Enterprise

January 3, 2014

To: Regulations Division, Office of General Counsel
Department of Housing and Urban Development
451 7th Street SW, Room 10276
Washington, DC 20410–0500

Re: Small Multifamily Building Risk Share Initiative Request for Comment [Docket No FR–5728–N–01]

To Whom It May Concern:

On behalf of Enterprise Community Partners, Inc., thank you for the opportunity to comment on the Federal Housing Administration's proposed Small Multifamily Building Risk Share Initiative.

Enterprise works with partners nationwide to build opportunity for low- and moderate-income families, starting with a safe and affordable place to call home. Over the past 31 years, we have helped build or preserve 300,000 affordable homes across all 50 states, invested $14 billion into communities and improved millions of lives.[1]

We are a family of companies comprised of Enterprise Community Partners (the parent nonprofit) and its related organizations: Enterprise Community Investment (a financial services company), Enterprise Community Asset Management (a residential asset management firm), Enterprise Community Loan Fund, Inc. (a certified Community Development Financial Institution), Enterprise Homes (a single- and multifamily housing developer) and Bellwether Enterprise Real Estate Capital, LLC (a multifamily and commercial mortgage originator). Bellwether Enterprise is a Special Fannie Mae Delegated Underwriting and Servicing Lender, a Freddie Mac Program Plus Seller-Servicer and Targeted Affordable Housing Lender, an FHA Multifamily Accelerated Processing Lender and a USDA 538 Rural Development Lender.

Small multifamily properties are a critical source of affordable housing for low- and moderate-income families. However, the relatively small mortgages on small multifamily properties—the category is usually defined as loans below $3 million—make it very difficult for lenders to originate profitably after accounting for personnel, legal and other transaction costs. Due to the slim margins, these loans tend to be originated by smaller local banks with limited access to the secondary market, meaning they typically have to hold the loans on their balance sheets. According to a recent survey from the Mortgage Bankers Association, roughly 2,500 lending institutions originated multifamily loans below $3 million in 2009, but the average institution made less than 10 loans that year.[2]

For these and other reasons, owners of small multifamily properties often have trouble accessing the capital they need to refinance, recapitalize or rehabilitate their buildings. The proposed Risk-Sharing Program has the potential to meaningfully expand access to long-term, fixed-rate mortgage credit to these properties.

As a community-based nonprofit, a certified CDFI and an FHA-approved multifamily lender, Enterprise is uniquely positioned to be a key partner in this effort. In addition, Enterprise Community Loan Fund, Inc., was recently approved to borrow $50 million in capital through the Treasury Department's CDFI Bond Guarantee Program, which could provide the patient, predictable and flexible capital necessary for these deals to work.[3]

That said, we have several concerns with the program's proposed structure, eligibility requirements, affordability requirements and other provisions. Below we will address each of these concerns in detail, with specific recommended changes and requests for clarification.

Proposed structure and risk-sharing agreement

Under the proposed rules, the FHA would enter into a 50-50 risk-share with Qualified Participating Entities, or QPEs. These QPEs are envisioned to be CDFIs or other eligible nonprofit institutions, in partnership with FHA-approved multifamily lenders.[4]

The notice provides few details on the fees associated with the Risk-Sharing Program, stating only that the mortgage insurance premium will be "different than HUD's other mortgage insurance programs." Without more information on the premium amount and restrictions on fees charged by the QPE, it is difficult to determine whether the 50-50 risk-sharing agreement is feasible.

That said, assuming that the mortgage insurance premium is consistent with the example in Section XII of the notice (i.e. roughly 45 basis points annually) and that other rules are generally consistent with the FHA Multifamily Accelerated Processing program (i.e. loan fees are capped at 3.5% or 5.5% with tax-exempt bond financing), we believe that a 50-50 risk-share may be too burdensome to the QPE, which could be a significant impediment to program take-up.

Bellwether Enterprise Real Estate Capital, LLC, our mortgage subsidiary, originated 45 loans with principal values of $3 million or less in 2013. We traditionally execute these loans through the Fannie Mae Delegated Underwriting and Servicing program, which requires its licensed lenders to cover the first 5% of losses plus a share of any further losses, with a cap at 20% of the original loan amount.[5] In exchange for retaining this risk, lenders are given significant flexibility over underwriting and pricing. For larger multifamily projects, we also have the option of executing eligible loans through the FHA Multifamily Accelerated Processing program, which does not require lenders to retain any of the risk.

Given the terms offered by Fannie Mae and other execution options, it is unclear what financial incentive the QPE would have to execute small multifamily loans through the proposed Risk-Sharing Program. Specifically, why would the QPE agree to retain 50% of the risk when it can retain significantly less through an alternate execution?

