



National Council of
State Housing Agencies

Put Housing to Work for People and the Economy Unleash the Power of State Housing Finance Agencies

State Housing Finance Agencies (HFAs) and their partners stand ready to produce tens of thousands of affordable homes for America's low- and moderate-income families, generating tens of thousands of jobs and hundreds of millions of dollars in tax revenue. HFAs call on the new Administration and Congress to unleash this activity by removing barriers the economic crisis has put in the way of HFA efforts to deploy federal housing resources critical to our country's housing recovery. HFAs urge the new Administration and Congress to take several immediate steps to bring to bear the proven power and performance of HFAs to spur home buying and rental housing production through the tax-exempt Housing Bond and Low Income Housing Tax Credit (Housing Credit) programs.

State HFAs play an indispensable role in the delivery of federal housing resources. They bring statewide perspective and focus, along with a deep understanding of the needs of their local markets. HFAs possess sophisticated finance, underwriting, and asset management capacity and a multi-decade record of responsibility, effectiveness, accountability, and success in administering tens of billions of dollars of housing assistance. They combine hard-headed business acumen with a mission-oriented public purpose to harness private capital to provide affordable housing.

In strong and weak economies, HFAs have been a constant, reliable source of flexible, affordable mortgage money for lower-income first-time home buyers, anchoring the first-time home buyer market. Using single-family Housing Bonds or, as they are commonly known, Mortgage Revenue Bonds (MRBs), HFAs have made 2.6 million families first-time homeowners, adding another 100,000 families each year.

HFA MRB loan performance is strong, with delinquency and foreclosure rates well below those in the conventional market, even today. HFAs never turned to subprime mortgage products. Through flexible yet prudent underwriting and often the added help of down payment assistance and home counseling that they uniquely provide, HFAs have proven over many years that homeownership is not only possible for lower-income families, it is sustainable.

Recognizing that not everyone is ready or suited for homeownership, HFAs and their partners have produced nearly 2 million affordable rental homes with equity provided by the Housing Credit. Nearly half of these homes are multifamily Housing Bond-financed. HFAs have financed nearly another 1 million affordable rental homes with Housing Bonds alone.

Using Housing Bonds and the Credit, HFAs add another 150,000 homes to our country's affordable rental housing inventory each year.

Recognizing HFAs' strong and enduring track record and capacity, Congress and the Administration earlier this year provided states under the Housing and Economic Recovery Act (HERA), \$11 billion in new Housing Bond authority, to be available in 2008 through 2010 to finance affordable single-family and multifamily mortgages. They also granted states a 10 percent increase in Housing Credit authority in 2008 and 2009, amounting to an additional \$60 million in Credit this year, to produce affordable rental housing. In addition, they provided Alternative Minimum Tax (AMT) relief to make Housing Bond and Credit investments more attractive, temporary authority to use Housing Bonds to refinance subprime mortgages, and increased flexibility to achieve Housing Credit development for underserved people and places.

With these new resources, HFAs were poised this year to produce 100,000 affordable homes in addition to the 250,000 homes they would otherwise generate with their annual Housing Bond and Credit allocations. However, HFA efforts to put all of these resources to work have been severely stymied by the deepening economic crisis, which has significantly diminished investor interest in Housing Bonds and Credits, reducing the amount of funds HFAs have available to finance affordable home mortgages and multifamily loans, increasing the cost of the mortgages they do make, and shrinking their affordable rental housing production.

The sidelining of HFAs could not come at a worse time for our housing and economic recovery. HFAs are virtually the only source of affordable, flexible mortgage money available today to lower-income first-time home buyers. Meanwhile, the opportunity for HFAs to help lower-income families access homeownership is greater now than in some time, with the increased affordability created by today's declining home prices and the expanded low-cost housing stock produced by record home foreclosures.

HFAs report that demand among first-time home buyers for their mortgages far exceeds the volume available. Constraints on the ability of HFAs to respond to this first-time home buyer demand also negatively impact the broader housing market, as homeowners looking to trade up are unable to sell their homes to first-time buyers.

Demand for affordable rental housing is also up, while its already short supply continues to dwindle. Even at full production, the Housing Credit does not begin to replace the low-cost rental housing lost each year to conversion, demolition, and abandonment. At a time when skyrocketing foreclosures are driving more families to affordable rental housing, the Housing Credit is expected to generate less than two-thirds its usual annual production this year. Meanwhile, developer applications for Housing Credits continue to outnumber those that receive allocations by a ratio of two to one nationally.

The Challenge

Investor interest in Housing Bonds and the Credit has diminished dramatically over the last six months because of declining investor income, financial institution deleveraging, and growing uncertainty about the national economic outlook, especially real estate. Fannie Mae and Freddie Mac, traditionally large purchasers of Housing Bonds and the Credit, are out of both markets. Other traditional Housing Bond purchasers, such as banks, mutual funds, property and casualty insurance companies, and other financial institutions, have strictly limited their purchases or have dropped out of these markets altogether.

