June 12, 2018

Mr. Alfred Pollard, General Counsel
Federal Housing Finance Agency
400 Seventh Street SW, Eighth Floor
Washington, DC 20219

RE: RIN 2590-AA83, Comments on Proposed Amendments to Affordable Housing Program

Dear Mr. Pollard:

The Local Initiatives Support Corporation (LISC) is pleased to provide comments on the proposed amendments to the Federal Home Loan Banks' (FHLB) Affordable Housing Program (AHP) regulations. The AHP is an important resource for the preservation, development and recapitalization of affordable housing financed and supported by LISC and developed by our partners. We appreciate the significant effort undertaken by the Federal Housing Finance Agency (FHFA) to update and streamline the program's regulations while retaining important flexibilities.

Established in 1979, LISC is a national nonprofit housing and community development organization that is dedicated to helping community residents transform distressed neighborhoods into healthy and sustainable communities of choice and opportunity. LISC mobilizes corporate, government and philanthropic support to provide local community development organizations with loans, grants and equity investments; as well as technical and management assistance.

LISC has a nationwide footprint, with local offices in 31 cities and partnerships with 86 different organizations serving rural communities throughout the country. LISC invests approximately $1.4 billion each year in these communities through various programs, including the low-income housing tax credit (LIHTC). Our work covers a wide range of activities, including housing, economic development, building family wealth and incomes, education, and creating healthy communities. With the above as context, we offer the following comments with respect to the proposed regulatory amendments.

<u>General Comments</u>
Before we address specific questions posed in the rule, we have some general comments about the proposal. The AHP creates high-impact partnerships among local communities, FHLBs, lenders and investors, and affordable housing developers that has created thousands of affordable homes that would not otherwise have been financially feasible. These projects involve inherent risk, which is an appropriate place for mission-oriented subsidy to be directed. Both developers and banks are and should remain appropriately concerned about identifying and mitigating the risk of these projects. But we believe that instead of supporting appropriate development risk, programmatic and regulatory incentives often create a significant concern over compliance risk. Instead of the AHP creating an incentive to avoid compliance failure, the

program structure should create rewards for member banks that take on appropriate risks that result in the completion of important projects.

Homeownership vs Rental. We support affordable homeownership opportunities but **do not support increasing the maximum share of AHP resources for homeownership** from 35 percent to 40 percent. While promoting homeownership for low- to moderate-income households is important and should be continued, it is well documented that basic housing affordability challenges for the lowest-income households have grown consistently worse. We are concerned the proposed regulation creates strong incentives for FHLBs to focus on homeownership activities without regard to the relative affordability gaps for homeownership and rental housing in their service areas. This is reflected not only in the proposed increase in the allowance for homeownership, but also in the proposed increase in homeownership awards (from $15,000 to $22,000) and in the elimination of homeownership retention requirements. The AHP has played an important role in supporting the preservation and development of new rental properties for very low-income and extremely low-income households, and the portion of AHP funding to this critical need should not be diminished.

The effort to create more explicit targeted outcomes for multifamily housing could further amplify the large **compliance imbalance between homeownership and affordable rental housing programs**. Other stakeholders have expressed strong and legitimate concerns about the complicated nature of the proposed targeted outcomes for multifamily housing, and we believe that this added complexity could have the unintended effect of driving the FHLBs toward a greater emphasis on homeownership awards. The increased complexity for rental housing may cause higher compliance risk for awardees and greater administrative and compliance burden for the FHLBs.

Appropriations Risks. FHFA should **provide relief from homelessness and special needs targeting in the event of lapses in appropriations.** Properties with operating and service subsidies, including HUD rental assistance contracts, are explicitly subject to the availability of ongoing funding, and developers and funders are unable to accept the obligation of taking on these obligations in the event of non-renewal. If the rental subsidy is discontinued for federal or state budgetary reasons, and not due to malfeasance of the developer, these agencies provide relief from the homeless and/or special needs restrictions to maintain project feasibility. AHP should provide a similar waiver to allow project rents and income targeting to increase to 50 percent of Area Median Income and to release the project from any specific restrictions if replacement subsidies cannot be secured. Otherwise, nonprofit developers must take on the financial burden of serving these populations without the benefits of rental subsidy (to remain in compliance with the AHP requirements) or put in the position of needing subsidy transition reserves which are not typically allowed in the AHP program and which would be required by investors or other partners focused on the ongoing viability of the project.

