Federal Home Loan
Bank Seattle

1501 Fourth Ave., Ste. 1900
Seattle, WA 98101-1693
206.340.2300 tel
206.340.2485 fax
www.fhlbsea.com

April 26, 2006

Shelia Willis
Secretary to the Board
Federal Housing Finance Board
I625 Eye Street N.W.
Washington, DC 20006-4001

RE: AHP Proposed Rule

Dear Ms. Willis,

The Federal Home Loan Bank of Seattle (Seattle Bank) appreciates the opportunity to comment on the proposed rule on Affordable Housing Program (AHP) Amendments published in the Federal Register on December 28, 2005, 70 FR 76938. Overall, we believe that the proposed changes are helpful and should improve the administration of the AHP. However, we are disappointed that the proposed rule does not address a need highlighted in the *Report of the Horizontal Review of the Affordable Housing Programs of the Federal Home Loan Banks,* issued by the Federal Housing Finance Board (Finance Board) on March 15, 2005. The report recommended that each Federal Home Loan Bank (FHLBank) be allowed to establish a scoring methodology based on the housing needs of its district. We encourage the Finance Board to address this concern as soon as possible to further enhance the AHP's effectiveness in serving the low- and moderate-income housing needs in our districts.

The proposed rule notes that it was intended to address seven principal factors. Our specific comments on the changes proposed in each of the seven categories are provided for your consideration.

1. DEFINITIONS

A. "**Affordable**" would be revised to make it clear that it references the amount of rent charged to the household, not the rent charged by the landlord. This is an important distinction for projects receiving rental subsidies, whereby the unit rent exceeds that which is paid by the tenant. The proposed rule would also add a new paragraph to clarify that rents charged under Section 8 are "affordable" for AHP purposes, so long as the rent met the AHP definition of "affordable" upon initial occupancy. Although the preamble to the proposed rule states that "rent charged to the household" would be defined to mean "the rent that is actually paid by the household occupying the unit," this clarifying language was not included in the revised regulation (951.1).

The Seattle Bank encourages the Finance Board to include this distinction in the definition itself. Additionally, the Seattle Bank recommends that language comparable to the HUD Section 8 provision be included for the USDA's Rural Rental Assistance Program. This allow the definition of "affordable" to include "rent charged to a household for rental units subsidized with USDA authorized rental subsidies under the Rural Rental Assistance Program (7 CFR 3560) if the rent complied with this section 951.1 at the time of the initial occupancy and continues to comply with USDA requirements for rental subsidies under the Rural Rental Assistance Program."

B. "AHP Project" would be revised to make it clear that the term is applicable to the competitive application program only. Currently, the regulation implies that this term also applies to the homeownership set-aside program. The proposed regulation also makes "conforming" changes to the definitions of "owner-occupied project" and "rental project."

The Seattle Bank supports this proposed change, but requests that either the regulation or the preamble make clear that it is possible that a project may be both an "owner-occupied project" and a "rental project." For example, a project might involve both a multifamily building and an owner-occupied building. In addition, we would request further clarity in terms of proper scoring, feasibility analysis, and monitoring for these types of mixed projects.

C. "Retention Period" would be revised to clarify that, in the case of rehabilitated units that are currently occupied and do not involve a closing, the retention period would begin on the date of the completion of the rehabilitation. Currently, the retention period for owner-occupied projects extends to five years from the date of closing.

The Seattle Bank supports this change but suggests that the definition be modified to read "5 years from the date that the FHLBank determines that rehabilitation has been completed."

2. Reorganization of the Regulatory Text

The Seattle Bank agrees that the separation of the competitive application program and the homeownership set-aside program into different sections in the AHP regulations is helpful in understanding the requirements of each program.

3. Revolving Loan Funds and Loan Pools

The proposed rule would permit AHP funds to be used for these purposes. Both the initial loans made by a loan fund or loan pool and subsequent loans made with amounts received from repayments of the initial loans must meet all "applicable" eligibility requirements. The initial loans must meet the commitments in the approved application for the full AHP retention period (five years for owner-occupied housing and 15 years for rental). Any subsequent lending of repaid AHP subsidy must be used for: (1) owner-occupied projects for households at or below 80 percent of area median income or (2) rental projects in which at least 20 percent of the units are set aside for households at or below 50 percent of the area median income. The subsequent lending will be subject to the AHP retention period, as well as to the monitoring and recapture requirements that the FHLBank must adopt. The revolving loan fund will return to the FHLBank any repaid AHP funds that are not used according to the requirements.