Consequently, HFAs are virtually frozen out of the Housing Bond market, unable to find investors willing to buy their long-term fixed-rate bonds at rates low enough to enable HFA funding of below-market rate mortgage products. In the absence of ready investors, the Housing Bond issuance queue continues to build, with 43 HFAs recently reporting a backlog of more than \$7 billion in Housing Bonds that they need to bring to market in the next six months.

In the meantime, HFAs scramble to keep their lending programs operating, selling modest amounts of short-term bonds to retail investors, relending loan sale proceeds, accessing credit lines, and tapping their own resources. Many HFAs have been forced to severely curtail their lending programs; seven have suspended single-family lending altogether.

The situation is even worse for the 38 HFAs with a total of \$30 billion in Variable Rate Debt (VRD) outstanding. These HFAs issued VRD in recent years to offer mortgages at interest rates lower than those supportable by fixed-rate debt. Today, these HFAs are struggling to find buyers as they remarket this debt, as traditional VRD investors, such as money market funds, have moved away from the market. If HFAs fail to remarket their VRD, which many need to do as frequently as weekly or monthly, they will be forced to repay it under aggressive amortization schedules, undermining their otherwise strong financial positions, potentially weakening their financial ratings, and diverting resources from productive housing activity.

The Housing Credit market is experiencing similar turmoil. With investor demand down dramatically, insufficient capital has been raised to purchase all the Credits states have allocated this year. Many traditional Housing Credit investors have limited or no capital to invest or tax liability to offset. Others are seeking higher returns in other sectors of the economy.

Industry experts estimate that for every two dollars of Credit HFAs allocate today, little more than one dollar of equity is available in the market. The lack of investment dollars has driven down the value of the Credit, with a dollar of Credit generating 70 cents or less in equity today, compared to a dollar or more just over a year ago. This means developments allocated Credits are receiving less equity with their sale, leaving funding gaps that HFAs are struggling to fill from other sources. Some developments, particularly those located in economically distressed areas or those perceived by investors as relatively risky, are not attracting investment

dollars at all. Experts estimate that overall, this year's Housing Credit market is short as much as \$5 billion in equity, jeopardizing the production of 40,000 affordable rental homes.

HFAs have turned in recent months to the housing GSEs—Fannie Mae, Freddie Mac, and the Federal Home Loan Banks—for help, even appealing to their new regulator, the Federal Housing Finance Agency (FHFA), to intervene. Until recent years, Fannie Mae and Freddie Mac had been large purchasers of Housing Bonds and the Credit, historically buying as much as half of all long-term Housing Bonds issued and more than a third of all Housing Credits allocated by HFAs annually. They also had been large purchasers of HFA loans. Several of the Federal Home Loan Banks have historically provided HFAs liquidity, through credit lines, advances, and taxable bond purchases, to support their lending programs.

So far, however, the housing GSEs have committed to do little to help HFAs through this difficult time. Fannie Mae and Freddie Mac have told HFAs they cannot buy their Housing Bonds and are unlikely to buy Housing Credits. Both are willing to consider the purchase of HFA loans, but only those that meet their increasingly tight credit and underwriting standards. Fannie Mae has made a limited \$500 million line of credit available to top-rated HFAs to support single-family lending, but that line has already been fully committed and may not be expanded.

Both Fannie Mae and Freddie Mac cite many constraints on their ability to help, including the debt ceilings imposed on them by their conservatorship agreements, the difficulty they face in raising capital and their increased cost of funds, the limited value to them of tax-advantaged assets, and their ever more conservative risk management and credit policies.

Several Federal Home Loan Banks have stepped up to help HFAs, with six banks—Chicago, Cincinnati, Dallas, Des Moines, Pittsburgh, and Topeka—recently providing HFAs assistance through standby bond purchase agreements, credit lines, and taxable bond purchases. The FHFA is encouraging the other banks to follow suit.

Recognizing the severe constraints on Fannie Mae and Freddie Mac, Treasury and the Federal Reserve launched in recent weeks an \$800 billion housing and consumer credit initiative that includes a \$100 billion commitment to buy GSE debt and a \$500 billion pledge to purchase GSE mortgage-backed securities. Without specific directives from Treasury and the Federal Reserve, however, this intervention alone is unlikely to cause Fannie Mae and Freddie Mac to assist HFAs, as it does not overcome the GSEs' overly rigid loan standards, increase their debt ceilings, or sufficiently lower their cost of capital.

More recently, the press has reported a potential Treasury and Federal Reserve initiative to stimulate home buying with a low-interest rate mortgage program run through Fannie Mae and Freddie Mac. HFAs need to be a part of any such program to ensure that its benefits are shared by the lower-income families HFAs so successfully serve and to enable such families to enter the market at even more affordable rates. By utilizing the proven HFA delivery system,

this program could reach many more worthy home buyers, for whom an interest rate break alone will not be sufficient to access homeownership. HFAs are also uniquely positioned to direct these mortgage resources to areas where they will have the greatest impact on stabilizing declining or vulnerable markets and promoting economic growth.

