Massachusetts
Housing
Partnership

160 Federal Street
Boston, Massachusetts 02110
Tel: 617-330-9955
Fax: 617-330-1919

www.mhp.net

March 31, 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 Massachusetts Housing Partnership (MHP) to participate in FHFA's *FHLBank System at 100: Focusing on the Future* roundtable discussion on March 3, 2023 in Washington, DC. The Federal Home Loan Bank (FHLB) system has an enormous opportunity to re-commit to its foundational mission to assist and enhance the financing of housing at all income levels, and I am pleased to offer the following recommendations in response to this initiative.

First, a brief introduction to MHP. The Massachusetts Housing Partnership was established as a quasi-public state agency in 1990 with a mission to expand the availability of affordable housing in Massachusetts. Since then, we have helped over 24,000 low- and moderate-income families to buy their first home and provided over $1.6 billion in financing for 26,000 apartments. Our primary source of capital is from banks, although we are also a Fannie Mae Multifamily Affordable Housing lender, an FHA MAP lender, and an FHA Housing Finance Agency Risk-Sharing lender. MHP is a Housing Associate of the Federal Home Loan Bank of Boston, where nearly all of MHP's funding banks are also members.

Based on our experience in financing affordable housing and in working with the banking industry over many years, we offer the following recommendations:

1) **<u>Provide Long-Term, Fixed Rate Advances with the Terms Needed to Finance Affordable Housing</u>**

   Reliable access to attractively priced long-term, fixed-rate financing is the most significant need of mission-based lenders like CDFIs and housing finance agencies. The Federal Home Loan Banks are uniquely well-positioned to provide this capital given their direct access to the capital markets and their mission, but terms vary significantly across the FHLB system.

   Affordable housing projects in particular need the stability of long-term, fixed-rate financing to avoid the risk that rising interest rates will threaten already tight operating margins. As an example, investors in federal Low Income Housing Tax Credit (LIHTC) projects require

fixed-rate financing with a term of at least 17 years to mitigate interest rate risk over the time that they own the property. While the majority of the FHLBs already offer fixed-rate terms of up to 30 years, available terms at other FHLBs can be as short as 10 years for CDFIs. Every FHLB should offer a 30 year advance term to facilitate the financing of affordable housing.

The availability of reasonably priced forward rate locks is also critical to the new production and substantial rehabilitation of affordable rental housing. Forward rate locks are typically required by construction lenders and LIHTC investors for affordable housing developments. Fannie Mae and Freddie Mac offer forward rate locks of 30 months or more with the option for at least one 6-month extension. Every FHLB should offer a minimum forward rate lock of 30 months with one 6-month extension to facilitate the financing of affordable housing developments.

Finally, amortization options should also be reevaluated. The maximum amortization schedule currently offered by the FHLBs is 30 years, but Fannie Mae, Freddie Mac, and FHA all offer 35 year amortizations for affordable housing loans because it substantially increases project feasibility. The FHLBs should offer a 35 year amortization option for advances supporting affordable housing. Further, for affordable housing loans that are match-funded using FHLB advances, the amortization schedules should be able to be customized to match the amortization of the underlying loan so that unpaid principal balances are matched over the loan term. All of MHP's bank advances (from several dozen banks) offer this amortization option for match-funded loans, and FHLB Atlanta does this as well with its Principal Reducing Credit advance product, but FHLB Boston and presumably a number of other FHLBs do not offer this option and that is an impediment to utilization.

2) **Update the Approach to Collateral Valuation, Especially for Affordable Housing**

Collateral requirements for advances are among the biggest impediments to borrowing from the FHLBs to support the financing of affordable housing. The FHLB system's approach to collateral valuation is unjustifiably conservative, especially for affordable housing developments. These developments have a different, lower risk profile than the broader multifamily housing asset class. For example, Low Income Housing Tax Credit properties have an annual foreclosure loss rate of less than 0.1%, but loans on these properties are often discounted by 25% or more by the FHLBs. Mark-to-market (MTM) requirements can dramatically increase these haircuts. The consequence, especially for mission-based lenders, is that it is simply infeasible to borrow from the FHLBs to finance affordable housing developments. Affordable multifamily properties should be treated as a distinct collateral asset class and incorporated into the FHLBs' collateral framework with higher collateral valuations reflecting their significantly lower risk profile.

