditures total up to fully half the total value of direct social policy expenditures. Rather than growth being dependent upon activist electoral coalitions and well-organized interest groups that are attuned to the U.S. political structure, the hidden welfare state operates under the radar of many politicians and interest groups. The politicians that consistently block direct social expenditures often support indirect tax expenditures, and the appeal of these expenditures often crosses the aisle. Republicans see it as minimizing the role of government and working with markets to achieve other goals, Democrats see the policy result as worthwhile. As a result, indirect expenditures can grow even in periods without "reform-oriented regimes" (Amenta 1998). These expenditures are often attached to revenue bills and, therefore, often become law with minimal discussion. The discussion that happens takes place in one committee each in the Senate and the House (Finance, and Ways and Means). Further, these expenditures are rarely advocated for by powerful interest groups, but they tend to generate an interest group composed of the third-party providers that are responsible for social provision in the system. Therefore, once these policies are enacted they can become progressively more difficult to reduce or eliminate. In a related vein, indirect expenditures tend to take on a life of their own. They are able to grow despite consistent opposition from the relevant bureaucracy: the Treasury. Aside from the Treasury, criticism is often weak because the expenditures are poorly understood.

provision. But Democrats in Congress also realized that, in an era of declining budgets to HUD, this legislation, which was bringing about a flow of resources into inner city housing projects for, was perhaps the best they could hope for. As Representative Rangel (D-NY) put it 1989,

> I have for years said that I would rather see direct federal spending to subsidize mortgages and rents for low-income housing since they are more efficient than tax incentives, but since the last administration chose to cut those direct subsidies by 80 percent over the last 8 years I have been compelled to seek support for housing for low-income tenants in the tax code… The credit had a slow start after enactment in 1986. However, as the rules became clear and developers and investors began to understand how to use credits production picked up. By 1988 more than two thirds of the credit allocated to the states was used and in 1990 the amount used is expected to be higher. The credits issued so far will assist the development of over 150,000 housing units. With its extension it is likely that the credit will even produce more housing at a greater pace over the next several years (U.S. Congressional Record, 1989b).

Subsequent changes in the industry and in the legislation came quickly. On the community development side, the LIHTC became one of the key resources that allowed intermediaries like LISC and Enterprise to situate themselves at the center of local development deals, providing them an institutional power they never before had. In the mid-1980s, both of these organizations founded new subsidiaries, NEF and ESIC, which would quickly step into the role of syndicating tax credit dollars and managing the funds that these credits would provide.[20] In addition, with extra sources of funding injected into the industry, LISC and Enterprise began to work very aggressively with banks as well as corporations in structuring deals. For corporations, the financial benefits attached to buying the credits made participation in this program a relatively simple calculus. For banks, however, there was another incentive attached to it, though there were different risks as well. Since 1977, as a way of combating redlining, banks had been under pressure to direct their business to the inner cities in which they had

[20] NEF was founded in 1987; ESIC was actually founded in 1984, but its syndication work began in 1987. ESIC and NEF would emerge as the primary syndicate organizations of LIHTC deals for the next decade.

operations. However, they could also receive Community Reinvestment Act credit through philanthropic activity in these areas. Most banks worked through these channels, as the conventional wisdom of the banking industry was *still* that lending in underdeveloped inner city areas was a high-risk proposition. However, with corporate dollars providing free capital and with careful attention by the intermediaries, who now more than ever wanted to protect the investments they courted, banks quickly came around to lending in the inner city.

Changes occurred on the legislative side as well. Once the tax credit occupied its position of bipartisan support—conservatives protecting it for the source of corporate welfare it had become, liberals protecting it as the primary engine behind the building of low-income housing—agreement and compromise quickly followed in appeasing all constituencies involved. First, through a series of amendments in 1989, the process was quickly deregulated, so that investors (corporations), intermediaries (LISC, Enterprise), and syndicators (NEF, ESIC) could treat the market for tax credits as a true market. This meant that corporations and the syndicators were free to skim off whatever amount of the tax credit the market would bear. In other words, if corporations wanted to negotiate to pay $.80 on the dollar per credit, that would perfectly legal; similarly, if a syndicate could structure a deal in which it could skim some amount of the tax credit in fees, that was legal as well. Figure 6 shows the real value purchase price of tax credits over the life of the LIHTC. This margin is a large source of the revenue for syndicators but also, in many deals, provides extra incentives for corporate investment.

