July 21, 2023

Marcea Barringer

Federal Housing Finance Agency

400 7th St SW

Washington, D.C. 20024

RE: Freddie Mac and Fannie Mae Preparation for the 2025-2027 Duty to Serve Plan Cycle

Dear Ms. Barringer:

On behalf of National Housing Trust (NHT), thank you for the opportunity to provide comments as Fannie Mae and Freddie Mac (together, "the Enterprises") begin preparing the 2025-2027 Duty to Serve (DTS) plans. **We are writing to urge the Federal Housing Finance Agency (FHFA) and the Enterprises to promote housing stability and preserve the affordability of existing and future Low-Income Housing Tax Credit (Housing Credit) properties by upholding the Right of First Refusal (ROFR) and limiting the use of Qualified Contracts (QC).**

An estimated nearly half a million homes created and preserved through the Housing Credit program could be lost within the next decade due to the loss of affordability restrictions. Though many policies contribute to this potential loss, two existing policies in particular – the nonprofit right of first refusal (ROFR) and the Qualified Contract – must be addressed to better protect and preserve the long-term affordability of Housing Credit properties.

At NHT, we equip communities for a sustainable, equitable future by preserving and modernizing existing homes—and building new homes that stand the test of time. Our team of experts and advocates brings resident services, lending, policy, sustainability, and development under one roof, giving us the tools to make real change possible for the people we serve. As a result, we are able to offer "practice-informed" policy recommendations to local, state, and federal entities in support of developing and preserving climate-resilient, affordable, and secure housing nationwide.

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In previous years, NHT has provided detailed comments on FHFA's Duty to Serve proposed rule and the Enterprises' Underserved Market Plans. The following comments focus on issues related to the nonprofit Right of First Refusal. NHT has separately signed an industry stakeholder letter submitted to Director Thompson that details our position and recommendations to limit the use of Qualified Contracts.

Since 2018, NHT has led a national effort to uplift concerns that some Housing Credit investors are unreasonably limiting the use of the ROFR, therefore allowing Housing Credit properties to be too easily converted to market-rate housing. Due to ambiguities in the federal ROFR statute, further reflected in imprecise language in partnership agreements, numerous legal disputes have arisen across the country challenging the nonprofit partner's ability to exercise the ROFR.

NHT recommends both Enterprises adopt language and practices that protect both existing and new Housing Credit properties and support state and local Housing Credit allocating agencies by:

1. Identifying Housing Credit properties approaching Y15;
2. Providing technical assistance to nonprofits;
3. Adopting stricter investor eligibility; and
4. Expanding language in Partnership Agreements to include:
    - Protecting language that clarifies the nonprofit ROFR;
    - Clear actions that trigger the ROFR;
    - Clear calculation of the ROFR purchase price; and
    - A Letter of Intent to vet investor eligibility.

NHT's recommendations, as discussed in greater detail on page 5, are informed by the impacts of disputes to the nonprofit partner's ROFR in addition to the investor tactics systematically challenging the nonprofit partners' ROFR.

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Nonprofit ROFR Disputes are Impacting Housing Credit Properties and Residents

The ROFR is a lever in the Housing Credit program that allows nonprofit partners to gain full ownership of a property after 15 years of compliance. Nonprofit owners are often better positioned to provide long term affordability and services to low-income renters, making the nonprofit ROFR an important tool for promoting housing stability. When the nonprofit ROFR is challenged, these actions have wide-ranging impacts on the low-income residents who call Housing Credit properties home, in addition to nonprofit general partners who are committed to the long-term preservation of affordable housing communities.

For lower-income renters, many of whom face housing instability, housing provided through the Housing Credit program by mission-driven developers provides safe, stable, long-term affordable housing in addition to other supportive services. **Challenges to the nonprofit's right to exercise the ROFR threatens affordable housing and low-income residents by diverting critical resources from nonprofit developer owners, as described below. As a result, supportive services for residents are reduced, much-needed property maintenance is deferred, and staff capacity is strained. Moreover, the ambiguity surrounding the nonprofit's ability to exercise the ROFR creates uncertainty about the financial future of the affordable property.**

Systematic challenges of the ROFR also affect the financial viability of a nonprofit general partner. While a ROFR dispute with an investor is taking place (sometimes over several months or years due to drawn out negotiations or litigation), prudent management of the property is essentially frozen as the investor limits the general partner's ability to secure loans or otherwise raise funds to maintain quality affordable housing. As property reserves erode, a nonprofit partner experiences higher levels of debt and expenses accruing to their balance sheet. Private, profit-motivated investors know that most nonprofit general partners do not have the resources to litigate ROFR contractual issues in court.