The Seattle Bank has not had sufficient time to fully analyze the implications of permitting the use of revolving loan funds and loan pools, but in light of the permissive nature of the regulation, does not oppose its inclusion in the proposed regulation.

4. **Use of AHP Funds on Projects Outside the District**

The proposed rule would prohibit an FHLBank from having an eligibility requirement or scoring preference for projects located in their district.

The Seattle Bank does not support this proposed change because we have learned that, during times of scarce resources, our members, sponsors, Affordable Housing Advisory Council (Advisory Council) and Board of Directors generally prefer to invest AHP resources within the district. The current regulation provides an effective tool for enabling FHLBanks to meet the needs of their members, sponsors, and communities, and the Seattle Bank does not believe that this proposed change would enhance the program. Additionally, out-of-district projects may impose expensive monitoring requirements such as site visits. They also expose the FHLBanks to greater risk because they may be sponsored by organizations and located in markets with which the FHLBank may not be familiar and for which the AHP implementation plan may not have established benchmarks or other tools for conducting feasibility review.

5. **Removal of Authority to Accelerate AHP Contributions from the Following Year**

The provision that allows for AHP funds to be borrowed from future earnings would be eliminated because it has been seldom used and may present operational difficulties. Specifically, it requires an FHLBank to project future earnings, and those projections may not be accurate.

The Seattle Bank does not accelerate funds for AHP for the reasons mentioned in the proposed rule. Thus, the Seattle Bank supports this change.

6. **Removal of Automatic Adjustment to the Maximum Dollar Amount Permitted Under the Homeownership Set-Aside Program**

Currently, there are maximum dollar amounts that may be allocated to the homeownership set-aside program, and these amounts are adjusted annually by the Finance Board to reflect any percentage increases in the preceding year's Consumer Price Index (CPI). The CPI adjustment would be eliminated because it has the potential, over time, to increase the amount allocated to the homeownership set-aside program at the expense of the competitive application program. The proposed rule would also simplify the requirement that a portion of the set-aside be for first-time homebuyers by specifying that "at least one-third" of the total set-aside be allocated to this program.

The Seattle Bank's practice has been to set aside 35 percent of its annual AHP contribution for the homeownership program, rather than a set amount. The Seattle Bank's set-aside program is used exclusively for first-time homebuyers. Thus, the proposed changes are consistent with the Seattle Bank's current practices and the bank has no objection to these changes.

7. Risk-Based Monitoring

A. Monitoring Requirements for AHP – The proposed rule would retain the current requirement for annual certifications by rental project owners under the competitive application program, but would make a number of changes to the monitoring provisions under both the competitive application and homeownership set-aside programs. A number of the current monitoring provisions are prescriptive in nature and set deadlines by which an FHLBank and other parties must undertake certain actions. The proposed rule would replace those provisions with more broadly stated performance objectives, which are intended to allow the FHLBanks greater latitude in determining the type and frequency of reports and certifications that are best suited for monitoring a particular project's compliance with the AHP rules. The proposed amendments would accomplish this goal by requiring the FHLBanks to adopt policies and procedures for monitoring progress to project completion and compliance with other AHP requirements.

The Seattle Bank supports this change.

B. Reliance on Other Monitoring – The proposed rule would expand the ability of the FHLBanks to rely on the monitoring of AHP-assisted rental projects by other governmental agencies that are providing tax credits or other funds to the projects, provided that the income targeting, rents, and retention period requirements monitored by such entities for their own programs are substantially the same as, or more restrictive than, those committed to in the approved AHP application.

The Seattle Bank supports this change. However, we recommend that 951.7 be modified to acknowledge the ability to rely on the monitoring of a state-designated housing credit agency with respect to low income housing tax credits "irrespective of their income eligibility standard," as noted in the preamble of the proposed regulation.

8. Other Changes

A. Advisory Councils

(1) Terms – The proposed rule would revise the current requirement that Advisory Council members serve three-year terms to allow members to serve "up to" three years. This would allow some members to serve terms of one or two years, which would decrease the likelihood that more than one-third of Advisory Council members' terms would expire in a given year. The proposed regulation would also require that policies and procedures be adopted regarding the appointment process.

The Seattle Bank supports these changes to the proposed rule.

(2) Officers – The proposed rule would require that there be a chair and vice chair of the Advisory Council. Currently, the Advisory Council is not required to have officers.

This is consistent with the Seattle Bank's current practice, and the Seattle Bank supports this change.

(3) **Duties** – The proposed rule would specify the duties of the Advisory Council to include providing recommendations on: (1) the amount of subsidy to be allocated to the competitive application and homeownership set-aside programs; (2) adoption of the AHP implementation plan and any amendments; (3) scoring criteria and related definitions for the competitive application program; and (4) eligibility and other requirements for the homeownership set-aside program. Currently, these duties are not specified.