(FIGURE 6 ABOUT HERE)

Second, two financial instruments, one old and one new, became critical to the system that was emerging, as they allowed the corporate investors to reduce any risk exposure they might have had in investing in LIHTC products. The main risk that remained attached to the

LIHTC for corporate investors was a rule that mandated that corporations receive the benefit of the credits and depreciation value (passive loss) over a 10 year period. The logic behind this provision was that there would be economic incentives on the side of the investor to ensure that the property would be a viable low-income property at least as long as the financial benefits for the corporation were still outstanding. However, this piece of the legislation became a sticking point for corporate investors: what corporation has the personal resources or expertise to manage and oversee investments in low-income properties. As NEF and ESIC emerged to step into the role of syndicators, they also served the purpose, together with their parent organizations, of property assessment, while the CDCs and local developers serve the role of property management. At this point, these organizations began to model their property control after Real Estate Investment Trusts (REITS). The ability to do this was another direct consequence of the Tax Reform Act of 1986, as changes in the tax code allowed REITS to manage their properties directly. Further, because corporations were now technically investing in trusts of low-income property, the relative risk of not receiving the credits or future depreciation write-offs was very low (in other words, the funds allow corporations to spread risk across a portfolio of low-income properties). A second financial mechanism has had a shorter lifespan than REITS, but it is no less important in reducing the relative risk for corporations in purchasing LIHTCs. Mortgage-backed securities essentially allow corporations to remain free from long-term commitments to the market, as Fannie Mae, Ginnie Mae, and Freddie Mac are always willing to purchase tax credits from corporations that would like to shift their portfolio of tax liability.

A third and final issue that touched the legislative realm had to do with capital gains. In 1989, President Bush threatened to veto the renewal of the LIHTC unless Congress agreed to his agenda to end the capital gains tax. Democrats were now in a considerable bind: vehemently opposed to ending the capital gains tax, they were also deeply committed to keeping the LIHTC alive as a program. The compromise that ensued, which was partially brokered by the corporate lobby would deal with the issue of capital gains in a much narrower way: instead of agreeing to eliminate capital gains completely, the compromise reached was that the corporate “investors” in LIHTCs would be exempt from capital gains tax liabilities when they cashed out of the property after 10 years. With this, the corporate lobby had helped mold this legislation into a largely risk-free financial mechanism.

DISCUSSION

In this section we draw out the implications of the case described above for the theoretical positions different camps have taken on the issue of policy formation and institutional change. To summarize what we have argued thus far with respect to the case: (1) the passage of the LIHTC in 1986 created a dramatic shift in the way resources were pulled together to build low-income housing; the new model of low-income housing development gave rise to an industry built on public-private partnerships leveraging corporate dollars that pass through intermediary organizations (syndicates), which not only guarantee the funding up front but also manage the financing of the properties. Corporations, for their part, receive a double tax break that was explicitly denied individuals in the passage of the legislation. The system effectively channels resources into the development of low-income housing to replace federal funding of Section 8 New Construction programs. However, it is also a (gratuitous) windfall for corporations. (2) In addressing the question of how it came to be that corporations were able to receive the “double-dip” tax break that individuals were denied, we relied on two sources of evidence to understand the emergence of this institution. First, we relied on the Congressional

Record to map out the terms of the debate around this legislation; second, we relied on in-depth interviews with individuals who played key roles in putting the legislation to use in the early stages. (3) The Congressional Record is very clear about the decision to not allow individual investors and developers the possibility of receiving both the tax credit and the write-off against depreciation values of the property—the passive loss. (4) However, one part of the Congressional Record, though not part of the debate over the LIHTC/passive loss tradeoff, does make clear that individuals in Congress were aware that if corporations figured out a way to buy the credit, they would be in a position to take advantage of the "double-dip". (5) Individuals who were part of the lobbying interest group on the community development side (i.e., Rouse and Hagan) were aware of the possibilities for corporations but still had to overcome the hurdle of creating the intermediary institutions that would underwrite the credits. (6) Once it becomes clear that corporations could indeed benefit from the double-dip, bipartisan support for the system falls into place and there is no further debate about the issue.