Project Commitments. Many banks require **securing all or most other funding commitments** before allowing projects to apply successfully for AHP while others do not. This presents significant challenges and barriers to projects closing effectively, as AHP resources are typically

not the largest portions of the financial structure of most developments. Possible changes to the process could include creating a preference for AHP to be secured as an early finance commitment, even if the AHP award is conditioned upon subsequent approval of other financing such as LIHTCs. Another suggestion is to increase the number of award rounds to more than one per year to align with state housing finance agency tax credit rounds. This would permit AHP awards to be considered as endorsements of quality tax credit applications and further expand the impact and leverage of AHP.

Requirement to Include All Affiliates and Team Members at Application. **We don't support the proposed requirements that a project sponsor include all affiliates and team members**, such as a general contractor in the AHP application, as outlined in 1291.21(b). These individuals are not likely to have been finalized at the time of application and we instead encourage FHFA to allow sponsors to certify adherence to the proposed requirements.

Administrative Reforms

We believe requiring sponsors to **create two operating pro forma for housing operations and supportive services adds unnecessary burden** while providing little value to the Bank. These costs would often be arbitrarily split so we recommend allowing applicants to continue to include supportive services in their operating pro forma. FHFA should instead require Banks to collect self-certifications from applicants indicating that AHP is not being utilized to fund services since it's not a statutorily eligible use.

The **draw-down of AHP award funds** sometimes requires duplicative submission processes and repackaging of closing materials. In addition, if the proposed changes increase ongoing monitoring and compliance after award (such as by requiring reviews of changes to the development team), then AHP becomes a less viable source of gap financing due to the increased administrative burdens for awardees.

The Banks should have a process for allowing applicants to **cure nonmaterial application flaws** before undergoing final review and ranking. The current process is unnecessarily rigid and can result in good projects getting disqualified for non-substantive errors or omissions.

Advisory Councils. The **advisory councils** are a critical access point to the program for nonprofit developers. Many banks do a good job of including nonprofits on these councils. However, some do not, and we are concerned about the proposed change that would explicitly allow for-profit organizations to be included under the "community and not-for-profit organizations" designation. While some for-profit entities might be appropriately included in these councils, we urge FHFA to define "community organization" in a way that would not include all developers of homes for moderate- and low-income households. We also urge that the majority of organizations included under this heading be not-for-profit organizations. Minimum representation by nonprofit organizations, including community-based nonprofit developers, CDCs and others, on the advisory board is critical to the program's success and credibility.

Revolving Loan Pools. We support **increased use of AHP funds for revolving loan fund** activity. We thank the FHFA for posing thoughtful questions on how the AHP can be more effectively utilized to support affordable housing lending opportunities due to the current challenges. Creating opportunities for AHP resources to be utilized for affordable housing lending opportunities will allow revolving loan funds to better deploy dollars based on local market needs and not be constrained by regulatory and administrative impediments.

The following lists LISC's specific comments by request number:

Subpart B – Program Administration and Governance

Question 1. What are the benefits and risks of allowing the Banks to establish Targeted Funds?

The current system spreads points across many priorities, so that a good project meeting a targeted need may not be competitive and often favors attributes in project deals that are not internally consistent within a single project. Streamlining the scoring to advance projects that advance a smaller number of distinct goals, rather than a combination of several sometimes inconsistent goals, is a welcome change.

Question 3. Would the proposed expansion of the contents of the Targeted Community Lending Plans impede the Banks' ability to respond to disasters through the AHP?

The proposed regulations raise concerns about how AHP funds could be utilized for disaster relief due to regulatory timing requirements. For instance, the proposed regulations state that a Targeted Community Lending Plan must be developed for General Fund, Targeted Funds, and Homeownership Set-Aside Programs and include data, public feedback, and other requirements to substantiate need in a given market. These requirements would make it difficult for AHP funds to be utilized quickly for disaster relief since these events cannot be known in advance and the requirements create a lengthy process to utilize AHP funds in a targeted manner. FHFA should consider how regulatory and administrative guidance can be structured to allow flexibility for the use of AHP resources in disaster relief.

In addition, FHFA should emphasize the role of AHP resources in disaster prevention, including helping to ensure that new and existing affordable housing incorporates resiliency measures to mitigate the impact of future disasters on scarce affordable housing.