This is consistent with the Seattle Bank's current practice, and the Seattle Bank supports this change.

(4) **Annual Report** – The proposed rule would extend the due date from March 1 to May 1 for the annual housing report from the Advisory Council to the Finance Board and require that it be publicly available on the FHLBank's Web site 30 days after submission to the Finance Board.

The Seattle Bank supports this proposed rule.

(5) **No Delegation** – The proposed rule would prohibit an FHLBank's board of directors from delegating to management its responsibility for appointing or meeting with the Advisory Council.

The Seattle Bank supports this clarification.

B. Competitive Application Program

(1) Eligibility Requirements

(a) **Rental Housing** – For projects involving the purchase or rehabilitation of rental housing that already is occupied, a household must have an income meeting the income targeting commitments in the approved AHP application at the time the application is submitted (951.5(c)(1)(ii)).

This requirement would make it very difficult for a sponsor to use the AHP to acquire an occupied building with the intent of changing the income configuration of the units. For example, a sponsor may wish to purchase an existing building that is currently 90 percent occupied by households at 60 percent of area median income and 10 percent occupied by households at 50 percent of area median income. Because the incomes must meet those targeted in the AHP application "at the time the application is submitted," this project would not meet AHP's minimum eligibility requirement that at least 20 percent of the units serve households at or below 50 percent of area median income. In this example, the sponsor would agree to meet the 20 percent at 50 percent requirement within a year through normal turnover or by not renewing some leases. A similar scenario could apply to a sponsor who wishes to acquire a building with market rate units and convert all or a portion to affordable housing.

As such, the Seattle Bank asks the Finance Board to consider, for projects involving the purchase or rehabilitation of rental housing that already is occupied, allowing a household to have an income meeting the income targeting commitments in the AHP application either at the time of application or before first disbursement of funds. FHLBanks would require evidence at application of a reasonable plan to meet the proposed targeting within one year of approval or prior to first disbursement of funds.

(b) **Project Costs** – The proposed rule revised the language from requiring project costs to be reasonable "in accordance with the Bank's project feasibility guidelines" to requiring them to be feasible "in accordance with the Bank's project costs guidelines." The proposed rule also adds a requirement that these guidelines take into consideration "other non-financial or household characteristics."

The intent of this change is unclear. If the intent is to require FHLBanks to establish cost guidelines for various line items on a development budget and to make those cost guidelines specific for the type of housing proposed, the FHLBanks' guidelines would be voluminous and cumbersome for members and sponsors to apply to their projects. Additionally, there is such a range of costs for various types of projects that it would be inefficient to attempt to anticipate all of the various needs of a particular project. For example, a special needs project for residents with severe disabilities would require special features for mobility and safety. Would separate cost guidelines be needed for a similar project in which half of the occupants were severely disabled and the other half had greater mobility? What about another project in which 20 percent of the units were reserved for people with special needs, and the types of special needs varied? If the Finance Board's intent is not to complicate evaluating project costs, then the Seattle Bank respectfully requests that this language not be revised.

(c) **Project Feasibility/Development Feasibility** – The proposed rule adds a requirement to assess a "project sponsor's experience in providing the requested assistance to households."

The Seattle Bank is concerned that the proposed rule may not allow a sponsor with extensive experience in rental housing to use AHP subsidy to provide down payment assistance for their first owner-occupied project because they do not have "experience in providing the requested assistance to households." It may also preclude small, rural organizations with small housing portfolios from being eligible for AHP. The Seattle Bank asks that the Finance Board clarify the language in question to provide the FHLBanks with the latitude to consider the totality of the sponsor's experience.

(d) **Minimum Bank Credit Product Usage Requirement** – The proposed rule would eliminate an option under the current regulation that permits FHLBanks to require members to use a minimum amount of credit products within the previous 12 months as a condition for applying for AHP.

This is consistent with the Seattle Bank's current practice. However, the Seattle Bank would prefer to see this option remain in the regulation to allow program flexibility for Advisory Councils and boards of directors to target scarce resources in a manner most appropriate for their districts.

