July 11, 2022

Director Sandra Thompson
Federal Housing Finance Agency
400 7th Street, SW
Washington, D.C. 20219

Re: FHFA Director Meeting Request & Recommendations

Dear Director Thompson,

The Local Initiatives Support Corporation (LISC) congratulates you on your confirmation as the Director of the Federal Housing Finance Agency. We applaud FHFA for taking significant actions under your tenure to promote affordable housing opportunities through its regulator and conservatorship role of the Government Sponsored Entities (GSEs). LISC was very pleased that FHFA increased Low-Income Housing Tax Credit (LIHTC) equity investments limits, strengthened Duty to Serve plans, increased Affordable Housing Goal commitments, and focused the GSEs on incorporating racial equity into their work through the new Equitable Housing Finance Plan process. These actions will help LISC and our partners create and preserve additional affordable housing.

Established in 1979, LISC is a national nonprofit housing and community development organization and certified community development financial institution (CDFI) 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. Our organization has a nationwide footprint, with local offices in 38 cities. In 2021, LISC invested over $2 billion in support of affordable housing developments across the county, primarily through the National Equity Fund (NEF), LISC's LIHTC syndication group.

LISC offers the recommended actions below to increase affordable housing options for low-income families through your work with the GSEs. We also request a meeting with you and your staff to discuss these in further detail and to understand your priorities.

Recommendations

Low-Income Housing Tax Credit

In 2017, FHFA allowed the GSEs to reenter the LIHTC market as equity investors, setting a $500 million cap, with $200 million required for mission related activities. This was important since the mission related activities focus helped provided equity for underserved markets. It also broadened the investor market after corporate tax rates were lowered from 35 percent to 21 percent, resulting in lower LIHTC equity pricing. Last year, FHFA raised the investment cap by $350 million for Fannie Mae and Freddie Mac, for a total of $1.7 billion. Any investments above $300 million in a given year are required to be in areas that have been identified by FHFA as markets that have difficulty attracting investors. These investments are designed to preserve affordable housing, support mixed-income housing, provide supportive housing, support rural housing projects, or meet other affordable housing objectives.

The Administration indicated in its recent Housing Supply Action Plan that the Enterprises anticipate further growing their LIHTC equity investments this year. LISC supports increases in the GSE's equity investment caps and recommends that they be adjusted by an inflationary factor going forward and that a portion of this extra investment authority continue to be dedicated to underserved LIHTC markets. These investments should also be eligible for DTS credit. This will allow the GSEs to increase their investment activity for projects difficult to finance and is especially important as Congress has expanded the LIHTC program through the establishment of a 4 percent floor for bond financed deals and provided $2 billion in disaster Housing Credits.

The LIHTC market is also subject to regulatory uncertainty as the federal banking regulators work together to revise the Community Reinvestment Act (CRA) regulations. The proposed rule out for comment would remove the Investment Test, which if ultimately adopted in a new CRA final rule could have negative impacts on LIHTC pricing. In addition, Congress is currently considering a further expansion of the LIHTC program, which will increase the need for investors. FHFA should continue to increase the GSE LIHTC cap beyond annual inflationary adjustments if the program receives additional resources from Congress or experiences negative pricing impacts from a new CRA regulation.

LISC was pleased that Freddie Mac developed LP transfer limitation language in 2021 with a subset of syndicators to help preserve the ability of nonprofit general partners (GPs) to exercise their Right of First Refusal (ROFR) rights as allowed in Section 42(i)(7). In recent years, there has been abuse of this provision, which has threatened the continued affordability of many Housing Credit developments by not allowing the nonprofit GPs to obtain ownership of LIHTC properties at a minimum purchase price at the end of the initial 15 year compliance period. Freddie indicated in their 2022-2024 Duty to Serve plan that they will include the ROFR language they developed in 2021 in all transactions with nonprofit GPs in order to help preserve nonprofit control and long term affordability. This will be available through all LIHTC syndicators. LISC applauds this action and encourages FHFA to instruct Fannie to include similar language to help nonprofits maintain control of these properties, as intended in the law.

In addition to strengthening ROFR protections, we believe that FHFA can help preserve LIHTC properties by stating the GSEs going forward won't purchase loans from lenders that finance properties utilizing the Qualified Contract (QC) process. Under the QC provision, an owner of a LIHTC property may, after year 14, request a QC from the Housing Credit allocating agency. This begins a one-year period during which the allocating agency seeks a qualified buyer to purchase the property and maintain it as affordable for the duration of the extended use period. The required purchase price for a qualified contract is stipulated by Section 42 and was designed to prevent backend windfalls to owners and investors by limiting them to an inflation-adjusted return on the original equity contribution. While the original intent of this provision was to create a limited return and some liquidity for investors at a time when the Housing Credit was an unproven program, for some properties it has come to function as a nearly automatic affordability opt-out after just 15 years of affordability. This is because the QC formula price in nearly all cases significantly exceeds the market value of the property as affordable housing. As a result, it is rare for the allocating agency to find a buyer willing to pay the qualified contract price. If the allocating agency fails to identify a qualified buyer within one year, the property is released from the affordability requirements of the program.