Question 9. Should the AHP retention agreement, if retained in the final rule, require AHP-assisted household to repay the subsidy to the Bank from any net proceeds on the sale or refinancing of the home or from the net gain?

LISC does not support removing the AHP retention agreement since there is risk that subsidy may be improperly utilized by homeowners. According to the proposed rule, over 80 percent of all AHP Homeownership Set-Aside resources are utilized as down payment assistance for first-time homebuyers. The average AHP subsidy is over $6,300 and the current five year retention

requirements are similar to the HOME Program. We do not support removing this requirement since although the risk is small, there is an opportunity for misuse of limited subsidy if the retention requirement is removed. In addition, we don't feel the overall administrative requirements are too burdensome for the Banks and are reasonable for this purpose.

Subpart C – General Fund and Target Funds

Question 15. How should preservation of rental projects be encouraged through the AHP while discouraging displacement of current occupants with higher incomes than those targeted in the AHP application submitted to the Bank for approval, and is the proposed requirement for a relocation plan approved by the primary funder reasonable?

AHP funds are often used to preserve affordable rental housing assisted under other federal housing assistance programs. FHFA should allow projects to grandfather existing residents as is done in other federal affordable housing preservation programs. This is consistent with current HUD policy and the proposed legislative changes to the LIHTC program. FHFA's relocation requirement for currently assisted properties should be consistent with these program's requirements. Where a property was not previously subject to affordability requirements, FHFA should require a relocation plan that provides tenant protections.

Question 18. What are the potential advantages and disadvantages of allowing the Banks to impose a maximum subsidy limit per project sponsor?

A sponsor subsidy limit would cap FHLB exposure to risk associated with a particular sponsor and would encourage spreading funds to more sponsors. However, sponsors differ substantially in their size, scale and geographic scope, and in the nature of their capacity and internal controls. We believe that the banks can have much greater impact if they make awards based on the merits of individual applications, taking into account the risks associated with each application, rather than setting an arbitrary sponsor cap.

Question 20. Are the current AHP revolving loan fund provisions reasonable, and how could the financing mechanism of revolving loan funds be used successfully with AHP subsidies?

The current AHP revolving loan fund provisions are structured towards reviewing the use of AHP subsidy for financing capital for the purchase, construction, or rehabilitation of affordable owner-occupied or rental housing. While this is an important use of these dollars, many community development financial institutions (CDFIs) would benefit from being able to utilize the subsidy for loan guarantees for these eligible activities. The use of subsidy for loan guarantees would enable CDFIs more flexibility when financing qualified projects and increase the leverage of AHP awards.

The current regulations state that subsequent revolving loan fund shall be utilized for qualified projects and where "at least 20 percent of the units are occupied by and affordable for households with incomes at or below 50 percent of the median income for area…" As noted

elsewhere in our comments, we suggest this be revised to align with the recent LIHTC income averaging flexibilities.

The regulations provide Banks flexibility in how they monitor subsequent revolving loan fund lending activities. We believe that overly complex administrative and compliance restrictions on subsequent CDFI revolving loan fund activity is unnecessary since these organizations are certified by the U.S. Department of the Treasury as mission-based lenders and have long track records of utilizing public and private resources for affordable housing relending purposes. We encourage the FHFA to provide the Banks subsequent relending best practices from the one Bank allowing these activities and issue sub-regulatory guidance to ensure the most consistent and least burdensome treatment.

Question 21. Why have certain AHP scoring criteria for revolving loan funds been difficult to meet, and how would AHP subsidy be repaid in the event of project noncompliance, and how can a revolving loan fund demonstrate a need for AHP subsidy?

The AHP is designed from a regulatory and administrative perspective to fund qualified affordable housing projects, either owner-occupied or rental housing. The use of AHP subsidy for affordable housing lending requires a different approach, both from the regulatory and sub-regulatory requirements. Applicants requesting to utilize AHP resources for revolving loan fund activities are often disadvantaged since both the regulations and application review requirements are designed to review and rate the need for project-level subsidy instead of lending capital. In addition, it's our understanding that only one of the FHLBs allows the use of AHP resources for this use since many FHLBs are unclear on how to administer a competition for lending purposes. Many Banks are also probably reluctant to fund these activities due to concern on how FHFA examiners, who also have limited background in the use of resources for these activities, will review their performance.