(e) Sponsorship by a Not-for-Profit Organization or Government Entity – Section 951.5(d)(5)(ii) carries forward the language currently found at Section 951.6(b)(4)(iv)(B) which lists sponsorship by a not-for-profit organization or government entity as one of the nine scoring criteria to be used in evaluating projects under the competitive application program. This scoring criteria fulfills a statutory requirement that the AHP "give priority to qualified projects *such as* (emphasis added) the following: ... purchase or rehabilitation of housing sponsored by any nonprofit organization, any State or political subdivision of any State, any local housing authority, or State housing finance agency." 12 USC 1430(j)(3)(C). The use of the term "such as" indicates that the language is meant to be illustrative, not exhaustive. The Finance Board has previously acknowledged the illustrative nature of the statutory requirement by adding Native American Tribes, Alaskan Native Villages, and Native Hawaiian Homelands to the list of not-for-profit or government entities. Similarly, we recommend that the term "local housing authority" be amended to read "state, regional or local housing authority". The term "local housing authority" could be construed to exclude regional or state housing authorities that serve the same public policy goals of local housing authorities. In Alaska alone, there are fourteen (14) regional housing authorities and a state housing authority. We see no reason to disadvantage those states in which the production and rehabilitation of affordable housing is facilitated by means of regional and/or state housing authorities either in lieu of or in addition to the laudable work done by local housing authorities. We believe the use of the term "state, regional or local housing authority" is fully consistent with Congressional intent and achieves the desired public policy objective.

C. Homeownership Set-Aside Program

(1) Timing of Household Income Eligibility Determination

(a) The preamble to the proposed rule states that a household's income is determined at the time it is "accepted by the member and the Bank to enroll" in the homeownership set-aside program, not at the time the household is qualified for a loan. The distinction is intended to make clear that households do not need to be mortgage ready when they are enrolled, thereby allowing the set-aside program to be used with matched savings programs, IDAs, and other programs that prepare buyers for homeownership. It is important to note that the proposed rule's language in 951.6(c)(2)(i) states that the household's income must be at or below 80 percent "at the time the household is accepted for enrollment by the member and the Bank...."

Current practice at the Seattle Bank is to determine income eligibility at the time the household is <u>qualified</u> by the member, not at the time the household is <u>enrolled</u> by the member <u>and</u> the Seattle Bank. There is often a period of several weeks, sometimes even months, between the time a member income qualifies a household and the time that income is verified (and therefore the enrollment is accepted) by the Seattle Bank. Rather than penalize the household for this delay, the Seattle Bank reviews the income documentation the member used at the time the household was income qualified to verify that the household is in fact income eligible. The Seattle Bank is concerned that the language of the proposed rule would not permit this practice to continue, which would create significant operational inefficiencies for members and the FHLBank, as well as potentially disrupt a household's ability to enroll in the program.

(b) Although not addressed in the proposed regulatory language, the Analysis to the proposed rule states the Finance Board's expectation is that FHLBank policies will preclude the use of the program by individuals who are temporarily low-income, such as students.

While the Seattle Bank is committed to ensuring that our subsidies are made available to those for whom it is intended, there are infinite scenarios in which students' low-income statuses may not be temporary, such as those pursuing careers paying incomes that meet the set-aside's income restrictions (administrative, some civil service, etc.), as well as those pursing careers in which it can take many years to earn a wage that exceeds the set-aside's requirements (nonprofit management, journalism, teaching, etc.) Both of these scenarios are further subject to the housing prices in local markets. It's important to note that students are not the only population that could be considered temporarily low-income. Consider households that were unemployed for a portion of a year and who, had they been employed for the full year, would be just slightly over the income restrictions, but because they were not employed for the full year, met the income qualifications. The Seattle Bank suggests that, to address the issue of temporary low-income status, the Finance Board allow FHLBanks to use a previous year's W-2, tax return (if available), or Verification of Employment. These documents would ensure that the household had been low-income for one entire year. Additionally, using a previous year's income would be consistent with the proposed rule's intent to allow homebuyers time to qualify for a mortgage. It would also ensure that all members in the FHLBank System were using the same methodology for calculating income, which would provide greater program transparency. Moreover, this recommendation would result in significant operational efficiencies for the FHLBanks and members as questions about income calculations would be obsolete.

(2) Member Financial Incentives. The Finance Board requested guidance with regard to whether the regulation should:

(a) Require all originators of homeownership set-aside assisted mortgages to provide financial or other incentives, even if the originator is not a member.

The Seattle Bank does not support imposing requirements on nonmembers because of the challenges this raises with respect to enforcing those requirements and imposing sanctions if the requirements are not met.

(b) **Keep the current regulatory requirement that members providing mortgage financing also provide an incentive, or allow this requirement to be at the discretion of the FHLBanks, as a preferential selection criterion for its homeownership set-aside program.**

The Seattle Bank's membership is comprised of many small, community financial institutions that would be disadvantaged by a requirement that preferential selection criteria favor those institutions with the resources to provide incentives to homebuyers. For these institutions, in many cases, the cost of income-qualifying the homebuyer and monitoring their progress toward saving for a down payment and improving credit are sufficient to demonstrate a sincere commitment to the success of the homebuyer. Therefore, while the Seattle Bank supports the requirement being made at the FHLBank's discretion, we do not if it is used as a preferential selection criterion.