While it may seem well-meaning to help a nonprofit avoid expensive litigation, private investors instead ask for a profitable cash payment (essentially a payout) or force the sale of the affordable property in return for leaving the partnership. When mission-driven developers are forced to spend limited reserves on legal feels or to pay the private investor directly to remove them from the partnership, few resources are left, leading some owners to sell their affordable housing portfolio and exit the affordable housing market altogether. This

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contributes to further housing instability for low-income residents. As real estate prices have soared across the country, these forced sales reap hundreds of millions of dollars in profit for investors who exploit the ROFR.[1]

These actions are both detrimental to the affordable housing industry *and* contrary to the original intention of Congress.

Investors are Systematically Challenging the Nonprofit Partners' ROFR

In 1989, Congress amended the Housing Credit program to permit Housing Credit partnership agreements between property owners to give nonprofits a ROFR to obtain full ownership of an affordable housing property after Year 15. **Congress took this action to encourage ownership by nonprofits for the purpose of maintaining rent affordability restrictions into perpetuity.** For most of the program's history, limited investor partners have exited the partnership at the end of the 15-year compliance period, as expected, and allowed the nonprofit general partner to obtain full ownership and continue to maintain the affordable housing in line with their mission. In recent years, as identified in Freddie Mac's DTS, outside investor parties are using certain tactics to disrupt this process.

As outside parties motivated solely by profits acquire control of investor partnerships in Housing Credit properties and begin to systematically challenge nonprofit general partner's exercise of the ROFR, the dire consequences resulting from the ambiguity in the federal ROFR statute have become clear. Limited partners have interpreted the ambiguous language in the federal ROFR statute to their benefit, extracting profits from affordable housing communities and precipitating a decline in the quality of housing for low-income families and individuals. Since 2016, there have been at least 47 instances of litigation on Year 15 / ROFR disputes across the country.[2] Some tactics typically used to disrupt the free exercise of the nonprofit ROFR include:

- Taking the position that the Section 42(i)(7) ROFR is the same as a common law right-of-first-refusal, including in the calculation of the ROFR purchase price and a bonafide third party offer.

[1] *Investors Mine for Profits in Affordable Housing, Leaving Thousands of Tenants At Risk*, WBUR (April 2021). https://www.wbur.org/news/2021/04/29/investors-low-income-housing-boston-south-end

[2] *LIHTC Court Rulings*, Novogradac (2022). https://www.novoco.com/resource-centers/affordable-housing-tax-credits/lihtc-court-rulings#rofr; in addition to written information provided by BC Davenport.

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  - A ROFR is not unique to the Housing Credit program and is often used in common real estate transactions, when afforded by a local ordinance. In these instances, the purchase price is calculated by the market. The ROFR in the Housing Credit program differs in that the price is set by the federal statute, not market price. This clearly establishes it as separate from the common law ROFR, with the statute identifying the ROFR purchase price as the sum of the property's outstanding debt plus taxes, yet disputes over the ROFR purchase price still occur.
  - Similarly, limited partners state that they are not required to recognize the rights established in the partnership agreement without a bonafide offer from an unrelated third party. As clearly stated in Section 42(i)(7), a nonprofit partner holds the right to purchase the building through a ROFR after the close of the building's 15-year compliance period, thereby negating any serious or bonafide offer to purchase by a third party.
- Disputing the conditions and scope of transfer rights.
- Delaying, obstructing, and disagreeing with related valuations.
- Refusing consent to refinance, either outright or by placing significant conditions on consent.
- Disputing fee calculations.
- Arguing over typographical errors.
- Asserting alleged breaches of partnership duties from many years prior, including by arguing that rents should have been set higher to maximize profits.
- Alleging breach of fiduciary duty by the nonprofit general partner.

These tactics have become more frequently utilized over time, represented by the growing number of cases that address ROFR disputes between investor parties and nonprofit developers. This is to the great detriment of nonprofit affordable housing developers around the country who share the Enterprises' goal of preserving affordable housing.

NHT Recommendations to the Enterprises to Strengthen Nonprofits' ROFR

In light of these conditions, we are pleased to see Freddie Mac's intent to better support non-profit ownership at the end of the Housing Credit compliance period and the inclusion of language in partnership agreements that protects nonprofits' ROFR. NHT agrees that it will largely affect only new transactions.

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To best address the growing problem, we urge both Enterprises to adopt language and practices that protect both existing and new Housing Credit properties. The following policy and programmatic recommendations were developed in partnership with state and local Housing Credit allocating agencies from across the country.

