National Community Stabilization Trust

October 27, 2017

The Honorable Melvin Watt
Director
Federal Housing Finance Agency
400 7th Street S.W.
Washington, DC 20024

RE: Comment on Federal Housing Finance Agency Strategic Plan: FY 2018-2022

Dear Director Watt:

Thank you for the opportunity to comment on the Federal Housing Finance Agency's (FHFA) Strategic Plan for Fiscal Years 2018-2022 (Strategic Plan).

The National Community Stabilization Trust (NCST) is a non-profit, non-partisan organization that works to restore vacant and abandoned properties to productive use and to protect neighborhoods from blight. Our programs facilitate the rehabilitation of vacant but structurally sound homes, enable safe, targeted demolition when needed, and support creative and productive re-use of vacant land. Established in 2008, NCST offers a unique blend of policy expertise and on-the-ground experience, and since our founding, we have worked with local partners across the nation to address the needs of more than 23,000 properties.

A flagship project of NCST's REO acquisition program is the Neighborhood Stabilization Initiative (NSI), which is a partnership with Fannie Mae and Freddie Mac to offer their REO properties through a special First Look program in 18 strategic markets around the country. FHFA has played a critical role in ensuring the launch and ongoing success of the NSI program. Through NSI, NCST has become familiar with the Enterprises' REO operations and activities in distressed markets.

NCST commends FHFA for including neighborhood stabilization in its Strategic Plan. We are grateful for FHFA's continued support for the responsible disposition of distressed REO properties through the NSI program, as well as the inclusion of the Community Impact Pools in the nonperforming loan auctions.

However, as we have noted previously in various public comments, NCST believes that the Enterprises can do more to provide access to flexible, affordable capital for the nonprofit community developers working in distressed areas. For still-troubled housing markets to recover, these neighborhoods need more non-distressed sales to take place and need safe and habitable homes available for sale to low- and moderate-income families. Many of these families are not in a position to acquire a distressed home and rehab it themselves, plus sales of distressed properties do not help create non-distressed comps. Thus, acquisition and rehab of distressed properties by intermediaries such as nonprofit community development corporations or other mission-oriented developers is critical both to support higher appraisals and to address the growing shortage of affordable for-sale inventory.

Conversely, Enterprise policies and programs that facilitate the transfer of distressed properties to any buyer willing to purchase them, regardless of what happens next, is likely to undermine the effort to support housing markets and communities. Many cash buyers and other investors never rehab distressed properties, instead either renting them in substandard condition or simply holding them in the hope that property values will rise.

We know that FHFA is aware of this dynamic and has asked the Enterprises to consider a number of issues related to the ongoing problem of troubled markets and access to affordable inventory. However, we would like to see some of these activities included in FHFA's public strategic plan:

- Promote Enterprise investment in CDFIs that finance nonprofit acquisition and rehab of distressed properties.
- Direct the Enterprises to develop renovation products specifically geared to community development nonprofits and other stabilization-oriented developers.
- Require the Enterprises to pilot new approaches that encourage lenders to make small-balance mortgages.
- Focus Enterprise support for single-family rental on safe, habitable, and most important, affordable rental, especially rental offered by non-profit or other mission-focused landlords.

Below, we provide more details on these four activities.

I. Promote Enterprise investment in CDFIs.

The reality of community-focused development is that many mainstream banks and other sources of market financing are unavailable or uninterested. Community Development Financial Institutions (CDFIs) provide an alternative source of financing for development in these distressed communities. Prior to 2008, Fannie Mae and Freddie Mac provided support for CDFIs in a variety of ways. However, since the inception of the conservatorship, FHFA has restricted the Enterprises from investing in CDFIs.

NCST believes that FHFA should not only permit, but encourage, the Enterprises to resume investing in CDFIs (as well as other nonprofits, land banks and Housing Finance Agencies) that support mission-focused developers seeking to acquire, rehab and resell or rent vacant single-family properties. Direct investment by the Enterprises in CDFIs will more efficiently and effectively increase the access to capital that these organizations currently lack. Providing significantly increased access to low or market rate funding for nonprofit affordable housing developers will encourage scalable operations, which in turn would enable those developers to access trades or materials with negotiated terms and/or payments that would lower their total development cost.

II. Direct the Enterprises to create renovation products accessible to and designed for community development nonprofits.

Acquisition and rehab developers require a specifically tailored program with terms and parameters consistent with how the acquisition and rehab business actually operates, regardless of whether the goal is resale to an owner-occupant or short- or long-term affordable rental. Renovation products designed for individual homebuyers do not match the need from the developer side.

For example, underwriting for single family housing acquisition and rehab developers is different from underwriting individual homebuyers, and it does not appear that a robust infrastructure is in place for nonprofit organizations to be manually underwritten for currently available loan products. Also, both Fannie Mae and Freddie Mac currently cap the number of loans that any one borrower can hold, and those caps apply to community development nonprofits as well as to individual investors. For organizations working at scale, the caps can be a problem in rehabbing for-sale properties; for organizations looking to build long-term single-family rental portfolios in distressed neighborhoods, being limited to 6 or 10 loans at any given time is simply unworkable.

While it is true that long-term mortgages are not the ideal financing for projects where a nonprofit is looking to acquire-rehab-resell quickly to an owner-occupant, a properly tailored product could make a significant difference for those who cannot obtain appropriate short-term financing. Plus, property-by-property mortgages tailored to meet the needs of nonprofit developers do make sense for single-family acquisition-rehab-long-term rental projects. Some of NCST's community buyers already hold rental portfolios, and our research indicates that more would like to.

