January 3, 2014

Regulations Division
Office of the General Counsel
Department of Housing and Urban Development
451 7th Street S.W.
Washington, D.C. 20410-0500

Re: Small Multifamily Building Risk Share Initiative: Request for Comment
Docket No. FR-5728-N-01

Dear Sir or Madam:

On behalf of the undersigned organizations, please accept comments on the above-referenced notice, published in the *Federal Register* on November 4, 2013. Our organizations represent multifamily developers, property owners, property managers and housing cooperatives who use federal and state government programs to finance affordable multifamily rental and cooperative housing, including Federal Housing Administration (FHA) mortgage insurance and Low Income Housing Tax Credits.

The Notice announces the U.S. Department of Housing Urban Development's (HUD) intention to implement a new initiative designed to facilitate the financing of small multifamily rental properties using the FHA Risk Share program. The initiative would allow certain mission-oriented lenders to participate in the FHA Risk Share program, provided they meet certain requirements. The initiative is limited to the financing of existing properties with 5 to 49 units or which do not exceed a loan amount of three million dollars. The initiative excludes new construction as an eligible activity.

We appreciate that HUD is interested in providing new means for financing small multifamily rental properties. Over the years, our organizations have urged HUD, as well as Fannie Mae and Freddie Mac, to develop a more streamlined program for financing such properties. We agree with HUD's assessment that owners of small rental properties face difficulty accessing financing due to diminished lending in this area, a reduction in financing by community and regional banks in the wake of the 2008 recession, and increasingly higher credit standards.

HUD notes that it has requested statutory changes to section 542(b) of the Housing and Community Development Act of 1992 that would allow loans originated under this initiative to be securitized by Ginnie Mae. Providing a secondary market outlet for these loans would greatly enhance the potential of the program to reach more property owners. The statutory changes also include the removal of the current affordability restrictions in order to reduce the burden on owners who access this capital, because the majority of such properties already house low and moderate income households. We agree that both statutory changes are desirable and would make a significant difference as to the success of the initiative.

Absent the statutory changes, HUD is proceeding with a more limited initiative. While we support the proposed initiative, we have some suggestions for HUD's consideration, as follows.

- <u>Expand the universe of eligible lenders</u>. The Notice requires that all participating lenders become FHA-approved lenders, but the proposal excludes FHA lenders that do not meet HUD's definition of "mission-driven" lenders. HUD states that it is limiting the initiative to mission-driven nonprofit and public lenders, or consortia of for-profit private lenders which form a joint venture with, or under the control of, a mission-driven nonprofit or public lender because of the current statutory income limit restrictions. Many FHA lenders are well-versed in financing loans for affordable rental properties and would bring a substantial level of expertise to the program. We recommend that existing FHA lenders who wish to participate and can meet the other requirements be permitted to do so.

- <u>Consider revising participant qualifications.</u> We have concerns that community development financial institutions (CDFI) and small banks may have difficulty in meeting the proposed qualifications to participate. We encourage the Department to look at ways to adjust requirements for these financial institutions in order to create and build capacity. Additionally, we support using partnerships with existing FHA lenders to assist with transaction processing and to build experience and added capacity.

- <u>The pilot should not exclude the financing of new construction</u>. There are many parts of the country where development of new units is as critical as renovation of the existing rental housing stock. This is coupled with the need to meet the pent-up housing needs of senior citizens, the disabled, and low- and moderate-income households. With access to the risk-share initiative, participating lenders could expand their financing in markets where demand for small rental properties, such as in rural areas, is growing.

- <u>Flexibility in loan terms is necessary, including minimum occupancy.</u> The minimum occupancy requirement of 93 percent for refinancing would exclude many small properties. For example, in a 10-unit property, a single vacancy would not meet the 93 percent threshold and would be ineligible for refinancing. Occupancy requirements should take into consideration property size, break-even occupancy after debt and reserves and property history. There is precedent for such measures and flexibility among FHA programs, such as Section 223(f), that requires 85 percent occupancy.

- <u>Flexibility in documentation requirements may be appropriate.</u> Many of the owners of smaller properties have limited budgets and rely on the funds from operations as their cash flow and profit. The cost of audited accounts and reports is likely to stretch the resources of the borrower. This risk-share pilot is intended to improve liquidity for small rental properties, but the requirements in the notice suggest barriers that may discourage smaller lenders and property borrowers. We offer the following examples of requirements that could be modified:

    - *Audited Financial Statements:* Small property owners produce financial statements that lenders review, but not audited statements. If the lender is willing to share the risk, HUD should accept that.

    - *Third-Party Services:* The proposal suggests that owners/landlords of small rental properties secure a variety of costly professional services (e.g., architecture, engineering, construction and market analysis). The reality is that lenders and owners/landlords of small properties are usually working with their own employees on loans, construction and approvals, as well as appraisals, environmental analysis, and legal review.

  - *Affirmative Fair Marketing Plans*. Small property owners adhere to existing anti-discrimination statutes, and would certify that they do not discriminate, but many do not have Affirmative Fair Housing Marketing plans.

- <u>Balloon mortgages may create issues for smaller banking institutions</u>. The ultimate purpose of this pilot is to gain access to the secondary market for mortgages on smaller properties in order to increase liquidity in the market. However, absent the securitization of the loans through Ginnie Mae, the compelling requirement for 35-year loan terms is not as material. For purposes of the pilot, requiring long-term self-amortization loans does not match bank liability and shorter-term lending practices. The refinance risk could be mitigated with an amortization period of 30 years for loans of 10-15 years and still provide longer term debt that typically is available through traditional banking relationships. We recommend that lenders in the pilot be allowed to finance shorter-term loans with 30-year amortization schedules.

- <u>Affordability requirements should be at the property level.</u> Small rental multifamily properties are inherently affordable and unsubsidized. While the notice provides some flexibility in mandating that these affordability requirements be satisfied through a deed restriction, we want to confirm that the affordability obligation is not specific to units, but to the property.

The proposed pilot program is an important effort to increase liquidity for owners and operators of small multifamily rental properties. We encourage HUD/FHA to carefully consider ways to expand the pilot through greater flexibility and wider lender participation, which we believe will better inform HUD as to the benefits of risk sharing for small properties. Given the anticipated limited exposure to the government, both in pilot scope and through the risk-share provisions, latitude to encourage small loan financing outweighs mortgage performance risk.

We appreciate the opportunity to comment and welcome the opportunity to provide additional information as necessary.

Sincerely,

Council for Affordable Rural Housing
Institute for Real Estate Management
National Affordable Housing Management Association
National Apartment Association
National Association of Home Builders
National Association of Housing Cooperatives
National Leased Housing Association
National Multi Housing Council