March 9, 2023

Sandra Thompson, Director
Federal Housing Finance Agency
Constitution Center
400 7th Street, SW
Washington, DC 20219

Dear Director Thompson,

Thank you for inviting the Community Development Trust (CDT) to participate at the March 1st FHLBank System at 100 Roundtable (the Roundtable.) In addition to our October 13, 2022 FHLBank Comment Letter to the Federal Housing Finance Agency (FHFA), the following are CDT's supplemental responses to questions that were posed at the Roundtable meeting.

1. *What is the single most important change you would recommend to the FHLBanks' products and services? If you believe no changes are needed, explain why not. What public policy purpose would be served by your recommendation? How would it affect the safety and soundness and mission achievement of the FHLBanks?*

   CDT Response: The most important and effective change with an immediate impact would be for **all eleven FHLBanks to allow unrated, unenhanced tax-exempt bonds which finance affordable housing projects as acceptable collateral** for CDFI advances**.** A few FHLBanks accept tax-exempt bonds as collateral but others, including our FHLBank, classify them as general municipal bonds which are not acceptable collateral. We believe there would be a significant impact on affordable housing production by allowing tax-exempt bonds as collateral.

   Multifamily units created or preserved with tax-exempt bonds are a significant portion of the more than 100,000 low-income housing units produced each year under the LIHTC program. Unrated, privately placed bonds are permitted by most bond issuers since they significantly reduce project transaction costs and processing times as compared to rated, publicly issued bonds, thus freeing up capital that can be applied to other project costs to help make projects financially feasible. These project savings, in aggregate, help to create more affordable housing. In addition, bond funded loans typically support larger projects with a greater number of affordable units, and often involve the rehabilitation and preservation of existing projects, than do projects funded under the 9% LIHTC program.

   Both unrated tax-exempt bond funded loans with 4% LIHTC (which are not eligible for advances) and taxable interest loans with 9% LIHTC (which are eligible for advances) are secured by the exact same type of real estate collateral. In fact, loans on LIHTC properties are one of the most secure real estate loans with a minuscule foreclosure rate over the 35+ years of the program, whether the loan is bond funded or a traditional taxable interest mortgage. Given the superior credit quality of this collateral, there is no justification for permitting advances to CDFIs on taxable interest loans but not on tax-exempt bond funded loans that finance LIHTC properties.

CDT was an inaugural awardee of a $125 million allocation from the CDFI Bond Guarantee Program in 2014 and we worked with the CDFI Bond Fund to accept tax-exempt bonds as collateral for advances from the Federal Financing Bank (FFB). If tax-exempt bonds are acceptable collateral for Treasury's FFB program, they should be acceptable collateral for the FHLBanks, as well.

2. *What other changes, if any, would you recommend to the FHLBanks' products and services?*

   CDT Response: The FHLBanks should recognize that loans on subsidized affordable housing projects, especially on those that are supported by LIHTCs, are more secure and lower risk than are other types of loan collateral including market rate properties. For this reason, we recommend that the FHLBanks establish **higher advance ratios on loans that are collateralized by LIHTC properties** due to the higher credit quality of the collateral as well as the public purpose of the projects. Nor is there any rational reason why the advance ratios should differ among the FHLBanks since the performance of these loans and properties is excellent no matter which FHLBank region a LIHTC property is located. CDT's 24-year history of making performing loans on a wide variety of LIHTC properties, with a focus on smaller properties, demonstrates these assets' strong performance.

   During this review process of the FHLBank system we have been in discussion with many CDFI's and personnel working within the FHLBank system. We recognize the importance maintaining the safety and soundness of the FHLBank system in regard to the risks and constraints of supporting community development outside of housing. In regard to this, we believe a portion of each FHLBank's retained earnings should be used to provide annual equity investments and/or grants specifically to a FHLBank's CDFI and community bank members. These investments and grants could support CDFIs' work within and outside of the FHLBank system's traditional housing lending platform.

3. *Do the FHLBanks offer the right mix of products and services to members? What market segments are well-served by the FHLBanks' programs and services? What market segments are not well-served?*

   CDT Response: The FHLBanks were established to provide liquidity to larger commercial banks, which is the basis for most of their products and services. But the responses to FHFA's original request for comments show that the FHLBank system is vital for community banks and CDFIs, as well.

