NCSHA
National Council *of*
State Housing Agencies

March 17, 2020

Mr. Joseph M. Gormley
Deputy Assistant Secretary for Single-Family Housing
U.S. Department of Housing and Urban Development
451 Seventh Street, SW
Washington, DC 20410

Dear Mr. Gormley,

On behalf of the nation's state Housing Finance Agencies (HFAs), the National Council of State Housing Agencies[1] (NCSHA) writes in response to HUD's February 14, 2020, Tribal Leader letter (Tribal Letter). NCSHA represents the state HFA in each state, as well as the HFAs of the District of Columbia, New York City, Puerto Rico, and the U.S. Virgin Islands.

While state HFAs are not among the entities covered by HUD's Government-to-Government Tribal Consultation policy, the Tribal Letter suggests HUD is considering steps in forthcoming rulemaking regarding Federal Housing Administration (FHA) policy on down payment assistance (DPA) provided by governmental entities in connection with FHA home mortgage insurance that demand our response.

State HFAs as a group are the leading provider of DPA for lower-income households in this country. We support FHA's interest in strengthening the performance of DPA-associated loans and ensuring all governmental DPA providers are acting in borrowers' interests.

Yet even though state HFAs and their DPA programs are not the sources of the problems FHA is trying to fix, the rulemaking approach FHA is considering could harm them considerably. The result could be less homeownership opportunity for lower-income households because of decreased DPA and affordable homeownership financing from the primary sources of it across the U.S.

Fortunately, FHA can take quick action to strengthen governmental DPA without reducing homeownership opportunity for lower-income households or hurting longtime proven partners of the department, as described below.

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[1] NCSHA is a nonprofit, nonpartisan organization. None of NCSHA's activities related to federal legislation or regulation are funded by organizations that are prohibited by law from engaging in lobbying or related activities.

The balance of this letter provides more information, in three sections:

- FHA's concerns about governmental DPA and some governmental DPA providers
- Drawbacks to FHA's approach and better alternatives
- The importance of state HFA homeownership programs

FHA's Concerns about Governmental DPA and Some DPA Providers

The Performance of Loans with Governmental DPA

FHA is concerned that the share of FHA-backed purchase mortgages with DPA increased to 40 percent as of last year, up from 30 percent in 2011. FHA reports that, since FY 2000, on average, mortgages with DPA have claimed at twice the level as mortgages without DPA and that loans with DPA from governmental entities perform slightly worse than those from relatives and others. [2]

Entities Providing DPA in Violation of Its Rules

FHA also has expressed concern about entities providing DPA in violation of its rules. In its 2018 Annual Report to Congress, FHA stated: "FHA is concerned that certain entities are now operating these DPA programs on a nationwide basis and in ways that generate benefits for the provider that do not appear to comport with the intent of the 'prohibited source' provision. These programs also appear to increase costs, but not benefits, to the borrower and put the MMIF at an unreasonable risk."[3]

State HFAs Are Not the Source of Either Problem FHA Is Trying to Fix

State HFA loans with DPA and FHA insurance perform better than all FHA loans with DPA from a government program (see p. 6). And state HFAs don't operate on a national basis — only in the single state where each is authorized under the law and required to meet state-approved requirements regarding transparency, public oversight, program activities, financial management, and employee compensation. Yet, the language of the Tribal Letter indicates the FHA will propose broad, sweeping policy that will significantly adversely impact state HFAs, too, when instead, it should consider a more targeted approach that will address the entities with which it has concerns.

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[2] U.S. Department of Housing and Urban Development, "Annual Report to Congress Regarding the Financial Status of the FHA Mutual Mortgage Insurance Fund," 2019.

[3] U.S. Department of Housing and Urban Development, "Annual Report to Congress Regarding the Financial Status of the FHA Mutual Mortgage Insurance Fund," 2018.

Drawbacks to FHA's Approach and Better Alternatives

<u>FHA's Approach Would Impose an Unnecessary Regulatory Burden on State HFAs</u>

FHA is concerned some governmental DPA providers may be violating the statutory and regulatory prohibitions against DPA providers deriving "financial benefits" from related mortgage transactions and therefore being "prohibited sources" of DPA.

The Tribal Letter suggests FHA intends to propose revising its regulations to define and limit "financial benefits" and allow only "de minimis administrative costs [also to be defined] … over the amount of assistance." The Tribal Letter suggests mortgage originators would be required to determine that DPA providers, such as state HFAs, comply with these requirements.

