NLHA

NATIONAL LEASED HOUSING ASSOCIATION

Testimony of the National Leased Housing Association

Presented by Laura E. Burns
Hearing on Affordable Housing Preservation - June 19, 2008
Committee on Financial Services

My name is Laura Burns. I am the President and CEO of the Eagle Point Companies and a board member of the National Leased Housing Association. My affordable housing experience began in 1985 while working in the public sector for the Boston Redevelopment Authority and later as a consultant and a developer. My company is dedicated to the preservation of the affordable housing stock and over the last six years we have acquired and/or rehabilitated 23 properties and 5,300apartments in six states and Washington, DC that will remain affordable for the next 30 years.

The National Leased Housing Association (NLHA) is pleased to submit our views relating to the preservation of the federally assisted housing stock. For the past thirty-five years, NLHA has represented the interests of developers, lenders, housing managers, housing agencies and others involved in providing federally assisted rental housing. Our members are primarily involved in the Section 8 housing programs – both project-based and tenant-based. NLHA's members provide or administer housing for over three million families.

Thank you for the opportunity to testify. NLHA has been working over the past year with the committee staff to craft workable legislation and our written testimony includes a number of recommendations to facilitate the preservation of the existing stock of affordable housing. Our specific comments on the draft bill are attached. We appreciate the interest of the Committee and its leadership in crafting a bill that will address many of our concerns.

Eagle Point Experience

I would like to spend my brief time today sharing several experiences that highlight particular barriers to my company's ability to complete preservation transactions.

Eagle Point has enjoyed some very successful and satisfying experiences in coordinating the complex world of state agency programs and the low income housing tax credit program with HUD programs. Eagle Point will only pursue preservation projects that have financial backing to achieve a full rehabilitation with an appropriate operating budget to ensure that we can maintain each property as quality affordable housing.

In 2004, my company acquired a property known as Delsea Village apartments in Millville New Jersey. This 100-unit family property - originally built in 1971 under the HUD Section 236 mortgage insurance program also has Section 8 project based assistance. the property had been well cared for by the prior

owner but for any property that is thirty plus years old, certain systems needed to be replaced and all of the apartments were dated and tired- a declining quality of life for the residents.
We gathered the financial commitments to acquire and renovate the property gained approvals for tax exempt bond financing, low income housing tax credits, a New Jersey low interest loan and other state agency assistance. We provided HUD with an independent study showing the expected market rents after our planned $20,000 per unit renovation. As a section 236 project, HUD guidance allows a budget-based rent increase up to the as-improved market rents upon completion of the rehab. Further, HUD allows the budget to include the new debt service and expected annual operating costs after the renovation. HUD approved the rent increase and use of the 236 interest reduction payment (IRP) subsidy. That project was successfully acquired and renovations began in April 2004.

In order to arrive at Delsea Village, our residents and visitors must drive straight through another HUD-assisted complex known as Delsea Gardens. Although the names and dates of construction are similar, the prior owners were different; Delsea Gardens was in much worse condition. Instead of mowing the grounds, the owner decided to simply pave the front yards. The exterior of the buildings, the play-areas and the manager's office all reflected minimal maintenance.

Delsea Gardens is 100 apartments with Section 8 project-based assistance and it seemed to us a natural and obvious decision to acquire and renovate Delsea Gardens. We negotiated a purchase and sale agreement and obtained the same financing benefits from the state of New Jersey. Our company looked forward to the day our residents at Delsea Village would drive through an improved neighboring property. We looked towards the day that both properties would have the same level of services and improvements so no child would wish he or she lived next door at the nicer property.