What does this case reveal about political processes in the era of the declining welfare state? What does it tell us about corporate power in the passage of certain pieces of legislation? Many scholars have examined the question of how state structure and interest group politics influence the emergence of various policies. Building upon the view that the autonomous state and political institutions are independent causal factors in political outcomes, some political sociologists have focused on demonstrating how particularities of the U.S. political structure play a central explanatory role in policy outcomes (Skocpol 1985; Skocpol and Amenta 1986; Amenta and Zylan 1991; Amenta and Poulsen 1996; Amenta 1998; Kingdon 1984; see Clemens and Cook 1999 for review). Taking a more managerial approach to policy outcomes, neoinstitutionalists have argued that interest groups and states engage in an iterative process from which new “conceptions of control” and new “institutional logics” emerge (Fligstein 1990; Dobbin and Sutton 1998; Clemens 1997; Guthrie and Roth 1999; see also Bourdieu 1990, 1996, 1998 for discussion of institutional logics of emerging fields). One of the problems with these literatures is that they are often dealing with explicit, high-profile policies for which there are clearly defined debates. Howard (1997) points out that many more obscure policies—such as those in the realm of taxation—are subject to much more covert backroom dealings, if only because they require more specialist knowledge. However, a deeper problem is that both of these literatures ignore critical issues that have been central to the study of political economy, namely class interests and the logic of accumulation. Jenkins and Brents (1991), for example, have argued that state-centric theorists ignore the larger political economy and, specifically, the central influence of class conflict on major social reforms. Pontusson (1991) discusses the ways that organized interests participate in the formation of governmental policy and the ways that governmental policies in capitalist economies increasingly serves business interests (particularly, according to Pontusson’s argument, in regimes where labor is weak). As the role of corporate interests have become more institutionalized as part of the political process in advanced capitalist economies, the corporate class’ influence over policy formation becomes more and more an endemic part of the political process.

Prechel’s (2000) theory of political capitalism also argues that, over the course of the 20th Century, the institutional arrangement of the capitalist state have grown to be increasingly supportive of business activity. Prechel identifies three core dimensions of political capitalism. First, the business class has the capacity to develop “a coherent conception of the relationships between their economic goals and the policies necessary to achieve those goals” (p. 277). Second, the capitalist class has the ability to agree on these goals and thus behave like a class.

And, third, the capitalist class has the capacity to exercise control over the state in implementing these goals in the form of policy. Essentially, this theory argues that, while it is important to think about the organization of the state and the relative autonomy of the state at different points in time, the state has become far less autonomous from the capitalist class than it has been in the past. According to Prechel, "political capitalism has produced an elaborate state structure that is engaged in more spheres of economic activity to promote capitalists' agenda" (2000: 277).

The policy formation and process of institutionalization of the LIHTC supports this view well. In the era of the receding welfare state the state has experimented with many different models for leveraging private funding to deliver public goods (see, e.g., Spitzer and Scull 1977; Hasenfeld 1985; DeSeve 1986). As early as the mid-1970s, the state had an agenda in place of cutting back the federal funding for new development of affordable housing and developing incentives for investment from the private sector, and in 1981, there was an explicit effort to put in place the incentives for individuals to become investors in low-income housing. But as the problems of this system became apparent in the mid-1980s, a new approach was put on the table. One of the interesting things about the debate over this new policy was the explicit nature of the discussion over the impossibility of allowing tax-paying citizens to receive both a tax credit *and* a write-off against passive losses their "investment" might incur. Yet, while the possibility was removed for individuals, the same was not done for corporations. The absence of the discussion of corporations with respect to the LIHTC in June of 1986 might lead one to believe that members of Congress had simply not thought about the possibility of corporations being the investors in low-income housing credits. Indeed, the institutions that would eventually emerge to syndicate tax credits did not yet even exist, and corporations were not likely to get into the business of property development and management. However, in September of 1986, it becomes clear that members of Congress *are* aware of this potential and that they would thus stand to benefit in exactly the ways that individuals were denied.

The more likely scenario is that this process reflects the dimensions of political capitalism described above—that corporations had a clear conception of their goals and that they were able to influence the policy outcomes to achieve those goals. In this case, the goals related to the issues of accounting and taxation and the specific political opportunity was the passage of the Tax Reform Act of 1986. The absence of the discussion of the corporate angle from the political debate suggests the possibility of a backroom political deal that would leave this issue out of the discussion in the debate in June of 1986. In either case, the logic of favoring business' interests certainly came into play in the aftermath: once individuals like Rouse and Hagan figured out how to put the first corporate-LIHTC deals together, the issue of the "double-dip" tax advantage is never mentioned again with respect to the LIHTC. At this point, the market logic, which favors capitalists' interests allows the policy to become "locked in place" (Chibber 2003).

