July 20, 2010

Alfred M. Pollard, General Counsel
Federal Housing Finance Agency
1700 G Street, NW, Fourth Floor
Washington, DC 20552

Comments: RIN 2590-AA27 Duty to Serve Underserved Markets for Enterprises

Dear Mr. Pollard:

Stewards of Affordable Housing for the Future (SAHF) and the Housing Partnership Network (HPN) welcome this opportunity to comment on the Federal Housing Finance Agency's (FHFA) Notice of Proposed Rulemaking to establish the Enterprise Duty to Serve Underserved Markets. Given the government sponsored enterprises' (GSEs) ongoing importance in the housing finance markets, it is critical that these rules ensure that the GSEs fulfill their statutory responsibilities to meet their duties to serve – especially their responsibilities to support affordable housing preservation transactions.

HPN is a peer network and business alliance of 97 of the nation's top-performing nonprofit housing developers, owners, lenders, and housing counselors. The Network helps these strong, accomplished organizations increase their production and impact through a unique, member-driven cooperative that shares knowledge and innovation, pools resources to access the capital markets more efficiently, and shapes policy that reflects and enhances their practice. Through their partnerships with business, government, and civic leaders, the Network's members tackle the most pressing housing and economic development challenges facing communities. Collectively, the Network members have developed and/or financed more than 750,000 affordable homes and apartments and provided homeownership and foreclosure prevention counseling to more than 450,000 families.

Stewards of Affordable Housing for the Future is a 501(c) (3) consortium of nine sophisticated, non-profit, affordable housing providers who are committed to the long-term, sustainable affordability of multifamily rental properties for low-income families, seniors, and disabled individuals. SAHF members include: the Evangelical Lutheran Good Samaritan Society, Mercy Housing, National Church Residences, National Affordable Housing Trust, National Housing Trust, NHP Foundation, Preservation of Affordable Housing, Inc., the Retirement Housing Foundation, and Volunteers of America. Together, SAHF members own and operate housing in 50 states, the District of Columbia, Puerto Rico, and the U.S. Virgin Islands – providing homes to approximately 90,000 low-income households across the country. SAHF's members promote their shared ownership objectives, which embrace the notion that stable, affordable rental homes are critically important in people's lives.

The following comments address a variety of issues particularly relevant to the duty to serve the market for affordable housing preservation. We thank you, in advance, for your consideration of these recommended changes to the proposed rule and to working with you further in designing effective duties to serve.

1. Expansive and Inclusive Definition of Affordable Housing Preservation

As FHFA moves to finalize the duties to serve, we strongly urge you to write rules that encourage an expansive and inclusive set of properties that could qualify for affordable housing preservation treatment and a list of activities that would otherwise count toward the satisfactory fulfillment of the GSEs' duty to serve requirement for affordable housing preservation.

In this spirit, we urge FHFA to revisit its announced posture of not approving new products while the GSEs remain in conservatorship. This seems short-sighted and inconsistent with the purposes of the duties to serve provisions. The duties to serve should encourage new approaches and innovation. Congress designed the duties to serve to identify important national housing needs for which the markets were not adequately developed, and to encourage the GSEs to add their expertise and experience – as well as their capital – to helping address these needs and develop these markets. Certainly, with proper oversight, the GSEs could introduce new approaches to addressing underserved market needs in ways that are consistent with the overarching goals of the conservatorship. That is, the regulator could certainly support innovations that are managed in a safe and sound manner and priced such that that they provide some benefit to the tax payers who have invested so much in these companies.

We read the statute to allow the regulator to include other types of properties than those specifically enumerated by the Congress and applaud FHFA for including properties assisted under the neighborhoods stabilization program (NSP). However, we would urge FHFA to clarify what types of NSP activities would qualify. It does not seem consistent with the statutory objectives if the rule would allow the GSEs to fulfill the preservation duty to serve by assisting NSP properties that are neither rental nor affordable to low-income households. We would recommend that the final rule also include credit for properties supported by HUD's rent supplement (Rent Supp), rental assistance program (RAP), and Section 8 moderate rehabilitation programs. The tools currently available to HUD to support the preservation of these properties and to protect in tenants in these so-called "orphaned" programs are currently limited. Expanding the preservation options for these at-risk properties is addressed in preservation legislation before the Congress as well as in HUD's new initiative for the Preservation, Enhancement, and Transformation of Rental Assistance (PETRA). Likewise, with PETRA, the federal government has launched an initiative to recapitalize and preserve approximately 1 million units of publicly-owned housing in the United States. The preservation duty to serve should encourage Fannie Mae and Freddie Mac to provide capital for this effort. It would be a positive for national housing policy if the duty to serve supported these broader national policy efforts.