However, Delsea Gardens was constructed and financed under a different HUD program that inexplicably does not allow rents to be set at the "as improved market rent"—only based on the current inferior condition. Furthermore, HUD rules limit this project to a budget based review using old debt service and the old cost structure. This of course would not have resulted in adequate funds to operate the property. We made every effort to obtain an approval for a rent increase under HUD rules- in the end, we could not get the approvals or the rent levels we needed from HUD even though after completion of the renovations our rents would not have exceeded the comparable market rents for the area as provided under MAHRA.
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Therefore, the approved subsidy was returned to New Jersey, the seller terminated the purchase contract and shortly thereafter sold the property to an owner who continues to operate the property at a minimal level with no improvements. The pictures before you were taken last week, three years after their neighbors moved back into their renovated apartments next door.

HUD has established this policy which differentiates outcomes for different properties without the direction of Congress. The proposed draft legislation before you would correct this inconsistency and allow a property that is to undergo rehabilitation to request a rent increase based on a budget with increased debt service and other appropriate costs.

We have been involved in another acquisition effort for almost five years- we had our first meeting with HUD four years ago to discuss the need to renovate a 118 unit elderly project in Connecticut which is owned by a non profit. For these last four years we have awaited HUD policy direction relative to whether the seller may accept some of the sales proceeds. Five and a half years from now when the mortgage matures, the seller, a rotary business group, has a unilateral right to sell the property at market rates, terminate the Section 8 contract and accept all of the sales proceeds. This seller has been patient in working with us and has agreed to defer over $1.5 million in value in order to complete the preservation transaction. The residents have had no choice but to be patient as they enter their fourth summer without renovations and might expect continued plumbing problems, broken elevators and deteriorating windows. We think we are finally close to getting HUD's approval.

A different seller might have decided to walk away from preservation and instead, wait another five years and accept significant increased financial benefit that can be used to further the nonprofit's mission. Again, this unwritten policy to limit sales proceeds to non profits has been HUD's misinterpretation of current law that results in properties that would otherwise be renovated and preserved today, being put at risk of loss in the near future. This draft legislation would address the issue so more properties would be preserved and renovated when the need arises and a preservation buyer is willing and able to acquire the property.

HUD Policies

The problems Eagle Point Properties experienced when trying to preserve Delsea Gardens were the direct result of inconsistent HUD policy application. What HUD would permit in a 236 decoupling situation like Delsea Village was not permitted in an identical property albeit with a Section 221(d)(4) mortgage. There really was no statutory basis for HUD's unequal treatment and no real explanation for Delsea Gardens residents who did not benefit from the major property renovation that was undertaken next door at Delsea Village. It is the frustration with short-sighted HUD policy decisions, some written, some unwritten, and the inconsistent application of those policies along with the recent HAP payment debacles, etc that will eventually result in current owners leaving the programs and will stymie the efforts of preservation entities like Eagle Point to acquire and rehab properties for continued affordable use.

HUD's reduced staffing (mostly due to a retiring work force) has resulted in the continued application of regulations and guidance that have not been updated in decades and are hardly relevant to today's properties. Such antiquated guidance and cumbersome procedures continue to alienate the industry. HUD needs to reinvent itself by examining its mission, attract and train bright young staff and install leaders with knowledge and vision (and authority) to look beyond the myriad of rules to the desired outcome. The current owners, managers and future owners want a partner in preserving and expanding the supply of affordable housing – not simply a regulator.

Until that time, we have to rely on Congress to intervene to clarify HUD's policies where they are (without good reason) interfering with responsible preservation efforts. A number of the provisions in the draft preservation bill would confirm HUD's authority under current law to remove artificial barriers and are strongly supported by NLHA.

Preservation Vouchers

The draft preservation bill includes an important provision that will ensure that residents living in properties with expiring mortgages are not physically or economically displaced. In 1996, when Congress restored owners' rights to prepay Section 236 or Section 221(d)(3) mortgages, Congress amended the U.S. Housing Act of 1937 to provide tenant protection to families or elderly living in such properties. Eligible residents who were not receiving rental assistance at the time of the prepayment were now eligible to receive a voucher if/when the owner raised the rents on the units. In other words, the prepayment of the mortgage eliminated the use restrictions related to the previous receipt of a below market interest loan. Once the mortgage is paid off, the owner is free to raise the rents to the market rent resulting in tenants paying more. The receipt of vouchers by eligible residents, those with incomes generally at or below 80 percent of median or in tight rental markets 95 percent of median, enables the families to afford the rents and stay in their homes. The statute was amended again in the next few years to provide enhanced vouchers to families/elderly living in properties in which the owners opted out of their Section 8 contracts.