The current LIHTC QC language is being used by some owners to remove properties from the LIHTC program after year 15, which results in a loss of affordability housing. Until such time as the LIHTC QC *legislation is changed to rectify this problem, the GSEs should not be allowed going forward to purchase loans from lenders which support this activity at the property level.*

Duty to Serve and Investments in CDFIs

LISC strongly supports the efforts of FHFA and the GSEs to support underserved markets through the Duty to Serve regulation. We applaud the thoughtful and creative work which has been done to date, particularly with affordable housing preservation programs.

LISC believes that the Duty to Serve effort should focus primarily on supporting and expanding transactions that improve affordable housing opportunities in underserved geographies and for low-income populations. The efforts of the GSEs pursuant to their Duty to Serve should be evaluated by the extent to which they facilitate *more* transactions to create or preserve these types of housing opportunities, particularly for households at the lowest end of the income spectrum. This is why LISC was pleased that FHFA rejected the previous DTS plan submissions since they provided *less* support and approved new three year plans which will scale their activities.

We believe the types of transactions that will expand housing choice and opportunity for underserved areas and low-income households are often smaller, more labor-intensive, and have different risk profiles than is typical in conventional mortgage underwriting. CDFIs have worked in underserved communities for many years and have first-hand knowledge of local markets and partners. We are adept at mitigating the risks that are often inherent in investing in them. With our strong loan portfolios, CDFIs are natural partners for expanding responsible investment in these markets, especially where there is little other support from GSE lenders.

LISC thanks FHFA for ensuring strong DTS plans from the GSEs for 2022-2024. We encourage FHFA to continue to hold the GSEs accountable for meeting these activity levels and to continue to engage stakeholders such as the Underserved Mortgage Market Coalition.[1]

LISC was pleased that Fannie's new three year DTS plan states that it "will explore the feasibility of investing in one or more CDFIs to provide improved access to affordable mortgage lending to consumers in high needs rural regions." This is a welcome advancement since a plain reading of the authorizing statute for DTS indicates the GSEs have the authority to invest in CDFIs performing DTS activities. LISC recommends that FHFA encourage the GSEs to make equity or equity like investments in CDFIs through other DTS activities, especially where they are having challenges making progress through their lender network.

Affordable Housing Program Revolving Loan Fund Regulation

In 2006, the Federal Home Loan Banks were provided authority in the Affordable Housing Program (AHP) regulations to provide AHP awards for revolving loan funds. The revolving loan fund provisions were designed to support distinct projects in specific locations, or for pipelines of expected projects meeting specific criteria. In 2018, FHFA revised the AHP regulations and stated in the proposed rule that it may undertake separate rulemaking to modernize the revolving loan fund provisions since very few FHLBs have provided AHP awards for this purpose.[2]

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 subregulatory requirements. Applicants requesting to utilize AHP resources for revolving loan fund activities are often disadvantaged

[1] https://www.lisc.org/media/filer_public/57/36/5736bac2-f8a8-4a3d-8ff6-672b5e65d955/071621_policy_comments_duty_to_serve.pdf
[2] https://www.govinfo.gov/content/pkg/FR-2018-03-14/pdf/2018-04745.pdf

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 FHLBs 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.

LISC supports increased use of AHP funds for revolving loan fund activity and encourages FHFA to revise the regulations to better support CDFI affordable housing lending. Creating opportunities for AHP resources to be utilized for affordable housing lending opportunities will allow the resources to be more responsive to local market needs and achieve higher leverage and impact.

Equitable Housing Finance Plans & Racial Equity

In September, 2021 FHFA announced that Fannie Mae and Freddie Mac would submit Equitable Housing Finance Plans identifying and addressing barriers to housing opportunities, including their goals and plans for advancing equity in housing finance. On June 8, FHFA announced the release of these three year plans, which will accompanied by annual progress reports. This new requirement is intended to reduce racial and ethnic disparities in homeownership and rental housing and was released after FHFA and the U.S. Department of Housing and Urban Development signed a memorandum of understanding regarding fair housing and fair lending coordination.