To address this need, NCST believes the Strategic Plan should include direction to the Enterprises to develop acquisition and rehab financing products for nonprofit housing developers that account for the different underwriting processes needed to evaluate these entities. NCST's buyers have already indicated that, for such a product to work it would need to have increased loan-to-value ratios, more flexible underwriting and a higher ceiling on the number of loans permitted.

III. Require the Enterprises to pilot ways to encourage lenders to make small-balance mortgages.

Another identifiable need in the neighborhood stabilization financing space is the lack of access to financing for small-balance mortgages in many markets, including smaller markets, distressed areas, and rural areas. NCST has conducted extensive outreach with our network of nonprofit and community-oriented buyers who tell us that this problem is widespread and disrupts the acquisition-rehab-resale cycle at many junctures.

Mortgage lenders, particularly large national banks, have never originated $50,000 mortgages (or in some markets, even $100,000 mortgages) at remotely the same scale as they originate larger mortgages, but in recent years, according to the Urban Institute, the numbers have dropped even more.[1] This credit gap has a disproportionate effect on distressed areas where property values remain low and even larger homes sell for fairly low prices. Not only does lack of access to credit provide an obstacle to homeownership, but it also opens the doors to predatory products that can leave families significantly worse off, such as land installment contracts.

NCST recommends that efforts to address this problem be included in the FHFA Strategic Plan. It is also noteworthy that small balance loans are often a specialty of CDFIs and HFAs, so the investment opportunities discussed above could also help to address the access to small balance credit problem that continues to cripple distressed housing markets.

IV. Focus Enterprises support for single-family rental on safe, habitable, and affordable rental homes, especially those offered by nonprofit and other mission-oriented landlords.

Despite the work being done by both Enterprises around the issue of single-family rental, this topic is not mentioned in the Strategic Plan. More than half of all renters currently reside in

[1] Ellen Seidman, "Where Have All the Small Loans Gone," (Urban Institute, 4/18/2017), available at http://www.urban.org/urban-wire/where-have-all-small-loans-gone

single-family homes (defined as properties with one to four living units).[2] In many neighborhoods, single-family homes constitute the greatest source of naturally occurring affordable rental housing. Unfortunately, current record-high rents and a shortage of units enable landlords – who are often remote investors – to rent out distressed properties without any market pressure to repair them. In some instances,[3] owners of distressed properties pass off their responsibility to maintain rental units onto the tenants under the guise of predatory products such as "rent-to-own" schemes or land installment contracts.[4] Unscrupulous investors are further aided by online auction sites,[5] which enable people around the globe to source low-value properties[6] on the cheap, either collecting rent payments until the home falls apart[7] or simply waiting until home values rise to flip them.

Recently, Fannie Mae's multifamily division ventured into providing government backed liquidity to large institutional investors to allow them to purchase thousands of single family homes for rental – approved by FHFA.[8] Unfortunately, this transaction did not contain affordability requirements of any kind, and the affordability profile of this deal significantly lagged the overall Fannie Mae multifamily portfolio.

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[2] U.S. Census Bureau, "Historical Census of Housing Tables," available at https://www.census.gov/hhes/www/housing/census/historic/units.html

[3] Alexandra Stevenson and Matthew Goodstein, "Rent-to-Own Homes: A Win-Win for Landlords, a Risk for Struggling Tenants," *New York Times: DealBook*, August 21, 2016, available at https://www.nytimes.com/2016/08/22/business/dealbook/rent-to-own-homes-a-win-win-for-landlords-a-risk-for-struggling-tenants.html

[4] Sarah Edelman, Michela Zonta and Julia Gordon, "Lease Purchase Failed Before – Can It Work Now?" (Washington: Center for American Progress, 2015), available at https://www.americanprogress.org/issues/economy/reports/2015/04/29/112014/lease-purchase-failed-before-can-it-work-now/

[5] Christopher E. Herbert, Irene Lew and Rocio Sanchez-Moyano,"The Role of Investors in Acquiring Foreclosed Properties in Low- and Moderate-Income Neighborhoods: A Review of Findings from Four Case Studies," (Joint Center for Housing Studies, Harvard University, 2015), available at http://www.jchs.harvard.edu/sites/jchs.harvard.edu/files/w13-11_herbert_lew_moyano.pdf

[6] Justin Weir, "Out-of-state homeowners hinder fight on blight," (Youngstown, Ohio: *Vindicator*, September 25, 2016), available at http://www.vindy.com/news/2016/sep/25/out-state-homeowners-hinder-youngstowns-fight-blig/?print

[7] Frank Ford, *et al.*, "The Role of Investors in The One-To-Three Family REO Market: The Case of Cleveland," (Joint Center for Housing Studies, Harvard University, 2013), available at http://www.jchs.harvard.edu/sites/jchs.harvard.edu/files/w13-12_cleveland_0.pdf

[8] Allison Bisbey, "Invitation Homes Obtains Financing from Fannie Mae," *National Mortgage News*, January 26, 2017, available at https://www.nationalmortgagenews.com/news/invitation-homes-obtains-financing-from-fannie-mae

NCST recommends that FHFA's Strategic Plan address the severe abuses and waste taking place in the single family rental market and direct the Enterprises to explore how best to support single-family rental to provide better affordability, habitability, and tenant protections, including how to provide appropriate financing for nonprofit and other mission-oriented landlords.

Conclusion

We appreciate the opportunity to comment on the Strategic Plan and FHFA's consideration of the above recommendations. Please let us know if you have any questions.

Sincerely,

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