The current statute needs to be amended (as proposed in the draft bill) to address two situations that were not contemplated in 1996. Firstly, it was not necessary to address mortgage maturations in the context of enhanced vouchers as the Section 236 properties or Section 221(d)(3) BMIR properties were at least ten years from their mortgage maturation (original mortgage terms 40 years and owners in most cases had a right to prepay the mortgage after 20 years). When the mortgages mature, the accompanying affordability requirements expire (including ELIHPA projects). In January 2004, the GAO issued a study on such mortgage maturations and projects that 11,267 mortgages will mature through 2013. The first such maturations have already occurred, and will peak after 2007.

Secondly, the enhanced vouchers provisions did not address situations in which a nonprofit sponsor prepays such a mortgage (or the mortgage expires) because the original eligibility for enhanced vouchers was tied to the ability of owners to prepay their mortgages without HUD permission (nonprofits need HUD permission to prepay in most cases). However, in today's low interest environment, it is not unusual for a nonprofit to seek and receive permission to prepay their mortgages to allow a refinancing and recapitalization of properties that are on average 30 to 40 years old, this includes Section 202 loans that were made prior to 1975, which did not receive Section 8 assistance.

Important Principles of Preservation

Any legislation designed to preserve the assisted housing inventory must recognize the complexity of preservation transactions and present opportunities for both for profits and nonprofits. The current draft bill appears to favor nonprofits. NLHA represents both nonprofit and for profit developers and has always believed that the industry benefits from the participation of any entity that has the commitment and expertise to provide quality affordable housing.

Further, the imposition of use restrictions that are inconsistent with those required under programs like the Low Income Housing Tax Credit (LIHTC) (which is the main tool used to preserve assisted housing properties) will make it difficult to underwrite many transactions. Further, it may seem like sound housing policy to require longer and longer use restrictions, however, the reality is that a property can only remain viable for so long (generally 30-40 years) without a major infusion of capital. Such use restrictions beyond the remaining useful life of a property will keep the property low income, but may not be a desirable place to live. The fact is that the expiration of use restrictions is often the trigger to recapitalize and preserve the assisted housing stock.

We encourage the Committee to adopt a 30 year use restriction for new preservation transactions that would be facilitated by the proposed grant program in the draft bill.

Tax Law

While not in the jurisdiction of the Financial Services Committee, a major step forward in preserving the assisted housing stock could be achieved through a change in the Tax Code. Preservation entities like Eagle Point are not always able to acquire affordable properties because the value of the properties is not sufficient to pay the tax liabilities of the investors. Many investors refuse to sell, resulting in a lost opportunity for long term preservation and a scarce asset that will eventually deteriorate without recapitalization. The current tax code benefits investors who choose to hold onto their partnership until death (when the heirs receive a step up in basis). NLHA supports a change in the code that will accelerate the tax relief provided upon death to investors who agree to sell their properties to entities (both for profit and nonprofit) that will renovate the properties and retain their low income use for at least 30 years.

The enactment of such exit tax relief would provide an immediate stimulus to the economy. For more information and background, see the attached "A Proposal to Preserve Federally Assisted Affordable Multifamily Rental Housing."

Both the House and Senate have introduced bills (H.R. 1491 and S.1318) that would accomplish such preservation (see attached background on exit tax). We urge the Committee to encourage the Ways and Means Committee to take action on H.R. 1491.

Thank you for the opportunity to share our views. I am happy to answer any questions.

NATIONAL LEASED HOUSING ASSOCIATION

A Proposal to Preserve Federally Assisted Affordable Multifamily Rental Housing

From the mid-1960s to the mid-1980s, the federal government made an historic investment in affordable rental housing for millions of lower income American families. Through a number of programs, Congress created financial incentives for the private sector to develop multifamily housing properties throughout the United States to address widespread housing shortages and distressed conditions evident in aging apartment buildings.

