



June 12, 2018

Submitted Electronically

Alfred M. Pollard, General Counsel
Attn: Comments/RIN 2590-AA83
Federal Housing Finance Agency
400 Seventh Street SW
Eighth Floor
Washington, D.C. 20219

Re: Proposed Rulemaking and Request for Comments: Affordable Housing Program Amendments (RIN 2590-AA83)

Dear Mr. Pollard:

The Federal Housing Finance Agency (FHFA) has requested comments on its Proposed Rulemaking on amendments to the Affordable Housing Program (AHP) regulation published on March 14, 2018 (the Proposed Rule)¹ and re-published with a correction and deadline extension on May 2, 2018. The Federal Home Loan Bank of San Francisco (the Bank) appreciates the opportunity to comment on the Proposed Rule.

The Bank offers the following comments to underscore our views on issues that are of particular concern for this Bank. Several of the Bank's comments are also reflected, to varying degrees, in the comment letter (System Comment) submitted by the Federal Home Loan Banks (the FHLBanks), on June 1, 2018. The Bank's comments focus on what we perceive to be practical roadblocks within the Proposed Rule's framework and we have offered what, in our view, are better alternatives.

1. The Outcome Requirements increase AHP complexity and jeopardize program transparency.

The Bank does not believe that the Outcome Requirements coupled with the expanded Targeted Community Lending Plan (TCLP) will provide the Bank with the requisite flexibility to address district and changing district housing needs. On the contrary, the Bank believes the prescriptive nature of the Outcome Requirements coupled with the monetary penalty if the Bank fails to meet the Outcome Requirements will force the Bank to design its program to ensure it meets the requirements, thereby further limiting its ability to target specific housing needs in its district. Moreover, the Bank believes the ability to re-rank applications if the Bank does not meet the Outcome Requirements will jeopardize the AHP's transparency and legitimacy – potential applicants will be unable to determine how and why their projects did not score high enough to receive an award.

¹ 83 Fed. Reg. 11344 (Mar. 14, 2018).

The Bank strongly urges the FHFA to abandon the Outcome Requirements in the Proposed Rule in favor of a more traditional scoring framework. As articulated in the System Comment, the Outcome Requirements in the Proposed Rule are unduly complex, will be difficult to administer, and will have the effect of losing the predictability and transparency that our users have come to expect and appreciate. Moreover, this proposed structure would create a static program that will be difficult to modify in reaction to changing needs in the housing market of the district and would impact the Bank's ability to shape and operate the program into the future. Specifically, the Proposed Rule includes threshold percentage allocations for the Bank's annual contribution that are tied to very particular, prescriptive regulatory priorities. While these priorities may be priorities today, there may be new and different priorities in the future that do not fit under any of the existing categories. As written, the Proposed Rule does not provide the flexibility for the Banks to shift priorities with the changing needs of the communities the AHP is intended to serve.

One facet of the proposed Outcome Requirements that is particularly troubling for the Bank is the requirement that the Bank:

"...award at least 10 percent of its required annual AHP contribution to low- or moderate-income households, or to projects targeting such households, for the purchase by such households of homes under any or some combination of the Bank's General Fund, any Bank Targeted Funds, and any Bank Homeownership Set-Aside Programs..."

The Bank has examined the home purchase funds we disbursed in the competitive and set-aside programs for 2016 and 2017, and found that the Bank would not have met this requirement in those years. The very high cost of homeownership in the district combined with the very low supply of affordable housing would make meeting this requirement very challenging for the Bank.

The Bank strongly urges the FHFA to re-think its proposal.

As an alternative to the Outcome Requirements in the Proposed Rule, the Bank recommends that the FHFA adopt a scoring-based methodology similar to that outlined by the CIOs and submitted to the FHFA on June 11, 2018, that also incorporates additional flexibility by allowing the FHLBanks to create Targeted Funds.

2. The proposed timing and accompanying governance requirements for the expanded TCLP in the Proposed Rule poses significant practical constraints on the Bank's ability to administer its programs, and respond to current needs and trends in its district, in a timely and orderly fashion.

The Bank notes that under the Proposed Rule, an FHLBank must approve and publish its TCLP at least 12 months prior to offering a Targeted Fund or, at a minimum, six months prior if an FHLBank only elects to offer a General Fund. The Bank's view is that these requirements will severely limit the Bank's ability to respond to emerging needs and trends in a timely fashion.

The Bank believes that to conduct the required research, use it to establish appropriate priorities and scoring criteria, survey and build consensus with the program stakeholders, including the Bank's members, AHP project sponsors, and the Bank's Advisory Council, all within the parameters of the Bank's required governance process, would require a considerable length of time likely ten months to a year. Tacking on the additional 6 or 12 months required lead time for publication in advance of offering General or Targeted Funds, translates to between one and two years to produce a TCLP. These requirements in the Proposed Rule would effectively preclude a Bank from reacting to emerging needs or trends on a timely basis. Furthermore, required timelines in the Proposed Rule, would essentially prevent a Bank from being able to use information gleaned from its most recent competitive round to either adjust its priorities or fine tune scoring for the next round.

