2018 AHP Proposed Amendments:
Required Outcomes Framework

The Federal Housing Finance Agency ("FHFA") recently published proposed amendments to the Affordable Housing Program ("AHP") regulation which offer some benefits to AHP, but also pose a number of challenges. The primary challenge is the proposed new outcomes framework that requires awarded AHP dollars to meet FHFA-established priority categories (see details below).

What Would Change if the Proposed Amendments are Enacted

For the past 28 years, AHP has used a transparent scoring system for its competitive program. Project applications are scored and ranked in descending order. Awards are then given to the highest-scoring projects until the funds are exhausted. The proposed outcomes framework would require awarded AHP dollars to meet multiple outcomes. This would create a complex award structure, resulting in unintended consequences that reduce program flexibility, establish preferences for certain project types and lessen the transparency of AHP.

Awarding AHP

Current Scoring System:
straight-forward, transparent

7 FHFA categories
+ 2 FHLBank categories
= **100 points**

Proposed Outcomes Framework:
Less responsive to market-based housing needs

- 10% of funds used for home purchase
- At least 55% awarded to two statutory priorities
- At least 55% awarded to two of three regulatory priorities, with a 10% minimum in each of those two priorities
- At least 55% of rental units reserved for households earning 50% or less of area median income

How the Amendments Would Impact AHP

1. *Reduced Flexibility*

The priorities in the outcomes framework appear on the surface to offer flexibility, but the practical implications actually make the program *less flexible* to meet local needs.

> ***Example:*** *An FHLBank's AHP annual contribution is $30 million. The FHLBank chooses to allocate 30 percent ($9 million) to its home purchase set-aside program and $21 million to the general AHP competitive fund. In order to meet the regulatory priorities, 55 percent of the total funding, or $16.5 million ($30 million x 55 percent), must meet two of the three regulatory priorities. This means that in actuality, 79 percent of the general AHP fund ($16.5 million/$21 million) must meet these priorities.*

Because FHLBanks will want to avoid the consequences of not meeting required outcomes, the FHFA priorities will drive scoring and overshadow the local needs of each FHLBank district. One consequence of the outcomes framework is that it creates a national, prescriptive program that does not allow flexibility to respond to and leverage local opportunities.

2. Preferences for Certain Types of Projects

Since FHLBanks would be compelled under the outcomes framework to meet the regulatory priorities, certain projects that align with the priorities would benefit, but other types of projects that don't align well with regulatory priorities would be at a competitive disadvantage, including:

- Rental and homeowner projects in urban areas that are new construction or involve property reuse, such as repurposing vacant, blighted substandard property or non-housing properties (e.g., former schools, industrial or commercial property); and/or
- Urban and rural rental projects that target units for households with incomes greater than 50 percent of the area median income (mixed income).

This may discourage some sponsors/developers from applying for certain types of developments.

3. Less Program Transparency

The new outcomes framework may force FHLBanks to diverge from the long-standing process of selecting projects in descending application score order. The proposed amendments would permit FHLBanks to "re-rank" applications and select lower-scoring applications in order to achieve the outcome requirements. FHLBank New York would make every effort possible to adjust its program to avoid a possible re-ranking, but if it were to still occur, this would make the process for selecting awarded projects more complex and less transparent.

AHP's current transparent scoring system is developed through a model governance structure established by an elected Board of Directors, with expert advice from a 15-person Affordable Housing Advisory Council in each FHLBank district. The scoring criteria and framework are published annually in each FHLBank's AHP Implementation Plan, which is transparent and well-understood by members and sponsors/developers.

Proposed Solution

The current AHP application scoring structure has worked successfully for 28 years. The scoring-based system, under the current regulation, also allows FHFA to establish program priorities as required by the statute establishing AHP. The final regulation should eliminate the outcomes framework and retain a scoring structure that:

- Provides FHLBanks with scoring discretion beyond what is available in the current regulation, and
- Adds the ability to create targeted funds, as proposed in the amendments, under a scoring structure that allows FHLBank discretion.

A scoring-based system is strongly preferred over an outcomes-based framework and will allow FHLBanks to sufficiently respond to local needs, encourage all project types to apply and maintain program transparency.