Today, largely because of the structure of current tax rules, this valuable housing asset to the federal government is at risk of being lost, either to continued physical deterioration in the case of lower valued properties, or to market rate conversion in the case of higher valued properties. Congress should enact legislation to give owners of federally assisted housing relief from recapture taxes to encourage the transfer of these properties to new owners who will agree to maintain the property as affordable housing for 30 years.[1]

Background. Prior to the enactment of the Low-Income Housing Tax Credit in 1986, the Federal government encouraged capital to be raised from individuals for investment in federally assisted housing by providing more rapid depreciation deductions for their investments. Today those investors carry low or negative basis in their partnership interests that would trigger large depreciation recapture tax obligations if the property were transferred. As a result most investors choose to hold on to their investment until the property is passed to their heirs and the negative basis is eliminated by the stepped-up basis rule.

<u>Lower valued property</u>. Across the nation there are thousands of federally assisted housing properties owned in a limited partnership structure which are badly in need of capital improvements that are not being made because they are locked into their current ownership. Sales of such properties typically do not generate enough cash to cover the recapture tax liability of the limited partner investors. Therefore the properties continue to deteriorate each year, putting them and their tenants at risk. Rather than selling the properties at substantial tax cost, or investing new capital in the properties, existing owners, many now of advancing

[1] The following organizations participated in the development of this proposal: American Association of Homes and Services for the Aging, Council for Affordable and Rural Housing, The Enterprise Foundation, Fannie Mae, Housing Partnership Network, Institute for Responsible Housing Preservation, Local Initiatives Support Corporation, National Affordable Housing Management Association, National Association of Affordable Housing Lenders, National Association of Local Housing Finance Agencies, National Association of Realtors, National Council of State Housing Agencies, National Foundation for Affordable Housing Solutions, National Housing Conference, National Housing Trust, National Leased Housing Association, National Low Income Housing Coalition, National Multi Housing Council.

age, are incented by the tax rules to hold the property until their death so that their heirs receive stepped-up basis.

This has led to a situation where a valuable resource to the federal government – hundreds of thousands of affordable housing units rented to low-income families – is deteriorating without the investment of needed capital to preserve the property.

Higher valued property. A far smaller number of federally assisted housing properties are located in hot housing markets where the market rents have been rising and the affordable housing units can easily be converted to market rate units or redeveloped as condominiums. While the higher resale value makes it easier to sell such property to new owners who will preserve the affordability restrictions, because of the high recapture taxes that would be owed by the limited partner investors, the far stronger incentive will be to sell the property at the higher price that can be commanded by purchasers who will convert the property to market rate housing or to condominiums. If this continues to occur, tens of thousands of units of affordable housing that represent an investment of billions of federal dollars, will be converted to market rate housing, reducing the supply of affordable housing even as the housing affordability crisis worsens in this country.

Exit Tax as a Stimulus to the Economy

The enactment of an exit tax provision would also provide an immediate stimulus to the economy. First, the Federal government will collect tax dollars on the cash portion of any gain attributable to sale that will never materialize as investors are now holding these properties until their death when their estates will be relieved of any tax burden. Next, the renovation of these properties undertaken by new ownership will create new jobs and increase consumer spending as new kitchen appliances, major building systems, plumbing fixtures and equipment will be purchased and installed. These capital improvements are accomplished without any additional expense to the federal government. As part of the transfer of these properties, state and local governments will also benefit from increased revenues as various transfer taxes and fees, along with sales taxes, are collected as a part of each transaction.

In addition, the transfer of these properties to qualified entities maintaining them as affordable housing will create further economic opportunities through the utilization of new private sector financing initiatives.

Let's take the example of an actual 267 unit property recently transferred and renovated with private equity and bond financing provided by a state housing finance agency. This property is 27 years old, having been built in 1981. The property is comprised of 267 units; 247 one bedroom units and 20 two bedroom units.

