March 10, 2022

Federal Housing Finance Agency
400 7th Street SW
Washington, DC 20024

Re: FHFA Strategic Plan: FY 2022 – 2026
Comment Letter

Dear Sir or Madam:

I am writing to offer comments on the proposed FHFA Strategic Plan, FY 2022-2026, Strategic Goal 2, Objective 2.4: Facilitate greater availability of affordable housing supply, including affordable rental housing.

I recommend that FHFA adopt an additional "means and strategies" to achieve this objective, as follows:

Monitor the market impacts of the Enterprises' conventional loan products to identify lending practices that may contribute to or accelerate the loss of affordable market rate properties; increase regulatory oversight or intervene, as appropriate.

I am a multifamily housing consultant and have held numerous senior management positions in the field of multifamily housing finance and affordable housing over the past 35 years at a state housing department and a state Housing Finance Agency, at Fannie Mae, at private mortgage banking firms, at the HUD/FHA mortgage insurance programs and at FHFA.

As a seasoned observer of and participant in the multifamily secondary market, I have long been concerned about certain of the Enterprises' conventional loan products, borrowers and lending practices that may erode the preservation of affordable, market rate rental units or accelerate their loss. While FHFA has used its regulatory authority to have the Enterprises better fulfill their mission obligations through specialized programs that finance (mostly subsidized) affordable housing, it has not focused on the probable negative effects of their conventional lending practices on the affordability of market rents. This seeming contradiction between the Enterprises' support for affordable housing while simultaneously operating conventional loan products that can undermine it should be addressed in FHFA's new Strategic Plan.

The primary reason for the lack of post purchase oversight is FHFA's practice of judging affordability based on rents in effect on the date of loan acquisition, with no post-purchase monitoring of borrowers or of properties that have been financed, except as it relates to safety and soundness concerns. Had it done so, FHFA would have seen that, concurrent with the Enterprises' support for subsidized affordable housing, they operate several conventional loan products that reward owners for raising rents, that promote consolidation to institutional ownership, that finance bad property owners, and, in the case of small multifamily properties, that potentially undermine the historic dynamics of this market segment. As a result, the Enterprises provide capital to many properties which may lose their rent affordability soon after being financed, despite FHFA having given them regulatory credit for the loan acquisition based on rents that were affordable at that time.

Of course, quantifying the exact effect that the Enterprises' lending practices may have on accelerating the loss of rent affordability is challenging due to rising market rents generally and since borrowers are private, for-profit owners who are not subject to rent restrictions as a condition of obtaining a USG backed loan. However, even if it is difficult to distinguish how much of the loss is due to the Enterprises' lending practices rather than the influence of broader market forces, certain of their practices and loan products can clearly be shown to accelerate the loss of affordable market rents and should be subject to greater scrutiny by FHFA.

The following are examples of some of the Enterprises' most pernicious conventional lending products and practices, including references to media reports which have drawn attention to their negative effect on renters.

Value Add Loan Products

Both Enterprises offer "value add" loan products that are specifically designed to finance property improvements that will support higher rents:

https://www.multifamily.loans/freddie-mac-value-add-loans

These are short term, floating rate, interest only loans that include financing for property upgrades and, per Freddie Mac, are "an excellent choice for investors looking to increase the marketability and profitability of their multifamily properties". Once the improvements have been completed and higher rents are in place, the loan can be replaced with long term financing that permits the owner to cash out equity in the property. While I do not know how many properties have been financed using this product, the loan is actually designed to promote gentrification and the loss of affordable rents in older properties. This would clearly seem to contradict the Enterprises' stated mission to provide long term, permanent financing that promotes and preserves affordable housing and should warrant intervention by FHFA.

Revolving Credit Facilities

Both Enterprises offer revolving credit facilities to institutional borrowers so they can acquire multiple properties and transition them to higher rents:

https://mf.freddiemac.com/docs/product/revolving_credit_facility.pdf

Per Freddie Mac, a credit facility is a: "real estate secured line of credit tailored to meet your specific needs, from short-term repositioning of transitional assets to portfolio acquisitions". ("Repositioning of transitional assets" means making property upgrades, boosting rents and renting to higher income tenants.) Credit facilities are floating rate, interest only, must have at least $100M in assets and are used almost exclusively by private equity firms and national REITs to acquire properties which are renovated and impose higher rents until they are refinanced with a permanent loan. Once refinanced, another property can be acquired using the revolving facility.