CONCLUSIONS

Today the LIHTC is an institution that is untouchable by either end of the political spectrum, and it has become the model for the leveraging of private funds for public goods.[21] It is also supported by a healthy community development industry that has radically transformed

[21] The New Markets Tax Credit, which was passed in 2000 as part of the Community Renewal Tax Relief Act, is a more general form of the LIHTC and was successful in Congress largely because of the extent to which the LIHTC is coveted by partisans on both ends of the political spectrum. The NMTC is for commercial not residential properties. Developers like them because they can be combined in the same project with LIHTC. So if you have an area that has a zoning requirement for ground-level commercial space you can use New Market credits for the commercial space and combine them with LIHTC credits for the residential. In the absence of this developers would have a significant portion of the deal without the benefits of credit, making it more difficult to raise capital.

the ways that low-income housing is funded and built in urban areas throughout the country. When legislators today discuss the LIHTC, they depict an institution that was forged through close bipartisan negotiation in the pursuit of a solution to the housing crises of the 1970s and 1980s. In 1990 Senator Moynihan recalled the process in the following way:

> In the 1980's we did begin a low income housing tax credit**.** As I recall, I offered this as part of the Senate version of what became the Tax Reform Act of 1986. On the House side, my dear friend, Representative Charles Rangel, enriched and enlivened the proposal. In the end we obtained a tax expenditure of $1 billion a year, with an extra helping for New York. The credit was extended in the Omnibus Budget Reconciliation Act of 1989 and continues through the remainder of this fiscal year. A lot of money, a billion dollars – per year. An investor in low-income housing receives the credit of a 10-year period, getting a credit equal to 9 percent of his investment each year. This works out to a 70-percent credit, in present value, over 10 years (U.S. Congressional Record, 1990).

Indeed, according to many in Congress, this legislation is often depicted as a transparently crafted piece of bipartisan legislation that came out of a time of acrimonious politics when the Republican-controlled Senate and White House often worked at cross purposes with the Democrat-controlled House. This account, however, is only half of the truth. Congress was very explicit about the need to close the passive loss loophole for individuals, especially given the replacement of this institution by the LIHTC. The double-dip could not be allowed. However, within a year corporations began receiving the very benefit of a double tax break from the purchase of these credits. Was it a mistake as the entrepreneurs watching from the sidelines suggested? Apparently not. The final entry into the Congressional Record of the 99th Congress suggests that individuals in Congress knew what was happening, and at least one Democrat was willing to go on record stating such. Congress knew what they were doing—they were providing another brick in the wall toward the privatization of the welfare state, but this time they were also creating the opportunity for an unprecedented windfall for the corporate community.

But the formal policy formation was only the beginning; the policy had also to be enacted by organizational actors in society. In 1986, the murky world of politics saw a small provision in the tax code that would fundamentally change the flow of resources in community development and constituting it as a new organizational field. It would also be a windfall for the corporate community, allowing corporations a benefit that individual citizens were denied. When individuals working in the community development field saw the opportunity open before them, they seized upon this opening to produce a new model of resource allocation in support of a much-needed public good. In doing so, they helped to reshape goals of the actors in this field. The constituencies that benefited from this new model truly were a bipartisan set of constituencies, and through this support, the institution quickly gained bipartisan support in Congress. In this sense, the implementation of the policy was as important as the backroom politics that produced it.

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Send inquires to Doug Guthrie, Department of Sociology, New York University, 269 Mercer St., 4th Floor, New York, NY 10003; doug.guthrie@nyu.edu.

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Research Questions Considerable time has elapsed since privatization was first implemented in a number of countries and therefore it is appropriate for the results to be evaluated at the macroeconomic level. This is particularly important in the developing world where privatization has been implemented as a political, economic, and social instrument for societal transformation (Stiglitz, 1998). Although a great deal of attention has been given to privatization in the developing world, most of the country-level studies have been descriptive and focused on the extent of privatization (Bennell, 1... Housing cooperatives currently provide moderate to low-income families with about 376,000 of units of affordable housing.1 This is equal to seventeen percent of the total number of rent reduction housing units owned by the nation's public housing authorities (HUD and Bureau of the Census, 1995; and Table 1).Â These cooperatives provided affordable housing for low and moderate income families, but they are not limited equity cooperatives (LECs) in the technical sense of having financial limits on the resale of membership shares. Most continue as cooperative housing today (Siegler and Levy, 1986; and Dolkart, 1993).Â These privatizations occurred mostly in the 1950s and early 1960s, but such activities were renewed in the 1980s and 1990s. fifth amendment to the United States Constitution.Â 8 See Paul Starr, The Meaning of Privatization,in PRIVATIZATION AND THE WELFARE STATE 15 (Sheila B. Kamerman & AlfredJ. Kahn eds.Â individual property owners fail to monitor, the existence of a market for corporate control provides a safeguard against inefficient man-agement.1 6 Similar incentives for cost reduction and careful moni-toring do not exist or exist in only an attenuated fashion in the public sector.1 7 Individual taxpayers do not have a direct claim to the surplus created by government.