For existing properties, NHT recommends that the Enterprises:

1) Support early intervention to identify properties approaching Year 15. This should include but not be limited to encouraging Housing Finance Agencies, in collaboration with nonprofit developers and advocates, to identify Housing Credit properties between years 10 - 14 and whose ownership partnership includes certain profit-motivated private investors.

2) Provide technical assistance to nonprofits. This should include reviewing partnership agreement language to ensure that nonprofits are aware of and better understand their rights and ability to exercise ROFR; creating a checklist for review ahead of a property reaching Year 15 of how to prepare to exercise and execute the ROFR; and providing support and resources if a dispute arises.

3) Adopt stricter investor eligibility. If equity providers who have actively sought to interfere with or defeat a ROFR face regulatory sanctions impeding their ability to do new business with a state or the Enterprises, this should cause them to consider modifying their practices with respect to existing properties. Therefore, the Enterprises should cease to conduct business with entities that have challenged a nonprofit's right to exercise the ROFR in any state or jurisdiction within the United States.

For future partnership agreements, NHT recommends that the Enterprises:

1) Strengthen protections through language that makes clear that the nonprofit ROFR cannot be conditioned upon receipt of a bonafide offer from any party, including a third party. This should include clarification that the ROFR outlined in Section 42(i)(7) is not the same as a right of first refusal under statutory, court-interpreted, or common law.

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2) Incorporate language that provides the general partner or managing member the power and authority to take any actions that could trigger and accept the nonprofit's right to purchase under the ROFR and to close on the sale of the property to the nonprofit. The language should affirm the ability of the general partner to act on behalf of the partnerships/company after the end of the compliance period, , and without the need to obtain the consent of the investor.

3) Clarify that the ROFR purchase price is calculated as the minimum purchase price permissible under Section 42. This ROFR purchase price should not automatically include unpaid fees or loans and should be calculated by the project accountants and deemed final other than due to manifest error.

- This is important because it is a common tactic of investors to object to the calculation of the ROFR price as a means of stalling and leveraging a payment by the general partner. The amended language would preserve that right while removing a point of investor leverage to object to the accountant's calculation of the ROFR purchase price.

4) Require a Letter of Intent to vet investor eligibility that includes written acknowledgement by potential investors or syndicators at the beginning of a Housing Credit partnership regarding past ROFR activity. Such a letter would affirm that they have never sought to achieve early termination of a Housing Credit extended use agreement through the qualified contract process, nor have they sought to undermine the exercise of the nonprofit ROFR.

To date, at least 21 allocating agencies[3] have adopted, in part or whole, the language outlined above to ensure nonprofits can exercise the ROFR to protect long-term affordability, and we encourage the Enterprises to do the same.

In addition to protecting and strengthening the nonprofit ROFR, NHT would also like to acknowledge our long-standing support of policies and actions taken to limit the loss of affordable housing through the qualified contract (QC) process. As the National Council of State Housing Agencies (NCSHA) has noted in its previous

[3] These specific allocating agencies represent the following jurisdictions: CA, CO, GA, ID, IN, ME, MA, ME, NV, NH, NJ, NY, New York City, OR, PA, RI, TN, VT, VA, WA and Washington, D.C.

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written and oral comments provided to FHFA and the Enterprises, and as is included in the separate industry stakeholder letter which NHT has signed, the qualified contract provision results in the loss of approximately 10,000 affordable homes annually.

We support the recommendations outlined in the industry stakeholder letter and encourage Fannie Mae and Freddie Mac to set policies of investing only in properties in which the owners have waived the right to a qualified contract, consider preservation concerns such as qualified contracts as part of the criteria used to determine which loans to purchase, and assist preservation-oriented buyers willing to make an offer to purchase a property at the qualified contract price.

NHT encourages the Enterprises to recognize in writing *both* qualified contracts and challenges to the nonprofit ROFR in their respective DTS plans to demonstrate a commitment to the long-term preservation of existing affordable housing. We also encourage Fannie Mae and all investor partners of both Enterprises to adopt the language that Freddie Mac has developed, in addition to our recommended suggestions, in partnership agreements involving nonprofit general partners. We believe that the Enterprises can play an important role in protecting the long-term affordability of these properties by limiting the availability of qualified contracts and strengthening the nonprofit ROFR.

Finally, NHT acknowledges that the ultimate cure to both QC and ROFR challenges is federal legislation that closes the QC loophole and affirms a nonprofit ROFR. Such legislation was included in the 2021 Build Back Better Act but did not gain the broad support necessary for passage. Support from FHFA and the Enterprises would help in highlighting these critical issues to Congress.

Thank you for the opportunity to share our expertise.

Sincerely,

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