Credit facilities have long been used to consolidate the ownership of multifamily properties in the hands of fewer and fewer institutional buyers. In fact, these borrowers have received many of the Enterprises' largest loans and are their biggest customers despite having ample private capital available to them without the need for USG backed financing. The negative effect of this concentration of multifamily ownership on tenant rents and living conditions was predictable, as is discussed in this recent article:

https://www.propublica.org/article/when-private-equity-becomes-your-landlord

FHFA should examine the influence of credit facility financing on broader multifamily market trends and their effect on escalating market rents and deteriorating tenant living conditions.

Small Balance Loans

Starting around 2014, Fannie Mae and especially Freddie Mac adopted major initiatives to penetrate the small property finance market by offering loan products with almost the same lending parameters and terms as are available to larger properties. Those include higher leverage, nonrecourse, floating rate, interest only and equity cash out loans. Lending in this manner may affect the incentives for how small property owners care for and manage their properties and their tenant relations and set rents, or it could lead to disinvest if market conditions deteriorate. Historically, bank loans to small properties had required low leverage, recourse and principal amortization with limited cash out except to fund deferred capital needs. Today, the Enterprises have supplanted bank lenders as the dominate source of financing for the small property segment.

The recent Harvard report on the State of the Nation's Housing 2022 found that market rents are rising fastest in the small property segment (at page 24), that "B and C" quality properties with affordable rents are quickly disappearing (at page 36) and that the ownership of small properties is shifting from individuals to institutions (at page 29). While it is unknown if, or to what extent, the Enterprises' lending practices may be contributing to the recent changes in the small property market, which had been one of the last significant sources of affordable market rents, it is an issue that FHFA should closely examine.

Financing for Bad Owners

Unfortunately, the Enterprises' loan underwriting does not seem to effectively screen out bad owners who are poor stewards of the properties financed and who push rents and abuse tenants, and the actions of these borrowers do not appear to be monitored by the Enterprises' loan servicers and asset managers. Examples of this abound.

In 2016, Fannie Mae provided over $1B in credit facility financing for the Yes! manufactured housing communities which, at the time, was hailed as preserving workforce housing in 13 states.

https://www.fanniemae.com/newsroom/fannie-mae-news/fannie-mae-finances-its-largest-manufactured-housing-deal-and-supports-29000-families

However, since the financing, the management and operation of these communities has suffered, and residents have been squeezed by rising lot fees and deteriorating conditions:

https://www.washingtonpost.com/business/economy/a-billion-dollar-empire-made-of-mobile-homes/2019/02/14/ac687342-2b0b-11e9-b2fc-721718903bfc_story.html

In 2019, Freddie Mac provided almost $1B in total financing on very advantageous terms so the Kushner Companies could acquire multiple properties in the mid-Atlantic market:

https://news.yahoo.com/kushners-freddie-mac-loan-wasn-143527460.html?fr=sycsrp_catchall

Later that same year, the borrower was sued by the MD Attorney General for illegal property management practices and unsafe property conditions:

https://edition.cnn.com/2019/10/23/politics/maryland-ag-lawsuit-kushner-companies/index.html

More recently this same borrower, who is notorious for their aggressive tactics, began wholesale evictions of low- and moderate-income tenants after the pandemic eviction moratorium expired:

https://www.washingtonpost.com/business/2020/11/05/kushner-evictions-pandemic-westminster-management/

How much responsibility the Enterprises bear for the actions of bad owners who exploit or abuse tenants, but are otherwise current on their loan obligations, can be debated. However, asserting that they have no responsibility at all for overseeing an owner's actions after a loan has been acquired should not be an acceptable answer, especially for two companies with explicit public mission obligations in their Charters and which operate USG backed financing programs. FHFA should do more to monitor borrower performance, to require the Enterprises to adjust their borrower underwriting standards to screen out bad actors, to require their lenders and servicers to identify and intervene with bad borrowers, or to limit or ban the borrower's future participation in the loan programs, as necessary.

Thank you for considering my comments on the proposed FHFA Strategic Plan.

Sincerely,

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