The initial due diligence for the acquisition generated revenue in excess of $265,000 to the local firms and companies which provided the title work, survey update, appraisal, physical needs assessment, environmental, architectural and engineering reviews, and accounting and legal work. The local governmental entity received $191,000 in revenue through payment of the realty transfer fee.

The transfer of the property included a construction/renovation budget of $4,445,500. This work provided economic benefit to many segments of the economy including the manufacturers, and therefore their employees, of the appliances and new system components, the suppliers and installers of these same items, along with the general contractor who oversaw the entire renovation. The various work items in the project included the manufacture and installation of

- new solar roof-top panels
- new triple pane thermal windows
- new tile, carpeting and painting
- updated security system
- new heating and cooling equipment
- new elevators
- new plumbing
- updated electrical systems and energy efficient lighting
- renovated kitchens with new stoves, refrigerators, microwaves, cabinets, countertops, sinks and faucets
- updated bathroom with new sinks, faucets, vanities and toilets

Proposal. A modest change in the tax rules can be adopted to preserve the stock of federally assisted affordable housing at minimal revenue cost to the federal government. Further such action could serve as a stimulus to the sagging economy. This could be accomplished by waiving the depreciation recapture tax liability where investors sell their property to new owners who agree to invest new capital in the property and to preserve the property as affordable housing for another 30 years. Since very few investors subject themselves to recapture taxes today, opting instead to pass on the property to their heirs at a stepped-up basis, the cost of this proposal should be modest, while the benefit to the federal government of extending the affordability restrictions will be far reaching. This concept is embodied in H.R.1491 legislation introduced by Congressmen Davis and Ramstad and S. 1318 introduced by Senators Schumer and Smith.

Comments of the National Leased Housing Association (NLHA) and the Institute for Responsible Housing Preservation (IRHP) on the <u>March 14, 2008 Draft</u> of "Housing Preservation and Tenant Protection Act of 2008"

March 31, 2008

Page 8 Section 3: Definitions

<u>"Nonprofit Organization</u>" There seems to be a bias in parts of this bill against using the low-income housing tax credit and in favor of using appropriated funds for preservation **We recommend that the definition of "nonprofit" be similar to the definition in the 202/811 programs by including for profit limited partnerships or limited liability companies with a nonprofit as the sole general partner.** This broader definition will permit use of proceeds from the sale of tax credits for acquisition and rehabilitation of projects, thereby achieving preservation goals while minimizing the expenditure of HUD funds

<u>"Qualified Preservation Entity</u>" **–**under (4)(A) the 40 year term is not consistent with tax credits and M2M, etc. The entities will need to raise money, generally through the tax credit program, to accomplish the necessary recapitalization. Requiring a term that is longer than the standard affordability periods in other housing programs will make the transactions very difficult to accomplish. **Please amend the term to be consistent with current programs and practices.**

Further, we are not aware of state credit agencies that buy properties and are unclear as to why (B) is necessary. **We suggest that (B) on page 8 be removed.**

Page 9 Section 101: Rent Supp/RAP Conversions

This section provides an opportunity for properties with Rent Supplement or Rental Assistance Payments (RAP) to convert to Section 8 (at owner option). If an owner chooses to convert, it must agree to accept the Section 8 for five years beyond the original mortgage maturation date. If the owner converts and subsequently marks up to market (after the first year) under MAHRA, it must agree to 10 additional years of Section 8. The owner may request a 20 year HAP contract.

This provision appears to be an amalgam of various drafts and ideas. Several questions are raised:

(1) The draft does not create new authority for project-based assistance under section 8. **Therefore, what existing authority is being used and are the terms of that authority consistent with the draft provisions?**

(2) The draft provides for the possibility of an immediate mark up to market of rents upon conversion, pursuant to section 524 of MAHRA, but the draft does not make section 524 applicable to converted contracts until 12 months have elapsed after conversion. Also, there may be a conflict with other provisions that limit the first year subsidy to the maximum amount payable under the previous contracts.