For this reason, assuming competitive fees, we recommend altering the risk-sharing agreement so that the QPE is responsible for the first 5% of losses plus a share of any further losses, with a cap at 10% of the original loan amount. This would put the lender's overall risk exposure on par with the Fannie Mae DUS program.

We also request additional clarity on how the QPE will be expected to split the retained portion of the risk among partners in the joint venture. Specifically, will it be up to the CDFI and the FHA-approved lender to divide that risk accordingly, or will the FHA require one of the entities to retain all of the risk? Can the QPE pass on all or a portion of that risk to other investors, or will it have to be retained in full? Whenever possible, we recommend providing the QPE with flexibility in implementing the risk-sharing agreement.

Proposed loan and project eligibility requirements

We recommend granting QPEs more flexibility on the type of loans they originate through the Risk-Sharing Program. Section IV.A.3 of the notice requires that eligible mortgages "must provide for complete amortization (i.e., regularly amortizing) over the term of the mortgage." However, many of the multifamily loans originated by Bellwether Enterprise to refinance and preserve workforce housing have a term of around 10 years with payments based on a 25-30-year amortization schedule. While we appreciate the FHA's goal of limiting risk exposure, QPEs need to be able to originate loans that are competitive with the current market.

We also recommend more flexibility on the loan size limit. The $3 million cap is reasonable in most housing markets, but it leaves out several smaller multifamily buildings in high-cost markets. For example, it is not uncommon for a 50-unit, Class B apartment building in Brooklyn or the Bronx to require a $4-5 million mortgage to be purchased or recapitalized. For this reason, Fannie Mae's Small Loan Lenders program extends its loan limit to $5 million in certain high-cost markets.[6] We recommend that the FHA enact a similar exception for its Risk-Sharing Program.

Finally, we request more clarity on whether "scattered site" multifamily properties will be eligible for financing through the Risk-Sharing Program. Section IV.D.2 of the notice states that eligible projects "must consist of 5–49 rental dwelling units (including cooperative dwelling units) on one site" with specific provisions for noncontiguous parcels of land within a single area. We recommend removing the "on one site" provision of the rule to allow QPEs to bundle several similar small properties into a single loan, thus controlling transaction costs and increasing efficiency.

Proposed lender eligibility requirements

Again, given our unique organizational structure and decades of experience financing affordable rental housing, Enterprise is well positioned to participate in the Risk-Sharing Program. But we have a few concerns about the program's proposed eligibility restrictions for QPEs.

First, Section IV.A.3 of the notice states that a QPE could be "a joint venture or similar formal arrangement between two or more for-profit private lenders" and a CDFI. We appreciate the FHA's broad goal of promoting competition among lenders, but it is unclear why a joint venture between one approved lender and one CDFI would be ineligible for the program—especially when those two entities are part of the same mission-driven organization. We recommend changing that requirement to "at least one private lender" and a CDFI.

Second, Section IV.B.1 states that the "officer who will be in charge of the FHA operation must have at least 3 years of experience in FHA mortgage operations." It is unclear whether the officer must be employed by the CDFI or, in the case of a joint venture, the position can reside within the FHA-approved lender. If the officer must be employed by the CDFI, we recommend changing the requirement to "at least 3 years of experience in multifamily mortgage operations," as many CDFIs do not work directly with the FHA today.

Third, Section IV.B.2 states that a QPE must "meet certain minimum financial capacity standards similar to those promulgated by the Federal Housing Finance Agency in 2010 as conditions for CDFIs to become members of the Federal Home Loan Banking System." We request additional clarity on whether the associated CDFI will have to be a member of the FHLB system, which could be a significant impediment to participation. If that is the intention behind this requirement, we recommend removing it.

Fourth, Section IV.B.3 requires that applicants demonstrate their financial capacity by submitting "a complete FHA lender Application" and additional certifications. If the QPE is a joint venture between a CDFI and an FHA-approved lender, would the CDFI still have to go through the FHA application process?

Finally, we would like to confirm that the QPE is not expected to pledge any collateral to the FHA or assign the underlying loans or cash flow in order to participate in the Risk-Sharing Program. The proposed rules do not explicitly address this issue.

Proposed affordability requirements

We applaud the FHA for including strict affordability requirements for participation in the Risk-Sharing Program. That said, we recommend allowing more flexibility on those provisions.

According to Section IV.C.1 of the notice, all projects financed through the program must abide by affordability restrictions that are generally consistent with the Section 42 Low Income Housing Tax Credit program. Specifically, 40% of the units must be affordable to families earning 60% of Area Median Income or below and 20% of the units must be affordable to families earning 50% of AMI or below.

