



May 21, 2016

Sylvia C. Martinez
Principal Advisor/Manager
Office of the Deputy Director
Division of Bank Regulation
Constitution Center
400 7th Street, SW
Washington, D.C. 20219

Re: Recommendations for the FHLB Affordable Housing Program

Dear Ms. Martinez,

On behalf of the undersigned members of the National Housing Conference's AHP Working Group, we thank the Federal Housing Finance Agency (FHFA) for embarking on an update of the Federal Home Loan Banks' Affordable Housing Program (AHP). In the AHP's more than 25 year history, it has proven to be a critical resource for affordable housing. The more than 758,000 homes it has helped to create or preserve are a lasting resource for the families housed there and the communities in which they live.

The national organizations in the AHP Working Group support the AHP and hope that this process offers a way to sustain and expand its operation. Part of the success of AHP has been its reliance on regionally-appropriate strategies implemented by the different FHLB, and we hope revisions to the program regulations will continue that approach. We therefore offer constructive suggestions drawn from the experience of each organization's members who work with the program regularly to develop affordable housing nationwide.

I. About NHC and the Working Group

The National Housing Conference represents a diverse membership of housing stakeholders including tenant advocates, mortgage bankers, non-profit and for-profit home builders, property managers, policy practitioners, real estate professional, equity investors, and more, all of whom share a commitment to safe, decent and affordable housing for all in America. We are the nation's oldest housing advocacy organization, dedicated to the affordable housing mission since our founding in 1931. As a nonpartisan, 501(c) 3 nonprofit, we are a research and education resource working to advance housing policy at all levels of government in order to improve housing outcomes for all in this country.

For the AHP Working Group, NHC brought together housing organizations whose members work with AHP regularly: Local Initiatives Support Corporation, Enterprise Community Partners, Housing Partnership Network, Stewards of Affordable Housing for the Future, National Alliance of Community

Economic Development Associations, National Council of State Housing Agencies and NeighborWorks America. Our aim is combine practitioner-level insights, with all of their variations, into a national perspective that can guide FHFA and the FHLBs.

II. Practical focus

In sifting through the feedback from housing practitioners (all of whom are members of one or more Working Group organizations), we have differentiated between two types of recommendations:

- **Practical improvements** identify ways the AHP can accomplish its aims more effectively or efficiently, such as by streamlining processes, including underrepresented voices, or modifying program requirements. Our recommendations focus on these practical improvements.
- **Priority requests** suggest a different emphasis for distribution of AHP funds. Stakeholders naturally feel most keenly the needs of the areas they serve and advocate for more attention to them.

Generally speaking, the Working Group agreed that the flexibility granted to each FHLB on funding priorities is an important component of the AHP program, and that decisions on priorities are best handled within each FHLB's advisory process rather than at a national program level. Our recommendations therefore focus on practical improvements.

III. Recommendations

As a guiding principle, we agreed that AHP funds are most effective as a dedicated source of funds for affordable housing in either of two forms: early, patient funds for predevelopment and essential gap-filler that completes a project. Our first two recommendations focus on these approaches, followed by additional suggestions for improving the process. Where appropriate, we include examples from recent AHP rounds (keeping the participants and properties anonymous).

A. Early, patient money

Often, the hardest part of creating or preserving an affordable housing property is getting it started. The initial capital to secure a site, perform necessary studies, create a development plan, and apply for development funding is extremely scarce, especially for nonprofit developers. AHP could effectively leverage many other public and private capital sources by getting deals started with predevelopment funds.

Such allocations are by their nature higher risk, because many events can interrupt a development project in the early stages. Predevelopment funds also have to be patient, because the timeline from

project conception to permanent financing can be long and unpredictable, even for experienced developers.

AHP is well-suited to handle the higher risk and longer, uncertain timelines. It does not have the strict repayment requirements of for-profit capital, and the FHLBs have a higher tolerance for letting AHP loans sit on a balance sheet than, for instance, a typical commercial mortgage lender. Through the AHP application process and advisory groups, the FHLBs have the means to mitigate risk by careful selection of partners with a proven track record of completing development projects.

B. Essential gap-filler compatible with other rental subsidies

AHP awards are not usually large enough to be the sole mission-oriented capital source in an affordable rental housing development, except for the very smallest properties in lower-cost areas. Instead, AHP fills the gap between total development cost on the one hand and typically a combination of a small commercial mortgage, Low Income Housing Tax Credit (LIHTC) equity, and grants on the other hand. Gap filler, by its nature, occurs in developments that already have other affordability commitments required by the LIHTC allocating agency, state or local government loans, rental assistance contracts, and other resource providers.