(3) After one year, whether a converted contract has expired or not, the contract is required to be transferred to section 524. This transfer prior to contract expiration should be optional with the owner as the 524 terms and conditions for some contracts might not be as desirable, thus creating a disincentive for conversion. **We support the concept, but prefer that the language be revised to address the above concerns, please see Section 110 of proposed *"industry" bill of April 2007. *** *The "industry" bill was compiled by NLHA with assistance from the Institute of Responsible Housing Preservation (IRHP) and contributions from NAHMA, the American Assoc. of Homes and Services for the Aging (AASHA) and SAHF. The proposed April 2007 bill is supported by other organizations such as IREM, NAHB, and the National Housing Conference For a copy of the industry proposal, please contact Denise Muha at dmuha@hudnlha.com*

Page 12-28 Section 102 Displacement Prevention

This section appears to try to preserve at risk (maturing mortgages) Section 221 (d)(3) BMIRs and Section 236 projects by providing rehab "grants" to owners to preserve properties using funds from un-obligated state agency uninsured rent supplement monies. Owners receiving such grants agree to maintain affordability for at least 20 years beyond the mortgage maturation date. Grants would also be made available to NP purchasers for any direct costs (other than the purchase price) and NP owners (and subsequent owners) would be required to agree to maintain the property for the remaining useful life of the property.

Grants would also be provided to owners "to maintain affordability" but would NOT be provided to projects owned by nonprofits. Rents would be capped at the lesser of market rent or 150 percent or FMR. Such assistance will only be provided to projects that agree to use restrictions for remaining useful life of property (but not less than 10 years).

We recommend that any qualified preservation entity be eligible for assistance for profits and nonprofits) and request that loans be provided (on request) in lieu of grants.

Section 102(b)**.** *Enhanced Vouchers.*

This subsection authorizes enhanced vouchers to eligible tenants residing in section 236 and section 221(d)(3) BMIR projects whose mortgages mature and unit subsidies therefore terminate. The draft requires a notice to tenants 9 months prior to this termination. When these same mortgages are prepaid prior to maturity and tenants are eligible for enhanced vouchers existing law requires a notice period of 150 days. The 150-day period is more than ample for both prepayment and maturity events. (although is may be too long if a mortgage is close to maturation). Experience with the excessively long one-year notice period for section 8 contract expirations indicates that during such long notice periods some tenants will act against their best interest and leave the project before termination and thereby lose their eligibility for voucher protection. (The one-year notice period for section 8 expirations was enacted prior to the availability of enhanced vouchers and it made sense in that context, but it no longer does, nor does 9 months). **We recommend this provision be amended for consistency current law and practice.**

Also, we recommend that lines 8-10 on Page 24 be removed that allow HUD to come up with additional "requirements" – the provision is very specific about the content of the notice, additional requirements will only cause confusion. **The use of "termination" is also very confusing. Why not insert "eligibility event" as the draft includes a definition. We suggest the definition on line 14 be amended (page 22) by inserting after the comma "(A) the maturity of the mortgage or loan; (B) the termination of an assistance contract that cannot be renewed; (C) the prepayment of a mortgage or loan or termination of an insurance contract, that covers a multifamily housing project that is not eligible low income housing as such term is defined in section 229 of the Low-Income Housing Preservation and Resident Homeownership Act of 1990 (12 U.S.C. 4119); or (D) the expiration of use restrictions imposed pursuant to the Emergency Low Income Housing Preservation Act of 1987 (12 U.S.C> 1715*l* note).**

The definition of "assisted multifamily housing property" is not adequate. We recommend that paragraph (2) (line 21 page 25) be deleted and replaced with (2) ASSISTED MULTIFAMILY HOUSING PROJECT - the term "assisted multifamily housing project" means a multifamily housing project" receiving assistance or formerly receiving assistance under – (A) section 236 of the National Housing Act (12 U.S.C. 1715z01)); (B) section 101 of the Housing and Urban Development Act of 1965(12 U.S.C. 1701s)); (C) the proviso in section 221(d)(5) of the National Housing Act (12 U.S.C. 1715*l*); or section 202 of the Housing Act of 1959 (12 U.S.C. 1701q). You can then delete (A) and (B) line 6-12 on page 27.