The Solutions

State HFAs ask the new Administration and Congress to put the Housing Bond and Credit programs to work for lower-income people and the economy by taking the following immediate steps to—

Unlock the Housing Bond program:

- Require Treasury to use Troubled Asset Relief Program (TARP) funds or other resources available to it to purchase long-term fixed rate Housing Bonds at reasonable rates, which will establish the market and draw in other investors.
- Encourage Treasury and the Federal Reserve to establish liquidity facilities for: HFA VRD, to attract buyers for this short-term debt by pledging to step in and purchase it if there are no other buyers when its terms call for it to be remarketed; and for HFA long-term, fixed-rate Housing Bonds, to attract investors by making funds available to them to purchase these bonds.
- Encourage the Federal Reserve to condition its GSE debt and mortgage-backed securities (MBS) purchases on GSE commitments to use a portion of the funds they receive to buy HFA Housing Bonds and provide HFAs liquidity to support their lending programs.
- Direct Fannie Mae and Freddie Mac to advance their affordable housing mission by supporting HFAs by buying their Housing Bonds and providing them liquidity through loan purchases, including FHA-insured loans, on reasonable terms and other means. Support these activities by increasing the GSEs' debt ceilings, relaxing the limit on the amount of their assets they can invest in tax-exempt bonds (the so-called 2 percent De Minimis Rule), and awarding them affordable housing goals credit for these activities.
- Direct the Federal Home Loan Banks to advance their affordable housing mission by providing HFAs liquidity on reasonable terms.
- Change the Housing Bond law, so as not to require issuers to designate housing purposes when they carry forward unused bond authority from one year to another, and extend HERA's AMT exemption to prior-year Housing Bond authority carried

forward to 2009 or future years and to bonds issued to refund prior-year Housing Bonds.

- Utilize the HFA delivery system to ensure that any forthcoming Treasury and Federal Reserve mortgage rate buy-down initiative reaches the lower-income families HFAs so successfully serve and to provide a further interest rate advantage to those families.
- Eliminate the so-called MRB Ten-Year Rule that requires payments on mortgages financed with Housing Bonds outstanding for more than ten years to be used to redeem bonds rather than to make new mortgages.
- Modify Community Reinvestment Act (CRA) rules to give banks CRA credit for HFA bond investments, liquidity facilities, and other activities that support HFAs.
- Expand bank interest in municipal bonds by increasing the bank qualified issuance limit.

Unlock the Housing Credit program:

- Allocate through Treasury at least \$5 billion in TARP or in newly appropriated economic recovery funds to state Housing Credit allocating agencies to make up equity shortfalls in 2008 and potentially 2009; subject these funds only to Housing Credit program rules, to expedite and facilitate their use.
- Change the Housing Credit law to increase the return on Credit investments, by allowing investors to use Credits against prior years' earnings and relaxing passive loss rules that limit some investors' Credit investment benefits.
- Fix the 4 percent Housing Credit at 4 percent to stimulate more bond-financed Credit production.
- Extend to Housing Bond-financed Credit developments the ability of states to use the higher of area median income or the national nonmetropolitan income to determine tenant eligibility and rents, to make otherwise infeasible developments viable.
- Modify CRA rules to provide CRA credit to national banks for Credit investments anywhere in the country.

Background

State HFAs are quasi-public agencies that operate in every state, the District of Columbia, Puerto Rico, and the U.S. Virgin Islands to provide affordable housing for lower-income working families and other underserved people. They are represented in Washington by the National Council of State Housing Agencies (NCSHA).

State HFAs issue Housing Bonds and allocate the Housing Credit in virtually every state to finance homeownership and rental housing. The Housing Bond and Credit programs are unprecedented public-private partnerships for affordable housing, with which HFAs and their partners have produced remarkable results.

With Housing Bonds and the Credit, HFAs have created some of the highest quality, most innovative affordable housing ever produced with federal assistance. All across the country, Housing Bonds and the Credit are turning around neighborhoods and transforming communities. They are bringing affordable housing to our inner cities and rural towns. They are building new housing and saving old. They are housing working families and the poor. They are providing housing hope to people with special needs, the elderly, and persons who are homeless.

In addition to Housing Bonds and the Credit, state HFAs administer the HOME Investment Partnerships (HOME) program in 40 states to provide both rental and homeownership assistance for low-income families. Often HFAs combine HOME funding with Housing Bonds and the Credit to reach people and places they could not assist with HOME funds alone. Many state HFAs administer other federal housing programs, including Section 8 and homeless assistance. They also administer state housing resources.

HFAs are uniquely able to judge and allocate federal housing assistance to the most pressing needs, wherever they exist in each state, in amounts sufficient to make a difference. HFAs are close to real, local issues and housing needs, but have the perspective to bring a state and regional focus to problems that cannot be solved within individual municipal boundaries. HFAs are in an unparalleled position to ensure that funding is applied where it is most needed and is integrated with other public investments in our physical, economic, and human infrastructure.