AHP is an important gap filler for many projects, but it also can add unnecessary complexity to transactions. For AHP to be most effective as a gap filler, it should be willing to subordinate itself to the terms of the other affordability commitments, which are generally equal to or stricter than AHP requirements. Similarly, the AHP can rely on the compliance monitoring, developer fee limits, and other program terms of funding sources to which it is subordinate. Greater willingness to adapt and subordinate would allow AHP funds to go farther and be more effective as the final gap-filler, especially in complex transactions.

We received many examples from developers about how extended negotiations around the interaction between an AHP loan and other capital sources add time and cost to the development process, even to the extreme of having awards rescinded or the recipient dropping the AHP award from the project funding:

- A nonprofit in the Midwest had an AHP award rescinded after construction start because the appraised value of the property did not match or exceed the purchase price, despite the fact that the transaction was explicitly for preservation of a distressed and over-leveraged asset.
- A nonprofit in the Mid-Atlantic had advanced funds to aid homeowner purchase of rehabbed homes on the expectation of reimbursement from an AHP award. However, AHP determined that since the nonprofit had advanced the funds, it did not need the AHP funds, and so rescinded the award.
- Because many QAPs offer additional points for multiple sources of funds, developers will apply for an AHP commitment, but because the banks review multiple times during the development

process and can refuse to fund at cost completion/certification or even as late as post-stabilization, the funds are deemed unreliable, forcing developers to seek additional sources of financing. There was a development in one of the Plains States where the debt-service coverage ratio was deemed to be too high at the third review and AHP funding was pulled.

- There are inconsistencies in the way AHP funds get treated. When the grant goes to the sponsor and is then lent to the property, some banks let interest be charged and others do not. But when proceeds flow from the property back (in interest), AHP often wants to take it back, even if it is structured as a loan only for tax purposes. Projects typically want to pay down AHP to pass the true debt test but that is often hard to do.
- The addition of rental assistance interfered with a project's AHP award. At the time of application for AHP grant funds, there was no rental assistance contract, but the deal ultimately closed with a commitment for Section 8. When the developer went to draw the grant, the bank decided the rental assistance contract made debt service feasible and forced the project to take a loan. Ultimately the bank allowed the project to move forward with an imbalance in the financials for the amount of the AHP draw, but the issue (which is now several years old) has not been resolved.
- In some cases, the additional compliance costs of an AHP award deter applicants from applying. Especially when an award is likely to be small relative to the overall project and the AHP compliance process is entirely separate from other subsidy sources, some mission-oriented developers will simply forego AHP entirely.

C. Allow multiple AHP allocation rounds in a year

Because AHP funds must fit into a patchwork of other funding sources within a given project, having a single funding round during the year is limiting. For example, since AHP awards are usually small when compared to LIHTC allocations, it would be logical for the AHP to adapt its calendar to those of the states it serves. That may not be possible in all instances, since the FHLBs span multistate regions, but greater coordination with state housing finance agencies could go a long way to reducing delays and to limiting missed opportunities. Furthermore, having more than one opportunity to apply and receive an award during the year may create opportunities to separate rental and homeownership projects so that each gets full attention from the FHLB.

D. Recycle awards to maximize impact

AHP loans often are, in effect, slow-fuse grants. If a property fulfills its affordability commitment for a set number of years, the FHLB forgives the loan. Other affordable housing gap lenders, however, tend to structure gap-fillers as soft loans with little or no payment required, maturity coterminous with the first mortgage, and a due-on-sale-or-refinancing clause. For most properties, recapitalization means going back to the soft lender to roll over the debt, which provides a natural opportunity to review

performance and adjust terms. For the rare property that is able to pay back the loan through a transaction, the result is more funds that can go back into affordable housing.

E. Allow more income-mixing and appropriate income targeting

Over time, the affordable housing community has come to see the benefits of mixed-income communities, while also recognizing the great need for housing affordable to those of lowest income. However, income targeting that preferences multifamily rental projects with a high percentage of very low income households is difficult to reconcile with other federal programs, such as HOME, CDBG and LIHTC, that set affordability thresholds at 60 percent or 80 percent of median income. Underwriting transactions to comply with overlapping program requirements and deep affordability targeting overly limits property income, particularly where there is no rental subsidy. That in turn limits the borrowing capacity of the sponsor and creates funding gaps and operational challenges.