2018 AHP Proposed Amendments:
Other Challenges for Sponsors, Developers and Members

Thresholds for Targeted Populations

The proposed amendments change the threshold amount needed for projects to qualify as serving targeted populations, such as the homeless, individuals with special needs or other targeted groups. The threshold would increase the portion of units reserved for targeted populations from 20 percent to 50 percent. This new threshold is not compatible with other funders and does not recognize the benefit of a mixed-occupancy development, which allows developers to cross-subsidize units in a project. Ultimately, since rental subsidies are difficult to secure, raising the minimum number of units required to serve targeted populations could have a negative effect on a project's feasibility and may discourage some sponsor/developers from applying for AHP.

Proposed solution: Retain the current 20-percent threshold amount.

Ability to Make Project Modifications

Under the proposed amendments, AHP project modifications may be delayed, and AHP sponsors unduly burdened, due to a new "cure-first" requirement. This change requires sponsors with awarded AHP projects that are not able to completely fulfill the commitments made in their AHP applications to attempt to cure the issue before requesting a modification to their project. Sometimes the cause is something beyond a sponsor's control, such as market conditions or changes in a third-party servicer provider. In these cases, having a cure-first requirement increases funding risk to the sponsor, may increase cost and may delay the disbursement of funds. Delays caused by this new requirement will impact members that have committed construction or permanent financing or are providing equity to the project.

Proposed solution: Retain the FHLBanks' current practice of verifying that any modified project would still have scored high enough in the funding round to receive the AHP award had the sponsor applied for AHP funding with the modifications in place.

Development Team Evaluation

The proposed amendments require FHLBanks to evaluate the ability of the sponsor and all members of the development team to perform the responsibilities committed to in the application. This will add documentation burden for sponsors. In addition, the entire development team may not be in place at the time of AHP application, making it impossible to assess total capacity.

Proposed solution: Retain the FHLBanks' current practice of reviewing the prior experience of the development team.

Homeownership Retention

Under the proposed regulation, the five-year retention agreement for homeownership is eliminated. This is a beneficial change for households that need a moderate amount of AHP to rehabilitate, construct or purchase a home. However, for projects requiring larger amounts of AHP per unit, it introduces a risk of misuse that FHLBanks need to have the flexibility to address. Specifically, elimination of the retention agreement may increase property "flipping" for AHP projects with a relatively high per-unit AHP subsidy, particularly in rapidly appreciating markets.

Proposed solution: Allow FHLBanks the discretion to use a retention instrument in certain situations.

Coordination with Other Funding Sources

The proposed amendments missed the opportunity to simplify AHP, optimize its impact and maximize the reliance on other funders, as outlined below:

- The "need for subsidy" and "project costs" sections of the proposed amendments do not specifically allow for the maximization of coordination with other funding sources. Requiring an FHLBank to independently underwrite a project's need for subsidy and viability is unnecessary and increases the burden on sponsors in cases where other funding sources have already underwritten the project. Many AHP projects use Low Income Housing Tax Credits (LIHTCs) as their equity source and housing finance agencies (HFAs) underwrite those projects to a more rigorous standard than AHP.

  Proposed solution: Allow FHLBanks to rely on the underwriting of HFAs and other funders with comparable standards in terms of cost reasonableness, viability of operations, development team capacity and need for subsidy.

- The proposed amendments require rental projects with supportive services to create two operating pro formas: one for housing operations and the other for supportive services. The requirement will cause projects to arbitrarily separate costs and funding streams. Because supportive services are integral to serving the residents living in the project's facilities and funding sources often cover both the housing and supportive services, this requirement will add unnecessary burden for sponsors/developers.

  Proposed solution: Allow projects to include supportive services in a project's operating pro forma.

Long-Term Monitoring of LIHTC Projects by Sponsors

The amendments add a new provision requiring members to amend current AHP agreements with LIHTC project sponsors, and include in future agreements, a provision that requires the sponsor to report to the FHLBank LIHTC projects that are noncompliant with income targeting or rent requirements during the 15-year retention period. The current AHP regulation does not require long-term monitoring of LIHTC projects. This adds a new requirement and burden on members to amend agreements and on sponsors to actively monitor LIHTC projects for 15 years.

Proposed solution: Eliminate this proposed new requirement.

Share your concerns with FHFA. The comment period for the proposed amendments closes on Tuesday, June 12, 2018. COMMENTS CAN BE SUBMITTED ONLINE AT FHFA.gov OR BY MAIL TO ALFRED M. POLLARD, GENERAL COUNSEL, ATTENTION: COMMENTS/RIN 2590-AA83, FEDERAL HOUSING FINANCE AGENCY, EIGHTH FLOOR, 400 SEVENTH STREET, SW, WASHINGTON, DC 20219.