   While many FHLBanks do not unfortunately provide long-term advances to well-capitalized CDFI members, they do provide a variety of funding options to members which are crucial for management of a member's assets and liabilities. But what is less common is a clear recognition of the secure nature of multifamily affordable housing as collateral for these advances. Many times the FHLBanks general loan collateral programs seem like 'one size fit all' rather than offering specific lending programs which recognize the differences in loan collateral. The banks often default to either AHP grants or very modest reductions in interest rates on advances to support affordable housing lending rather than by expanding or adjusting their collateral requirements which would truly support this very secure lending activity.

4. *How do FHLBank members use advances and letters of credit? To what extent are they used to support affordable housing? Community and economic development?*

   CDT Response: CDFIs use FHLBank advances to help provide the capital for lending to affordable housing and community development projects. CDT is a CDFI that is solely devoted to affordable multifamily housing and community development lending so all its loans are mission driven.

   The lower cost of FHLBank advances as compared to alternative sources of capital permit CDFIs to provide lower rates to borrowers while also allowing CDFIs to earn sufficient income to pay operating expenses and grow their organizations. Lower borrowing rates also helps more projects to be financially feasible to fund. The main challenge of using FHLBank advances is the low advance ratios which force CDFIs to mix the advances with higher cost sources to fund a loan. For example, when a FHLBank advances only 75% of a loan amount, then the CDFI must fund the remaining 25% using other higher cost and more limited sources of capital, which will then be unavailable for other potential community development investments.

5. *How can the FHLBanks play a larger role in supporting affordable, equitable, sustainable, and resilient housing through their core business lines or with only limited subsidies (that is, beyond AHP)? Is there a role for pilot programs?*

   CDT Response: As discussed throughout this letter, the FHLBanks could play a larger role in supporting affordable housing by **accepting unrated tax-exempt bonds on affordable housing projects as collateral** and by **increasing advance rates, permitting 30-year loan terms and allowing subordinate loans on affordable housing as eligible collateral from well-capitalized CDFI's**. While CDT supports the research goals of pilot programs, we recommend the FHLBank system initially focus on the 'low hanging fruits' discussed in this letter and in our original October 13, 2022 Comment Letter.

   Making these suggested improvements would have an **<u>immediate impact</u>** in affordable housing. An example of an affordable housing property that we currently cannot finance because of our FHLBank's restrictions is a proposed 165-unit new construction community in suburban Atlanta affordable to low-income senior residents at 50% and 60% AMI levels. The project is sponsored by a Person of Color led development firm and requires a permanent $13 million unrated tax-exempt bond and a $1.7 million subordinate mortgage from CDT to help complete the capital sources. The credit profile is exceptionally strong with CDT only required to lend less than $15 million of the $50 million project.

The shortage of affordable housing nationwide is due to many factors, but one large contributor is the amount of capital required to develop projects. The AHP program has been vital to the creation of many units, particularly those which use LIHTC. CDT has been the permanent lender on many projects and the gap financing provided by AHP grants has helped many of them get off the ground. While AHP grants are a critical source of gap-filling capital, even if the available AHP dollars were doubled or tripled from their 10% level, there would be little impact on the nation's overall affordable housing shortage.

Given the substantial retained earnings of the FHLBanks, we believe the development and/or expansion of other programs outside of AHP grants could be beneficial to expanding FHLBank's involvement in affordable housing and overall community development. A pilot program that could be considered would be **providing equity investments and/or grants annually specifically to the FHLBank's CDFI and community bank members**. These investments and grants could help support a CDFI's work within and outside of the FHLBank system's traditional housing lending platform while not exposing the system to undue risk since the funding would be from a portion of the excess retained earnings of individual banks. In particular, equity capital and grant funding could assist CDFI's with capital required when utilizing FHLBank advances and providing needed community development capital outside the housing core of the FHLBank system.

6. *Should there be a common set of terms across the FHLBanks for some or all products? If so, what should those common terms be? If not, why not, and (when and) how should the terms differ?*

CDT Response: Affordable housing lending is needed throughout the nation and is supported by the strong credit quality of the collateral no matter where it is located. In addition to requiring all FHLBanks to accept unrated tax-exempt bonds on affordable housing projects as collateral, we do not believe there is any rational reason why the advance ratios for affordable housing loans on LIHTC properties should differ among the FHLBanks or be the same as typically more risky loans on market rate properties.

In fact, advance ratios and other favorable terms and products, such as 30-year term advances and subordinate loan collateral, for **<u>well capitalized</u> CDFIs should be equal to what is available to member banks**. However, the FHLBank's 'one size fits all' guidelines for CDFIs fails to differentiate between the financial stability and organizational capacity of mature CDFIs with large performing loan portfolios and a sole focus on affordable housing. These factors could justify a FHLBank applying different standards for advance ratios, etc. for CDFIs that have little capital, a limited track record, loan types with higher default ratios, and smaller portfolios as compared to a larger, well capitalized CDFIs.