A broader but a more flexible affordability requirement would allow each regional FHLB to attract a more diverse pool of affordable housing projects, including mixed-income projects, to better compete for AHP funds. We recommend that maximum points be awarded for projects where 100% of units are reserved for households with incomes at or below 80% of median income and the average income across all units does not exceed 60% of median income. As a point of comparison, the Treasury Department has for several years now proposed allowing the Low Income Housing Tax Credit program to be more compatible with income mixing, by proposing to allow a weighted average approach to tenant income limits rather than a strict 60% AMI ceiling. AHP regulations should allow more flexibility for each region to allocate funds with based on affordability requirements for rental properties that are more compatible with properties housing people with a range of incomes.

For homeownership projects, income restrictions are necessarily different. Somewhat higher incomes are both appropriate for homeownership and often necessary for residents' success. AHP should also recognize the importance of homeownership counseling in ensuring resident success. FHFA should ensure that the changes in AHP regulation allow for different income targeting for homeownership than for rental.

F. Recognize business imperatives for nonprofits in developer fees

Nonprofit housing developers and financial institutions face most of the same business imperatives as their for-profit counterparts, but affordable housing policy too often restricts their ability to operate as successful businesses. We are pleased that the current AHP regulation allows nonprofits to receive a developer fee from a project. We encourage FHFA to maintain this provision and strengthen it by allowing greater in-kind contributions by nonprofits to count in developer fee and equity calculations.

G. Encourage participation by nonprofit partners

The AHP could provide more support to the nonprofit development and CDFI partners who implement AHP development and financing. Outreach to nonprofits who work with the AHP program suggested several ways the FHLB programs could encourage increased activity.

First, simplifying and streamlining AHP applications would encourage more nonprofits to apply. Multiple nonprofit developers in Chicago, Illinois; St. Louis, Missouri; and Pittsburgh, Pennsylvania; have reported the application is confusing, burdensome, and a disincentive to apply. Ensuring that updated regulations give each FHLB the freedom to craft an understandable and accessible application would be valuable.

Second, the advisory boards are a critical access point to the program for nonprofit developers. Many banks do a good job of including nonprofits on these boards. However, some do not. Minimum representation by nonprofit organizations, including community-based nonprofit developers, CDCs and others, on the advisory board is critical to the program's success and credibility. In 2016, one bank has chosen not to have a local or regional nonprofit community development nonprofit organization on its board, although in the past the board has included such organizations. Nonprofits in the region feel this has led to housing counseling funds not being well targeted. We urge FHFA to encourage the use of advisory boards and ensure that there is a consistent local and regional nonprofit presence.

Third, training and direct technical assistance to nonprofit applicants during the application process directly encourages participation. Assistance could be provided by FHLB staff. Alternatively, an FHLB could facilitate training and technical assistance through member financial institutions that could receive CRA service credit for assisting nonprofit developers. Some FHLBs already provide this support and applicants have found it helpful. Updated regulations should encourage more training and technical assistance.

H. Encourage outreach to FHLB members to be active with AHP

FHLB members can be key partners in affordable housing development, beyond their contributions to the AHP, through the FHLB system. Greater outreach to FHLB members could stimulate more equity investment, provision of liquidity, volunteerism, and other involvement in affordable housing.

I. Make AHP more effective in rural areas

Several features of AHP are overly rigid in their requirements for rural projects, unnecessarily limiting what can be accomplished. For instance, the dollar for dollar match requirement can effectively disqualify rural projects with limited cash flow, limited or no rental assistance, and residents whose incomes are too low (at 30% of an AMI that is low to begin with) to contribute meaningfully to property operations. Absent enough cash flow to support significant debt, some rural projects also cannot secure member financial participation, which further disadvantages applications. For the projects that can secure a member loan, it is often small, which caps the amount of the AHP grant as well.

Additional flexibility would allow the AHP to serve a wider range of projects in rural areas. We are not recommending that the AHP grant more (or less) awards to rural projects. Rather, to the extent AHP awards go to rural projects, we recommend that the programs in each region do not unnecessarily limit the range of need they serve.

IV. Toward a stronger AHP

The Working Group sees this update of the regulations as an opportunity to strengthen the AHP and expand its reach and impact for affordable housing. We thank FHFA for the opportunity to offer suggestions and welcome further interaction as the agency develops the regulation. For questions on any of the matters discussed here, please contact Ethan Handelman, Vice President for Policy and Advocacy, National Housing Conference, 202-466-2121 x238, ehandelman@nhc.org.

Sincerely,

Enterprise Community Partners
Housing Partnership Network
Local Initiatives Support Corporation
National Alliance of Community Economic Development Associations
National Council of State Housing Agencies
National Housing Conference
NeighborWorks America
Stewards of Affordable Housing for the Future