The Bank further maintains that these timelines will complicate the Bank's ability to align the timing of AHP awards with the timing of other major funders, specifically, tax credit and state housing agencies. Given that the Bank must offer a General Fund, may offer Targeted Funds, and will likely offer one or more homeownership set-aside programs, having to simultaneously manage the required governance process while establishing and communicating timing requirements, and while considering the timing of other funding sources, will pose significant operational challenges for the Bank. The Bank urges the FHFA to reconsider the expanded TCLP requirements in the Proposed Rule.

The Bank is troubled that under the Proposed Rule, our success or failure to meet the Outcome Requirements would be assessed *after* the close of the competitive round. Notwithstanding the strength of the market research that the Bank may have relied upon, the Bank's ability to accurately predict the characteristics of the pool of project applicants more than a year before the competitive round is unrealistic, particularly given that in our experience, the AHP does not drive production of affordable housing. In other words, the Bank believes that regardless of how well we design our scoring and set our priorities, other forces in the industry will prevail to determine outcomes. We would strongly disagree with any assumption that AHP and its scoring objectives drive the development of certain types of projects. While that assumption may be valid in certain pockets of the country, and with respect to specific types of projects, the Bank has not found it to be true in our district. Historically, the Bank's AHP scoring criteria do not incent sponsors to develop certain types of projects over others. Instead, the incentive to build particular affordable housing projects comes from priorities determined by much larger and more impactful funding sources including federal (through HUD and LIHTC) and state funding sources.

The Bank recommends that the requirements of the TCLP remain unchanged from the existing regulation, except in the event that the Bank offers a Targeted Fund. In that instance, the Bank requests that the 12-month advance notice be eliminated.

3. Supportive services expenses should be accepted as standard operating expenses.

The FHFA has determined that supportive services expenses are not an eligible use of AHP subsidy. The Bank has advocated strongly for acceptance of supportive services expenses (at

least at some reasonable level) as a standard expense necessary to operate most, if not all, affordable rental housing projects, and to be viewed in the same vein as other operating costs including, property management and security fees, and payroll expenses.

The Bank strongly believes that on this point, the AHP is out of step with other major funders and not keeping up with affordable housing industry standards. The position of the Proposed Rule, disallowing supportive services as an operating expense, is at odds with the mandatory inclusion of supportive services in AHP projects serving special needs households. Furthermore, since other major funders not only allow, but expect, supportive services expenses to appear on the operating pro forma, the sponsor who submits an AHP application must in effect create a separate pro forma as a workaround to the prescribed regulatory requirements. In practice, the Bank has found that when business practices diverge materially from one funder to another, this tends to lead to confusion and inadvertent misrepresentation.

The Bank strongly urges the FHFA to reconsider its position on this topic.

The Bank recommends that the FHFA: 1) recognize supportive services as a standard operating expense in the running of an affordable housing rental project; or 2) allow FHLBanks, to establish in their Implementation Plans, with input from their Advisory Councils, a supportive services operating expense benchmark.

4. FHLBanks should have discretion to determine whether and when to fund alternate projects.

The Proposed Rule requires that Banks must fund alternate projects within a year of approval if previously committed AHP subsidies become available. Since the inception of the AHP, this Bank's practice has been to fund alternates only if, in the period just prior to final approval of the AHP competitive awards, we are informed that a project (within the list of recommended approvals) is withdrawing thus freeing up sufficient subsidy to fund an alternate project. This practice has worked well for the Bank.

In the Bank's experience, after the results of a competitive round are announced, projects that were not awarded typically begin the process of securing other funding sources to replace an expected AHP grant and/or reconfiguring their projects in the absence of an AHP grant. The project's financials generally do not remain static. In order to compensate for the lack of an AHP grant, project sponsors may also have to reconfigure their project plans, which may affect their original scores.

If the FHFA's concern was to ensure that AHP funds are used promptly and to the fullest advantage, the Bank is in complete agreement and we have structured our policies and procedures accordingly. This Bank has always committed more than its statutory minimum by recycling de-obligated funds into the next competitive round.

The Bank recommends that the FHFA make no change to the existing regulation's requirements for approval of alternates and continue to allow individual FHLBanks to determine whether and when to fund alternate projects.

5. FHLBanks should have discretion to determine whether to request projects cure noncompliance before considering modification requests.

The Proposed Rule requires that, before the Bank can approve a project modification, the Bank must request that the sponsor cure noncompliance. There are instances in which a project modification is appropriate, even though there is no noncompliance. The FHLBanks should be permitted to approve project modifications in situations in which there is no noncompliance.