Owners often require outside subsidy—namely Low Income Tax Credits or Section 8 vouchers—to reach that level of affordability. However, not all small multifamily properties financed by CDFIs will include such subsidies. For example, we estimate that roughly one in five multifamily properties financed by Enterprise Community Loan Fund receive neither LIHTC nor Section 8 subsidies..

By comparison, the CDFI Bond Guarantee program restricts financing to projects in "Underserved Rural Areas" or "Low-Income Areas," defined as neighborhoods where the median income does not exceed 80% of Area Median Income. Since the Risk-Sharing Program targets the same lending institutions, we recommend that the FHA use the same general affordability requirement for this program.

In addition, if a project does include LIHTC or project-based Section 8 vouchers—which both have stringent affordability restrictions—it should automatically be deemed to meet the affordability requirements for financing through the Risk-Sharing Program. Taken together, these requirements would help actively expand affordable housing without establishing an unnecessary barrier to program participation.

Importance of Ginnie Mae Securitization

We commend the FHA for requesting statutory changes that would authorize Ginnie Mae to securitize loans on small buildings made under the Risk-Sharing Program. We see this as an essential step to getting the program off the ground. Unless QPEs have access to the secondary market through Ginnie Mae, they will likely have difficulty accessing the capital they need to originate these loans.

Conclusion

We see the proposed Risk-Sharing Program as a promising way to expand capital to small multifamily properties, which are a critical source of affordable rental housing in the U.S. And this program is needed now more than ever.

Today more than one in four renters are paying more than half their monthly income on housing—an all-time high—often leaving them one paycheck away from losing their home. According to the Harvard Joint Center on Housing Studies, there are currently 11.8 million very low-income renters competing for just 6.9 million affordable rental homes, a gap that has grown precipitously in recent years.[7]

We look forward to working with the FHA to improve the Risk-Sharing Program and maximize its impact on this ongoing crisis. In summary, we recommend the following changes to the proposed rule:

- Provide more details on the expected mortgage insurance premium and restrictions on fees charged by the QPE.
- Alter the risk-sharing agreement so that the QPE is responsible for the first 5% of losses plus a share of any further losses, with a cap at 10% of the original loan amount.
- Allow the QPE to be a joint venture comprised of at least one CDFI and one FHA-approved lender.
- Extend the loan limit to $5 million for certain high-cost markets, similar to the Fannie Mae Small Loan Lenders program.
- Expand program eligibility to allow "scattered site" multifamily properties.

- Allow greater flexibility on loan terms.
- Align the affordability requirements with the CDFI Bond Guarantee program, with automatic exceptions for projects that include Low Income Housing Tax Credits or Section 8 subsidies.
- Provide additional clarity on how the QPE will be expected to split the retained portion of the risk among partners in the joint venture, where the "officer" position will reside within the QPE and whether eligible CDFIs will have to pledge collateral, apply for FHA-approved lender status or become members of the Federal Home Loan Bank system.
- Continue to pursue statutory changes that would authorize Ginnie Mae to securitize small multifamily loans originated under the Risk-Sharing Program

Again, thank you for the opportunity to comment. If you have any questions about the above recommendations, please contact Andrew Jakabovics, Enterprise's Senior Director for Policy Development & Research, at ajakabovics@enterprisecommunity.org, or John Griffith, a Senior Analyst at Enterprise, at jgriffith@enterprisecommunity.org.

Sincerely,

Enterprise Community Partners, Inc.
Enterprise Community Loan Fund, Inc.
Bellwether Enterprise Real Estate Capital, LLC

ENDNOTES

[1] For more on Enterprise Community Partners, see http://www.enterprisecommunity.com.
[2] Fannie Mae, "Fannie Mae's Role in the Small Multifamily Market," 2011. Available at https://www.fanniemae.com/content/fact_sheet/wpmfloanmkt.pdf.
[3] For more on Enterprise's borrowing under the CDFI Bond Guarantee Program, see http://www.enterprisecommunity.com/news-and-events/news-releases/cdfi-guarantee-bond-program
[4] Under the proposed rules, an individual CDFI that is also an FHA-approved lender can also serve as a QPE. However, the vast majority of QPEs are expected to be joint ventures, simply because very few CDFIs are FHA-approved lenders.
[5] The exact risk sharing agreement for the Fannie Mae DUS program depends on the lender and the individual deal. For more on the program, see https://www.fanniemae.com/content/fact_sheet/wprskret.pdf.
[6] For more on Fannie Mae's Small Loan Lenders program, see https://www.fanniemae.com/multifamily/small-loan-lenders.
[7] Harvard Joint Center on Housing Studies, "America's Rental Housing: Evolving Markets and Needs," December 2013, available at http://www.jchs.harvard.edu/americas-rental-housing.