It's important to note that there are examples of other affordable housing programs which fund both project-based development and affordable housing lending opportunities. The Capital Magnet Fund, which is administered by the U.S. Department of the Treasury, provides the FHFA a good example of how regulatory and administrative requirements can be structured to support both affordable housing project-level and lending activities.

Question 22. Would the proposed outcome requirements for the statutory and regulatory priorities facilitate use of AHP subsidies by revolving loan funds, and if so, how?

We don't believe the proposed outcome requirements, including the removal of the homeownership retention requirement or the targeted outcomes facilitate the use of AHP subsidy for revolving loan funds. As discussed above, we don't support removing the homeownership retention requirements due to the risk of improper use of limited subsidy. We also have concerns about the overly complicated nature of the targeted outcomes and how this may be amplify compliance burden for both lending and project-based activities.

Question 23. What are the potential positive or negative impacts of eliminating the owner-occupied retention agreement requirements for revolving loan funds?

As stated above, we do not support removing the owner-occupied retention requirements due to the higher risk this would cause the AHP.

Subpart D – Homeownership Set-Aside

Question 25. Are there any potential positive and negative impacts of increasing the subsidy limit per household from $15,000 to $22,000, and should the subsidy limit be higher or lower?

FHFA (or the banks) could consider setting a per-household maximum subsidy unit that is no higher than the average per-unit subsidy for rental projects since this would create parity between award uses. Please also see our overall comments on expanding the portion of AHP funds dedicated to homeownership.

Subpart E – Outcome Requirements for Statutory and Regulatory Priorities

Question 28. What is the utility of the proposed outcome approach to income targeting, and are the proposed 55 percent threshold, its applicability solely to rental units, and income-targeting at 50 percent of AMI appropriate?

It's a positive step to require that a certain portion of funded units are income-targeted, but AHP can make a greater impact by aligning with other affordable housing subsidy programs. Most rental properties seeking AHP awards would already seek to serve households below 60% of AMI, and 50% of AMI does not serve a significantly different population. We recommend that maximum points be awarded for projects where 100% of units are reserved for households with incomes at or below 80% of median income and the average income across all units does not exceed 60% of median income, which is consistent with recent changes in the LIHTC program.

Questions 29 - 31. Is the proposed increase in the minimum threshold from 20 to 50 percent for the number of units reserved for homeless households, special needs populations, and other targeted populations appropriate?

We don't support this change for several reasons. First, the amount of the AHP subsidy is frequently five to ten percent of the total development cost. These capital grants are too small to allow significantly lower rents through decreased permanent debt load, and onerous restrictions make projects less attractive for tax credit investment and create a need for significant transition reserves, tying up gap funding that could otherwise be used for additional features or building additional homes. In addition, some states are under U.S. Department of Justice consent decrees which limit the percentage of units serving the homeless and/or persons with disabilities to no more than 20 or 25 percent of the total units in a property in order to promote a policy of greater community integration. Many states and cities do not have

the gap capital resources, paired with project-based rent subsidies, to support the development of supportive housing projects that have 50 percent or more of the units targeted to special needs.

We appreciate and support the concept that AHP has Scoring Criteria that gives extra points for projects reserving units for Homeless Households and/or Special Needs. But as noted above, the existing rule lacks a critical element of flexibility used in the Homeless Emergency Assistance and Rapid Transition to Housing Act and under the California Tax Credit Allocation Committee qualified allocation plan that provide relief from homeless targeting if rent subsidies are cancelled or not renewed due to no fault of the developer. This flexibility minimizes the need for transition reserves that tax credit investors usually require if annual appropriations are insufficient to continue the rental assistance payments, such as in a Project-Based Section 8 rental assistance contract. The State of California and many other state and local subsidy providers do not place the statutory risk of insufficient appropriations upon the developer, and doing so would be a strong disincentive to pursue these important projects.

Question 32. Is the proposed 20 percent minimum threshold for the number of units in a project reserved for extremely low-income households appropriate?

AHP's support for units serving ELI households is important and should be continued. However, targeting that preferences multifamily rental projects with a high percentage of very low-income households is difficult to reconcile with other federal programs, such as HOME, Community Development Block Grants, and LIHTC, that set affordability thresholds at 60 or 80% of median income. These would also create incentives for concentrations of populations of extremely low income and with disabilities, which are generally discouraged and sometimes prohibited by law as discussed above.