(c) **Impose additional incentives, such as a matching funds requirement, member-provided financing, or preference to a member working in partnership with a nonprofit.**

The Seattle Bank does not support adding these proposed requirements to the regulation. Rather, we prefer to have them included in our implementation plan at the discretion of our Advisory Council and Board of Directors. Currently, the Seattle Bank requires matching funds and some member incentives (but not member financing). Despite much discussion by the Advisory Council over the years, we do not require a member to work in partnership with a nonprofit because such a requirement favors urban areas where nonprofits with homebuyer education expertise tend to be located.

(3) **Progress Toward Use of AHP Subsidy** – The proposed rule would require FHLBanks to establish policies and procedures, such as time limits, for determining whether progress is being made toward drawdown and use of homeownership set-aside funds, and whether to cancel approval for lack of such progress.

It is unclear as to how this is different from the current 951.3(b)(1)(vii), which requires FHLBanks to have a time limit for use of AHP subsidy. The Seattle Bank would not support a proposed rule that established monitoring procedures to track homebuyers' progress toward closing on a home. Each homebuyer's circumstance is unique, and the FHLBanks and their members cannot afford the administrative costs of reporting each homebuyer's status. (For example, there are currently over 1,000 households enrolled in Home$tart, the Seattle Bank's homeownership set-aside program, for whom the Seattle Bank would have to receive regular status updates on their progress toward purchasing a home.) As long as time limits are established for how long funds can be set-aside and not disbursed, there will be assurance that the funds are made available to ready homebuyers within a reasonable period of time.

(4) Cash Back – The proposed rule would prohibit a member from providing cash back at closing and would require members to use any homeownership set-aside program subsidy beyond what is needed for closing costs and the approved mortgage amount to further reduce the principal of the mortgage loan.

The Seattle Bank agrees that the entire subsidy must be used to reduce principal on a mortgage, but does not support the idea that a member cannot provide any cash back to the buyer at closing. If the buyer has more of their own cash than is needed to close the loan, the buyer should be able to keep that cash to build reserves, rehabilitate the home, purchase appliances or other needed household items, etc. It is counter to homebuyer education counseling programs to require households to contribute every dollar they have toward the purchase of their home. Instead, they are counseled to save money for the purposes mentioned above. Imposing this regulatory requirement would likely conflict with the homebuyer education classes that the FHLBanks may require households to take as a condition of receiving the subsidy. Additionally, the Seattle Bank believes it is appropriate for the regulation to have jurisdiction over Seattle Bank resources, but not over private or other resources not provided by the FHLBanks.

D. Relocation of Households in Rental Projects – The proposed change would allow the FHLBanks to deal with situations where approved rental projects are forced to relocate for reasons such as the exercise of eminent domain or a need for additional units or services, and the project sponsors will be transferring the same residents to a new building. Currently, the AHP regulation treats these situations as a sale that requires the repayment of the entire amount of AHP subsidy, thereby releasing the project from its AHP commitments and making the AHP subsidy available for other AHP-eligible projects, unless the property continues to be subject to a deed restriction or other legally enforceable retention agreement or mechanism incorporating the income-eligibility and affordability restrictions committed to in the AHP application for the remainder of the retention period.

The Seattle Bank is supportive of this change. However, to prevent abuse, it should be made clear in the regulation that approval of any relocation is at the discretion of the FHLBank.

E. AHP-Related Operating Expenses – The Seattle Bank would also request that the Finance Board re-visit the manner in which the required annual AHP contribution is determined. The Federal Home Loan Bank Act requires that each FHLBank contribute 10 percent of the preceding year's net income. However, the statute does not address whether expenses related to managing the AHP can be deducted from the required contribution. We would recommend that the net income of the FHLBanks be determined exclusive of expenses related to the AHP, and that the FHLBanks be allowed to deduct expenses related to the program from the annual 10 percent contribution.

The Seattle Bank appreciates the opportunity to provide comments on this important proposal. If there are any questions regarding our comments, please direct them to Steve Johnson, AHP Manager, 206.340.8738, or Gerry Champagne, outside counsel, 617.395.7603 .

Very truly yours,

Richard Riccobono
Executive Vice President and Chief Operating Officer

cc: Steve Johnson, AHP Manager
Federal Home Loan Bank of Seattle