FHFA has already incorporated a racial equity focus through other actions, including issuing stronger Affordable Housing Goals, with a focus on ensuring that the GSE's activities reach low- and moderate income households, minority communities, rural areas, and other underserved populations. Rightfully, the new Affordable Housing Goals include two new goals, which set production targets for single-family home purchase activities in communities of color and low-income neighborhoods.

LISC supports the strengthened Affordable Housing Goals and Equitable Housing Finance Plans. We encourage the GSEs to address racial equity issues through all of their work, including Duty to Serve. Many, if not all of the DTS activities, disproportionately impact racial and ethnic minority households. While the authorizing statute for DTS does not require FHFA or the GSEs to address such issues, LISC encourages FHFA to explicitly incorporate racial equity components in all relevant DTS activities and reporting. This should include providing the public with disaggregated reporting and supporting research that shows how the DTS activity affected racial and ethnic minorities.

LISC also recommends that FHFA continue to work with the GSEs and public to strengthen the Equitable Housing Finance Plans. For instance, Freddie's plan states it will conduct research on evictions during the first year and then phase in tenant protections in the second and third years of the plan. Fannie didn't include similar actions in their plan. Presumably, Freddie will include eviction protection requirements with properties receiving GSE multifamily mortgages. LISC agrees with the Urban Institute that rental housing projects receiving financing through both Fannie and Freddie should agree, as a term of the financing, to engage in eviction only as a last resort. In practice, this means only allowing just cause evictions such as nonpayment of rent or lease violations.[3] We also agree that properties receiving such financing should include source of income discrimination protections, so that tenants with public assistance benefits such as Section 8 Housing Choice Vouchers are better able to access rental housing.

FHFA should also utilize the large amount of data maintained by Freddie Mac and Fannie Mae to further equitable housing outcomes. LISC agrees with outside researchers that the FHFA should instruct the

[3] https://www.urban.org/research/publication/fhfas-equitable-housing-finance-plans-fannie-mae-and-freddie-mac-equity-should-be-primary-business-consideration-gses

GSEs to create an equity finance focused public use database so that advocates and the public can better understand the GSEs role in these issues. Recent research utilizing Freddie Mac's data has shown how pervasive racial bias is in the appraisal process. These learnings enable the public to better understand such inequities and how to structure policy solutions.[4]

Speculation in the Multifamily Housing Market

LISC and our partners released a report earlier this year, which explored the relationship between speculative practices in the multifamily housing market and its impact on tenants in the form of housing maintenance quality and evictions.[5] The report found that:

- Lower-income, Black and Latinx neighborhoods seeing signs of gentrification experienced more speculation than whiter, wealthier areas;
- Tenants suffered in buildings that were sold for higher values and that took on more debt;
- Landlords who acquired properties at higher values or who took on more debt evicted their tenants at 1.5x the rate of others who owned similar properties in comparable neighborhoods; and
- Properties that received affordable-housing investments were significantly better maintained than properties in similar neighborhoods without such investments. They were also less likely to be acquired at higher values or to take on higher debt levels than properties in similar neighborhoods—in other words, they were more likely to be removed from the cycle of disinvestment and speculation.

LISC recommends that FHFA examine how the GSE's multifamily loan purchase activity impacts tenants and rents. Fannie and Freddie provide large sources of liquidity in the multifamily housing rental market, and have recently come under scrutiny for financing provided to large private equity landlords that have displaced tenants. FHFA should work with GSEs to: 1) examine their existing loan portfolios to ensure tenant well-being, with additional scrutiny of transactions where there are large projected rent increases without significant capital improvements to the property; 2) scrutinize new prospective lenders for their track record, and to make sure that new debt purchases are used to preserve the quality of property and its affordability, and to prevent displacement; and 3) utilize the Equitable Housing Plan process to prioritize racial equity goals by advancing low-cost financing for high-quality, deeply and permanently-affordable affordable developments and social housing projects. We believe these actions, in conjunction with Duty to Serve and Equitable Housing Finance Plan activities, can meaningfully improve tenant well-being and further affordable housing options.

Thank you for considering our recommendations and Mark Kudlowitz (mkudlowitz@lisc.org), LISC's Senior Director of Policy, will reach out to your staff to request a meeting to discuss them and your priorities.

Sincerely,

Matthew Josephs
Senior Vice President, LISC Policy

Matthew Reilein
President and CEO, National Equity Fund

[4] https://www.freddiemac.com/fmac-resources/research/pdf/202109-Note-Appraisal-Gap.pdf
[5] https://www.lisc.org/media/filer_public/fc/26/fc26b3d0-8d45-41d6-a90c-f3b9966b7796/032422_gambling_with_homes_or_investing_in_communities.pdf