We would also propose that FHFA make it clear that preservation activities can also include financing or other interventions that serve to conserve energy consumption in multifamily housing. Reducing the operating costs of a development and lowering the utility costs paid by the tenants is consistent with the long-term preservation of the property as affordable housing.

The final rule should also make it clear that eligible activities could include a strategy of acquiring subsidized or unsubsidized properties (or a controlling interest in these properties), rehabilitating these properties, and restructuring the financing of these properties in order to preserve the properties as affordable housing over the longer term. Under a duty to serve approach to unsubsidized properties, a Fannie Mae or Freddie Mac business partner might acquire market rate properties that were not previously subsidized, but would agree, through the use of other subsidies and the application of use restrictions, to structure the deal as a long term affordable housing preservation transaction. With the current softness in the multifamily real estate markets, preservation entities have the potential to pursue a strategy that begins with the acquisition of unsubsidized properties with relatively low and affordable market rents, and then structure the properties' management and capital structure to keep the properties affordable over the longer term, with or without subsidy. Without subsidy, the acquiring entity could commit, through a restrictive use agreement, to keep the property affordable at market rents for low- and moderate-income households as workforce housing. This approach might be particular effective in dealing properties owned or which come into the portfolios of the GSEs.

2. <u>Enterprise Involvement with Low Income Housing Tax Credit Properties</u>

The Low Income Housing Tax Credit (LIHTC) program is the most important federal government capital program for the preservation of affordable housing. Before the recent economic crisis, the Enterprises played an outsized role as investors in affordable housing tax credits. In fact, Fannie Mae and Freddie Mac were at one time the largest and most reliable investors in housing credit. As the Enterprises withdrew from the housing credit markets, along with other traditional investors during the recent crisis, prices paid for the credits fell and many developments with tax credit allocations lacked investors altogether. The abrupt market change disrupted many affordable housing developments and preservation projects around the country. The federal government stepped in and provided state agencies with the ability to exchange unused credits for grant dollars in 2009, allowing many projects to go to closing. However, these markets are not yet restored to pre-crisis health.

While it is hard to argue that Fannie Mae and Freddie Mac should return to the markets as equity investors in the LIHTC program until they return to profitability, there are numerous ways in which the GSEs could support the housing credit market consistent with their new preservation duty to serve.

First and foremost, we note that the discussion in the proposed rule of the GSE participation in the LIHTC market only makes reference to the Enterprises' roles as equity investors in tax credit deals. In fact, the GSEs have participated in these housing-credit related affordable housing transactions on the debt side also. Clearly, it is consistent with the spirit and the language of the duties to serve to encourage robust GSE participation in the debt financing of LIHTC transactions where these are focused on the longer-term preservation of affordable housing.

Secondly, as preeminent investors in tax credit equity, Fannie Mae and Freddie Mac remain owners of many affordable housing properties around the country – many of which have reached or will reach the end of their 15 year tax credit compliance period during the period of time covered by the duties to serve. We would urge the final rule on duties to serve to make it clear that the GSEs would get credit against the duties to serve obligations in those instances where they transferred or sold their ownership interests in tax credit properties to a nonprofit owner for the purpose of continued affordability of the property.

Given the recent travails in the housing credit market and the continuing fragility of the market, we supported the decision earlier this year by FHFA and the Treasury Department to block a proposed sale of Fannie Mae's tax credit portfolio. At the time we wrote that the proposed transaction "could undermine future pricing for the tax credit transactions…" and that "…[l]ower prices would dramatically reduce the production and preservation of affordable housing." We continue to urge you to consider the dampening effects that the underutilized Fannie Mae and Freddie Mac portfolios may have on pricing in the current market and to urge caution going forward should additional opportunities for the sale of these tax credit portfolios arise. Any future proposals regarding such transfers need to fully consider the potentially negative effects of secondary market sales on the market prices for housing credits and the effects of these lower prices on affordable housing opportunity.