For example, if a sponsor submits a modification requesting a change to its green building commitments or homeless unit reservation based on a change in the project's budget or financing commitments, the Bank believes it would be appropriate to only consider the project sponsor's "good cause" explanation (which, pursuant to the Bank's modification policies and procedures, must include a reason why the project sponsor could not fulfill the commitment or why fulfilling the commitment would now harm the project in ways that were not originally anticipated).

As financing for affordable housing becomes increasingly scarce following tax reform and in the face of continuing cuts to government housing programs, the Bank feels strongly about preserving the AHP's ability to accept and adapt to projects' needs.

The Bank recommends that the FHFA remove the requirement that the sponsor must first attempt to correct the "noncompliance" with original scoring commitments if the project's revised score is within the range of approved projects in its competitive round and the change is for good cause.

6. Remediation of project noncompliance should be recognized as "good cause" warranting project modification.

The Bank considers remediation of project noncompliance, by itself, to be good cause for modification. Projects which, as modified, would still be eligible for an award in the round in which they were approved, should continue to be eligible notwithstanding changes after approval. The Bank believes that requiring a project to first attempt to cure noncompliance when the project, as modified, is eligible based on scoring, feasibility, and need-for-subsidy, adds unnecessary administrative costs for the Bank, the project sponsor, and the member, without providing any benefit to the project or to the program.

The Bank recommends that the FHFA recognize remediation of noncompliance as a valid "good cause" for a project modification.

7. Leaving the existing definition of need for subsidy unchanged is in the best interests of the program.

Over the course of the multi-year modernization process, the FHLBanks have consistently expressed concern regarding regulatory requirements that would restrict their ability to coordinate with other affordable housing funders and to create effective and appropriate solutions to situations not contemplated in draft guidance or in the Proposed Rule. The Proposed Rule includes prescriptive language in the preamble that does just the opposite – restricts the Bank’s ability to be flexible in coordinating with other funders to ensure viable affordable housing projects are given an opportunity to develop and thrive.

This Bank remains resolute in its belief that leaving the existing definition of need for subsidy unchanged would be in the best interests of the program. Under the existing definition, the Bank has established a streamlined administrative process that empowers the Banks to seek sensible, fair, and pragmatic solutions in cases where a project’s need for subsidy could be in question.

The Bank recommends that the FHFA remove new language in the Proposed Rule with respect to the need-for-subsidy determination and re-adopt the language in the preamble to the 2006 regulation where need from subsidy is determined by the difference between sources and uses of funds in the development budget.

8. The Bank supports the elimination of the Retention Agreements for homeownership units receiving AHP Subsidy.

While the Bank understands that the purpose of the retention agreements is to discourage “flipping” of homes, based on the amount and the quantity of repayments received by the Bank, the Bank believes that flipping has not occurred. To illustrate this point, in the Bank’s portfolio of set-aside transactions, only 2% of the subsidized homebuyers repaid a portion of the subsidy at an average amount of less than \$4,000. The Bank agrees entirely with the rationale presented in the preamble – that the obligation to repay not only deprives the low-income household of the full benefits of homeownership, it may also pose a financial burden. Moreover, the Bank agrees that the amounts in question have not merited the administrative burden on the Banks and the members. We also note that removal of the AHP retention requirement will eliminate on-going conflicts with other sources of homeownership down payment assistance, such as with HUD’s FHA single family housing policy.

The Bank is supportive of the increase in the permissible set-aside grant from \$15,000 to \$22,000 but does not believe that this should have any bearing on the decision to eliminate retention requirements. Given the exorbitant price of housing in much of the Bank’s district, the increase in the maximum subsidy will only partially fill the huge gap between the price of a home and the mortgage that a low-income household can afford, and would thus be too small to incent a buyer to flip a property.

Alfred M. Pollard

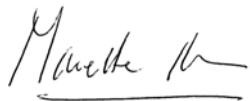
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Notwithstanding the views of this Bank, we recognize that other FHLBanks are dealing in a variety of economic landscapes and market dynamics. Thus, the Bank supports the FHLBanks system position to allow FHLBanks to retain the current retention requirements at their discretion.

In closing, the Federal Home Loan Bank of San Francisco appreciates the FHFA's efforts throughout this modernization process – its willingness to engage in meaningful dialogue with the FHLBanks and Advisory Councils, and to open-mindedly listen to the various stakeholders. It is in this spirit of cooperation that the Bank offers its recommendations for improving the Proposed Rule which are, it believes, consistent with the FHFA's goals of balancing the Bank Act housing priorities with the FHLBanks' goals of achieving a more flexible scoring system in order to target changing specific housing needs in their districts.

Sincerely,

A handwritten signature in black ink, appearing to read "Marietta Núñez", with a horizontal line underneath the signature.

Marietta Núñez
VP, Director of Community Investment
Community Investment Officer