With respect to "financial benefits," state HFAs already operate under a bevy of state law, regulation, and public oversight that ensures all their activities are in the public interest. State HFAs' audited financial statements and other financial information are available to the public. State HFA staff compensation is subject to state law, regulation, and disclosure requirements. State HFA board directors, who by virtue of their positions have a fiduciary responsibility to ensure the efficient use of their agencies' funds for the public good, are named on agency websites and subject to ethics and conflict of interest requirements.

To the extent state HFAs generate income from their affordable homeownership programs — which enables them to operate without reliance on taxpayer funding or state appropriations — those monies are, by state law and regulation, invested in the agencies' affordable homeownership and rental housing activities.

We understand that not all governmental DPA providers operate under such stringent and transparent laws and regulations regarding their finances and uses of program income. We support FHA's interest in gathering such information from governmental entities whose homeownership and DPA programs operate without such safeguards and accountability, as we describe below.

But it is not necessary for HUD to impose such safeguards and requirements upon state HFAs. Doing so would only add unnecessary regulatory burdens on the states and their private-sector lender partners (as we describe below) — a move totally at odds with widely supported principles of federalism and the Trump Administration's admirable commitment to reducing regulatory barriers to affordable housing, led by Secretary Carson, which the state HFAs through NCSHA have actively supported.

<u>FHA's Approach Could Discourage More Lenders from Participating in FHA Programs</u>

While some state HFAs originate a small number of home mortgage loans, typically only to serve a special population or underserved market in their state, the vast majority of state HFA homeownership financing and DPA is provided in partnership with mortgage originators, such as community banks, credit unions, regional lenders, and others.

The Tribal Letter suggests FHA is considering requiring that lenders confirm that DPA is not from a prohibited source by reviewing the DPA provider's "funding plan." Such a requirement could add a substantial administrative burden on thousands of lenders nationwide, particularly those that operate regionally or nationally and would have to evaluate specific DPA programs for each state in which they partner with a state HFA. Many of them might pass on their increased costs to home buyers or withdraw from those state HFA programs.

The work required and liability assumed to evaluate DPA funding plans could disincentivize lenders from participating in state HFA programs. We expect the drop-off would be especially severe among smaller lenders and those serving rural and other underserved areas.

All this would significantly undermine the Trump Administration's efforts to bring more lenders back to FHA, an effort led by Deputy Secretary Montgomery.

Even larger lenders typically do not have the specialized expertise to analyze such funding plans, including determining whether they show what the Tribal Letter refers to as "an accounting of all associated costs." Either specialized training would be necessary for personnel tasked with conducting these additional HUD-required reviews, or new staff would need to be hired to fulfill this new regulatory mandate.

The Tribal Letter asks if HUD should require lenders to submit DPA provider agreements regarding use of the DPA to originate mortgages for FHA insurance. It appears HUD might require this paperwork on an individual loan basis. This seems excessively bureaucratic and contrary to efforts to reduce red tape.

Furthermore, the comfort FHA is looking for may not be in the agreements themselves. Many state HFAs have stand-alone lender manuals that articulate in detail program operational requirements and processes to be followed by their lender partners for all aspects of their programs, including for the provision of DPA. State HFA plans are likely to differ, making timely and accurate FHA Homeownership Center review a serious challenge and major burden.

NCSHA is also concerned about the Tribal Letter's question about whether DPA providers should provide lenders access to their DPA funding plans, "showing all sources of funds and an accounting of all associated costs." This raises serious questions we believe HUD should answer and explain before issuing a proposed rule. For example, what accounting rules would be required for these reports? What standards would HUD establish for how individuals involved in DPA programs track and allocate their time and associated proportional salary and benefit costs?

FHA Can Address Its Concerns Quickly with Better Alternatives

We support FHA's interest in strengthening DPA associated with FHA home mortgage loans. Rather than pursuing a complicated, costly approach that would undermine FHA's mission, we propose two alternative steps FHA could take quickly.

First, better track governmental entity providers. FHA says it lacks information on the performance of loans with DPA from individual governmental entities. A simple solution would be to require reporting of such entities' tax identification numbers. Nonprofit DPA providers already do so, and the Senate supports the same for governmental entities (see Senate report language accompanying FY 2020 HUD appropriation).

Second, rely on existing state laws and regulations to ensure a level playing field of public accountability. For governmental entities that already operate under legal and regulatory oversight regarding transparency, oversight, program activities, financial management, and employee compensation in the jurisdictions where they operate, such as state HFAs, FHA should not add unnecessary additional red tape — which would reduce access to homeownership for those who can least afford it. Instead, FHA should simply ensure all governmental entities meet the same standards of public accountability that apply in any governmental jurisdictions where they provide DPA in connection with FHA loans.