7. *Should there be changes to the eligible types of collateral? What factors should be considered in determining the types of collateral the FHLBanks should be able to accept?*

   CDT Response: In addition to accepting unrated tax-exempt bonds as collateral throughout the FHLBank system, increasing advance ratios and allowing 30-year advances for well-capitalized CDFI's, our October 13, 2022 Comment Letter discussed permitting subordinate loans by CDFI members to help increase the supply of affordable housing. There is a broad need for gap financing in projects that even an expanded AHP program could not fill. As discussed in question five, CDT has immediate subordinate loan opportunities on affordable housing we cannot provide financing because our FHLBank does not permit subordinate loans as collateral from CDFI's. Some FHLBanks permit member banks to pledge subordinate loans as collateral but not CDFIs for reasons that are unclear which implies that CDFIs are somehow less capable of underwriting the real estate or of managing risk than are banks. This is simply untrue given CDFIs' long track record of success and demonstrated expertise in financing affordable housing. **Allowing CDFI's to pledge subordinate loans within established credit parameters on affordable housing properties would assist in housing creation and preservation** while not jeopardizing the safety and soundness of the FHLBank system.

8. *Are there other services the FHLBanks [could or should] provide to members such as training on various issues (such as cybersecurity) or hosting events through which members and others in the community can share ideas and information? To what extent are the FHLBanks doing this now? Are there areas in which they are uniquely qualified to provide assistance?*

   CDT Response: Advancing members provide full guarantees to the FHLBank which puts their balance sheets at risk. If the project collateral were to fail, the member would suffer the loss and must repay the FHLBank. As such, we hope that CDFIs can be seen as full partners within the FHLBank system based on our expertise in providing financing to help alleviate the nation's affordable housing shortage. We believe that all FHLBanks would benefit from regular engagement with their member CDFIs to discuss loan products that would benefit community development efforts but are within the limits of the FHLBank purpose and system. There could also be improved connectiveness of members across the FHLBanks by introducing CDFIs and community bank lenders to the larger banks and insurance companies to support each of their missions. For example, CDT's ability to grow depends on equity capital invested by many of the FHLBank's banking and insurance members. In turn, these members look to CDFIs to assist them in various community development initiatives.

9. *Are the Community Investment Program (CIP) and Community Investment Cash Advance Program (CICA) being appropriately leveraged? Are there barriers to greater participation and if so, what are they?*

   CDT Response: CDT's only experience with the Community Investment Program (CIP) has been through our FHLBank. While we appreciate the lower cost of advances available through CIP, small basis point reductions in rates won't substantially impact CDT's ability to finance affordable housing. A bigger impact on CDFIs would be to increase the advance ratios on CIP qualified loans, which would not affect the soundness of FHLBanks, particularly if limited to financing subsidized affordable housing. While CDT's FHLBank has been helpful in our use of CIP advances, the biggest challenge is the advances must be one-year or longer and must support recently closed loans. Often CDT does not need to borrow immediately after a loan has closed and does not need the capital until a later time. However, because everything that CDT does is mission focused, we believe that **all of CDT's advances, and those of similar CDFIs, should automatically be treated as CIP advances**.

10. *Other bullet points outlining the points you would like to discuss.*

   ***CDT Response*:** We wish that all FHLBanks would be equally supportive of their CDFI members' community development funding needs and be consistent in the products they offer to well-capitalized CDFIs and their banking members. The lack of consistency among FHLBanks creates an unequal playing field for CDFIs based solely on where they happen to be located. Like the Federal Reserve and Office of the Comptroller of the Currency's recent initiatives to modernize how Community Reinvestment Act assessment areas are determined, we believe that CDFIs such as CDT which are active nationwide should not be limited by the location of their incorporation or of their corporate office to determine their FHLBank affiliation. Instead, CDT should be able to work with FHLBanks in other regions where CDT lends if that FHLBank is more supportive of affordable housing products and lending.

Thank you for the opportunity to meet with FHFA to discuss how FHLBanks can better support CDFIs which finance affordable housing. We are available to elaborate on any of the recommendations in this letter or on our October 13, 2022 Comment Letter.

Best regards,

Joseph F. Reilly

Christopher Blair

Joseph F. Reilly
President and CEO
jreilly@cdt.biz
Phone: 212.271.5019

Christopher C. Blair
Chief Product Officer & Treasurer
cblair@cdt.biz
Phone: 212.271.5073

cc: Merilyn Rovira, CDT