Underwriting transactions to comply with overlapping program requirements and deep affordability also constrains cash flow and creates operational challenges, particularly where there is no rental subsidy. A broader but a more flexible affordability requirement would allow a more diverse pool of affordable housing projects, including mixed-income projects, to better compete for AHP funds. We recommend that maximum points be awarded for projects where 100% of units are reserved for households with incomes at or below 80% of median income and the average income across all units does not exceed 60% of median income, which is consistent with recent changes in the LIHTC program.

While multifamily rental housing projects are eligible for AHP assistance as long as greater than 20% of units are affordable to very low-income households (incomes under 50% of area median income), regulatory requirements that heavily weight deeper income targeting have made it difficult for mixed-income projects to successfully compete for subsidy dollars.

Question 33. Do the three proposed regulatory priorities described in proposed § 1291.48 – underserved communities and populations, creating economic opportunities, and affordable

housing preservation – constitute significant housing priorities that should be included in the regulation, or should other housing priorities be included?

We support explicit identification of these goals, including the preservation of existing affordable housing. We also recommend adding "financial coaching" to the services meeting the "creating economic opportunities" target. But as noted above, we are concerned about the level of complexity and the administrative burden created for FHLBs, program applicants, and awardees by overlapping requirements and post-award monitoring. Also, while we appreciate an effort to harmonize the collective impact of AHP and the Duty to Serve programs, grant programs from the FHLBs have significantly different origins and purposes than a regulatory program that does not have access to programmatic subsidies.

Subpart F - Monitoring

Question 39. Are the proposed reductions in the Banks' monitoring requirements reasonable, taking into consideration the risks of noncompliance and the costs of project monitoring?

Yes. We strongly support the elimination of redundant oversight and compliance burdens. AHP is an important gap filler for many projects, but current rules can add unnecessary complexity to transactions. For AHP to be most effective, rules should allow awards to be subordinate to other affordability commitments, which are generally equal to or stricter than AHP requirements. Similarly, the AHP can rely on the compliance monitoring, developer fee limits, and other program terms of funding sources to which it is subordinate. For instance, we do not support requiring sponsors to notify a FHLB when a project is out of compliance with LIHTC income or rent requirements since this would require Banks to amend agreements and actively monitor LIHTC projects. The current LIHTC compliance monitoring has proven to be successful so this is unnecessary and only creates additional administrative burden for sponsors and the Banks. Greater willingness to adapt and subordinate would allow AHP funds to go farther and be more effective as the final gap-filler, especially in complex transactions.

There are many examples about how extended negotiations around the interaction between an AHP award and other capital sources add time and cost to the development process, even to the extreme of having awards rescinded or the recipient dropping the AHP award from the project funding. Ironically, the sometimes unreliable nature of AHP awards has led some developers to seek back-up subsidy sources to protect their projects from risk, which thereby leads to the awards being rescinded as redundant, which makes it increasingly difficult to place AHP funds where they can have the greatest impact. In some cases, the additional compliance costs of an AHP award deter applicants from applying. Especially when an award is likely to be small relative to the overall project and the AHP compliance process is entirely separate from other subsidy sources, some mission-oriented developers will simply forego AHP entirely.

Question 40. Is data available on the noncompliance rates of projects funded under the PBRA Section 8 Program?

HUD regularly publishes information on Section 8 PBRA property inspection scores. These properties are also subject to numerous oversight requirements, including owner certification of compliance, management and occupancy (MOR) reviews performed by performance based contract administrators, tenant income certifications, and others.

Our organization has supported HUD's efforts in recent years to track the performance of properties in its portfolio more carefully to identify signs of early distress. It's important to note that these indicators are not evidence of noncompliance, but were designed to allow HUD to offer assistance to owners that may be facing difficulties, and should never be used to penalize owners, projects, or their residents. We encourage FHFA to partner with HUD to access their Section 8 PBRA MOR data to better understand this program's low noncompliance rates.

We thank the FHFA for the opportunity to offer suggestions and welcome opportunities to explore these and other possible improvements to the AHP. Please contact Mark Kudlowitz (mkudlowitz@lisc.org), LISC Policy Director, if you need additional clarification or follow up on any of the recommendations provided in this letter.

Sincerely,

Matt Josephs
Senior Vice President for Policy