In addition, HUD should publish an advance notice of proposed rulemaking with more details about what HUD intends to propose before it publishes a proposed rule. Providing more information and a comment period before the proposed rule stage would help HUD avoid taking actions that may have unintended consequences that would impair important governmental DPA programs.

The Importance of State HFA Homeownership Programs

<u>State HFA Loans Fill Critical Gaps in the Housing Market</u>

As FHA knows from its decades-long partnership with state HFAs, state HFA loan programs, including those with DPA, fulfill a unique and important role in our country's housing finance system.

- *State HFAs serve low-income buyers*. In 2018, state HFAs provided more than $27 billion of financing to help more than 156,000 households buy homes. The median state HFA-assisted homeowner's income was $57,039, 10 percent below the national median and 46 percent less than the median income of all home buyers in 2018.

- *State HFAs serve borrowers of color*. In many areas state HFAs are the drivers of affordable homeownership opportunity for borrowers of color, as reflected in the minority borrowers' shares of HFA homeownership financing in these states:
    - Alabama – 35 percent
    - Arizona – 53 percent
    - California – 68 percent
    - Colorado – 44 percent
    - Georgia – 65 percent
    - Kentucky – 24 percent
    - Minnesota – 33 percent
    - New Jersey – 47 percent
    - North Carolina – 42 percent
    - Texas – 77 percent

State HFA Loans Differ from Other FHA Loans

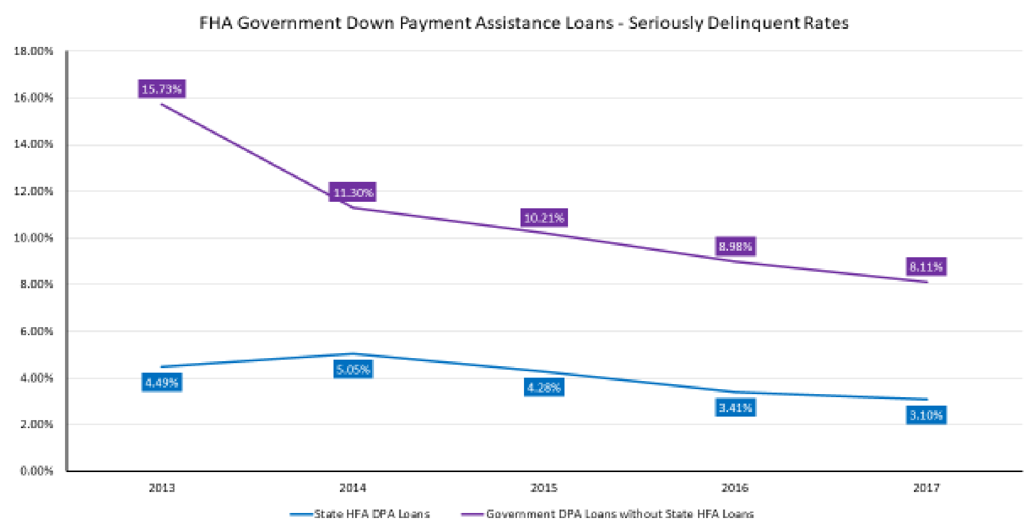
- *State HFA loans are more targeted to borrowers who need assistance*. In 2018, fully 73 percent of HFA loans served borrowers earning at or below area median income (AMI). By contrast, FHA estimates that 56 percent of all its program loans went to borrowers earning at or below 115 percent of AMI.

- *State HFA loans are smaller — and with smaller amounts of DPA*. The average loan size for HFA loans was 17 percent smaller than the average size of all FHA loans in 2018 ($171,084 compared to $206,041). The average amount of state HFA DPA in 2018 was 16 percent less than the average for all FHA loans in 2018 ($6,930 compared to $8,232).

State HFAs Differ from Other Governmental DPA Providers

- *State HFAs are authorized under state law to meet statewide homeownership needs*. Every state HFA operates under the laws and regulations of its state, and abides by state-approved requirements regarding transparency, public oversight, program activities, financial management, and employee compensation.

- *State HFAs deliver better loan performance*. An NCSHA analysis of 130,000 state HFA loans with DPA and FHA insurance, originated from 2013–2017, shows that HFA DPA loans had a serious delinquency rate significantly lower than the rate for all FHA loans that included DPA from a government program:



NCSHA, on behalf of its state HFA members, would welcome the opportunity to provide further insight into the concerns raised by the Tribal Letter and opportunities to strengthen the delivery of DPA to FHA-insured homebuyers.

Sincerely,

Garth B. Rieman
Director of Housing Advocacy and Strategic Initiatives
National Council of State Housing Agencies