In crafting the final rule, we would also recommend that the duties to serve are implemented in a way that encourages innovation by the GSEs in expanding the portion of the affordable housing market supported by LIHTC. Specifically, the Enterprises could serve a powerful and needed role in helping to restore a healthy LIHTC market by introducing a secondary market for trading tax credit equity positions. With the expertise in tax credit risk and compliance management built up by the GSEs over the years, the two companies are uniquely positioned in the market to create a trading mechanism and a guarantee program that would allow the more efficient transfer of tax credits among entities with different needs for tax-advantaged investments. The GSEs could play an important role in bringing greater liquidity to this market and help to overcome some of resistance that new investors might have to investing long-term in tax credits. We strongly urge FHFA to work with Fannie Mae and Freddie Mac to bring this important service to the market.

3. <u>Multifamily Real Estate Owned (REO) and Loss Mitigation Opportunities</u>

The Government Sponsored Enterprises also have another powerful opportunity to support affordable housing preservation through the creative disposition of their real estate owned (REO) portfolios. As Fannie Mae and Freddie Mac acquire properties that go into foreclosure, this unfortunate moment creates a terrific affordable housing preservation opportunity. The transfer or sale of these properties, with seller financing, should be strongly encouraged in the duties to serve provisions. In this instance, we would again recommend that FHFA look at the definition of preservation broadly to allow Fannie Mae and Freddie Mac to utilize their entire multifamily REO inventory for preservation activities of this nature and not just limit qualifying transactions to previously subsidized developments. In undertaking loss mitigation efforts with respect to their loan portfolios, the GSEs should also be encouraged to consider including long-term affordability commitment obligations as consideration from borrowers for entry into certain restructuring arrangements.

4. More Flexibility in Underwriting

The duties to serve provisions are clearly meant to encourage greater underwriting flexibility on the GSEs' parts in order to support the enumerated market segments. The GSEs should apply more flexibility in their underwriting requirements for deals involving affordable housing. Increased flexibility does not imply that the GSEs need to take on additional risk. We note positively that the Fannie Mae and Freddie Mac have moved to loosen up their requirements for affordable housing finance, especially with respect to their prior underwriting requirements on Section 8 rental assistance appropriations risk. Previously the GSEs had required inordinate operating reserves to cover the appropriations risk, sucking significant resources out of the transaction for unproductive uses and setting a standard for lending industry that makes preservation more difficult. The GSEs will now take this appropriations risk in most instances. These kinds of underwriting changes and flexibilities should be fostered by the duties to serve regime.

More generally, the GSEs have adopted a set of underwriting requirements addressing many different aspects of a financing transaction. In the average case, this is an efficient approach, allowing conventional loan applications to be evaluated quickly, without the need for extensive analysis by GSE staffs. However, affordable housing preservation transactions often come with preexisting conditions or quirks that make them not strictly compliant with one or more of these many underwriting standards. If the GSE underwriting standards are rigidly applied in a "one-size-fits-all" manner, preservation transactions will be rejected out of hand for GSE financing. The duties to serve should help the GSEs adapt their approaches to nonstandard transactions. The Enterprises should consider the track record of experienced and successful preservation developers and place more reliance on the sponsor quality to increase their confidence in project proposals.

5. Toward an Open and Transparent Process

We support the proposed requirement for the Enterprises to file an "underserved markets plan" to shape their duties to serve activities. We would strongly urge FHFA to make these underserved market plans available to the public shortly after these are filed by the GSEs and allowing the public to review and comment. The public input can only serve to improve the regulator's assessment of the adequacy of the plan and could add to the innovation and impact that the duties to serve are supposed to have with respect to how these markets operate.

Finally, we would urge FHFA to adopt a more rigorous evaluation process for the performance of each GSE against its own underserved market plan. The proposed evaluation outcome of a "satisfactory" versus an "unsatisfactory" rating seems insufficiently imprecise. We would recommend a grading scale with more granularity and levels of performance. We would also recommend that the grading include a report by FHFA on the GSE activities under their duties to serve that includes both the qualitative and quantitative metrics against which the GSEs performances were calibrated. A meaningful report could also include comments from the public and comparisons to other financial institutions operating in these markets as a basis for the regulator's assessments.

Thank you for the opportunity to comment on these important issues.

Sincerely,

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