As an example of the importance of this issue, the current collateral valuation/MTM approach was a deal-breaker in a proposed affordable housing advance program between FHLB Boston and a group of six New England Housing Finance Agencies. The program would have generated significant advance volume and supported deeply affordable projects with essentially risk-free 100% FHA-insured multifamily loans. At the time, FHLB Boston was requiring an 18% haircut, with an additional MTM requirement that would have increased the haircut to 35% or more in a rising rate environment. By contrast, the Federal Financing Bank, which does not take credit risk, accepted the identical collateral at par value with no MTM haircut. The collateral valuation approach of FHLB/FHFA, especially regarding MTM, made this program infeasible, without justification.

MTM requirements should not apply to long-term, fixed-rate affordable housing loans that: 1) are being held to maturity by the lender, and 2) have been match-funded by the FHLB with the FHLB advance collateralized by the underlying loan. In the highly unlikely event that the lender fails, the servicing rights can be transferred to another servicer while the advance stays in place. With appropriate structuring, the match-funding provides an effective hedge against interest rate risk, obviating the need for a MTM approach.

Also, the FHLBs should have a uniform approach to government and agency securities and credit enhancement products like U.S. Treasury securities, Agency MBS, FHA-insured multifamily loans, etc. where the risk profile of the collateral is not affected by geography. As but one example among many, collateral haircuts can be up to five times higher (ranging from 1% to 5%) for U.S. Treasury bonds depending on the FHLB, and this range can't be justified by the credit risk.

Finally, the FHLBs should help to facilitate the lending or donation of collateral by bank members to CDFIs and housing finance agencies to support their mission-based lending in return for potential CRA credit. We are aware of at least one example where a CDFI was able to take advantage of a loan or donation of collateral to help secure an FHLB advance, and this approach should be replicated across the system.

3) **Increase Funding for the Affordable Housing Program to 20% of Net Earnings**

The requirement to fund 10% of net earnings toward AHP is not sufficient given the public mission of the FHLB system and the extraordinary need for more affordable housing across the country. Over the 20 years from 1991-2011, the FHLBs contributed up to 28% of net earnings toward a combination of AHP and RefCorp payment obligations. An increase in AHP funding to 20% of net earnings is therefore sustainable, justified by the public privileges (explicit and implicit Government backstops, privileged regulatory status, etc.), and necessary to address the significant shortfalls in funding for affordable housing and community development across the country.

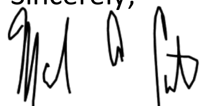
But more funding alone for AHP is not sufficient. The AHP programs are too complicated, and there needs to be a concerted effort to simplify the AHP requirements and allow AHP funds to be used more flexibly. For example, with a more defensible collateral valuation approach as a starting point, AHP funds could be used as pooled reserves to address specific risks in order to further reduce collateral requirements for mission-based lenders who are doing high-value affordable housing and community development work.

4) **Adopt a Robust Set of Housing and Community Development Goals**
For the FHLB system to re-commit itself to its foundational mission, a robust new set of housing and community development goals is needed to help stimulate innovation in the Banks' products so that FHLB members and housing associates can better address the housing and community development needs of their local communities. As an example, currently there are no goals related to FHLB advances for affordable rental housing. This lack of focus on the most critical housing need among low-income households is apparent in the FHFA's most recent report on the FHLBs low-income housing activities. In 2021, the eleven FHLBs collectively financed only 2,396 rental housing units under CIP, its targeted affordable housing program. This is a tiny fraction of the 44 million rental housing units in the US, and the required rents and incomes for those few units were far higher than what would be considered affordable for low-income renters by HUD.

The FHLB system has the resources and tools to have a major impact on affordable housing and community development finance, but frankly it is not living up to its full potential. This potential is unrealized because of overly conservative regulatory and credit policies that unnecessarily restrict access to debt capital for affordable housing and community development activities. These barriers to access are felt especially keenly among mission-based lenders, who have struggled to access the long-term, fixed rate financing that they need for affordable housing from the FHLBs despite the system's ready access to the capital markets.

Having provided over $1.6 billion in multifamily financing with no loan losses in our 30+ year history, MHP is truly excited by the prospect of working more productively with FHLB Boston and the FHFA to bring additional debt capital to affordable housing while appropriately managing risk. Thank you for the opportunity to participate and offer our recommendations as part of the *FHLBank System at 100: Focusing on the Future* initiative. I would be happy to discuss any of these recommendations further at your convenience if helpful.

Sincerely,



Mark A. Curtiss
Managing Director