Page 26, when defining "comparable properties" see (B) "are not receiving project-based rental assistance of any kind from any source" – this is confusing. **Clearly a project with rental subsidies is not "Comparable" to the market, but shouldn't this be clarified to include tax credit properties and properties with mortgage subsidies, as they are not market comparable either**.

Pages 28-35 Section 103 Federal Right of First Refusal

This provision is important and controversial, but the draft is riddled with bracketed questions from leg counsel. We strongly oppose any first right of purchase provision and recommend its deletion from the bill.

The provision appears to apply to prepayments of mortgages, maturity of mortgages and expiration of subsidy contracts. It seems to require the owner to sell the project upon the occurrence of one of the above events and sell only to certain purchasers. An owner apparently cannot keep the property for its own use.

Previous statutory restrictions on the contractual right to prepay have been found by the courts to be a breach of contract. While this provision is less direct, it still curtails contractual prepayment rights by taking property away from an owner if it expresses an intent to exercise its prepayment rights.

The better approach to preservation is to provide incentives and to remove disincentives, not coercion and appropriation of property.

Pages 35-39 Section 104 PBVouchers instead of Enhanced Vouchers

This provision would allow owners to request project based vouchers in lieu of enhanced vouchers (at PHA discretion). The PBVs would not count against the 20 percent cap. There is a similar provision in SEVRA. **We support this provision.**

Pages 39-41 Section 105 State AgencyContracts

This is a confusing section, beginning with the words in the section heading that the housing is not subsidized by the federal government, which is not true.

Subsection (a) attempts to modify the meaning of certain State agency section 8 contracts. It is not clear that this provision can override HUD's interpretation of its own contract form. **Further, if this provision results in a forced modification to the terms of the contract, to the disadvantage of the owner party to the contract, breach of contract litigation could ensue.**

Subsection (b) appears to be an attempt to alleviate some but not all of the harm done to owner parties to these contracts if subsection (a) is effective. Specifically, subsection (b) would permit a mark-up-to-market of rents during the last 5 years of the State agency contract if the owner commits to a 5-year extension contract at the end of the state agency contract term. However, the next provision provides that if State agency debt financing is still outstanding, to mark up to market (at any time apparently), the owner must commit to a 20-year contract and a 55-year affordability period.

Under the current contract, an owner with one of the affected contracts, can terminate at any time and renew under section 524 at comparable market rents with a 5-year contract commitment or it could opt-out of the program. **This section, therefore, abridges contractual rights of owners. <u>We oppose this provision.</u>**

Page 42 Section 106 Conversion of PB Certs to PB Vouchers

This provision attempts to clarify the conversion of Project-based certificate to Project-based vouchers. **Not sure it is necessary, HUD recently issued a notice on this (see PIH Notice 2008-14).**

Pages 43-44 Section 107 State/Local Preemption

This provision provides that if a property does not have a plan of action under LIHPRHA, the preemption provision in current law would not apply. **The Section 236 and Section 221(d)(3) programs are Federal programs regulated by the Federal government and therefore Federal law should preempt State law in this context. Furthermore, tenant protections are in place under current law that require at least a 150 day notice (but no more than 270 days) to tenants, HUD and local governments prior to prepayment, prevent owners from raising rents for 60 days and provide enhanced vouchers for residents (up to 80 and in some cases 95 percent of median income). With the protections in place, there is no need to amend the law. <u>We oppose this provision.</u>**

Page 44 Section 108 HUD Held/HUD Owned

The provision attempts to provide project-based assistance when HUD disposes of HUD-held or HUD-owned properties. The intent is to address inconsistencies with HUD implementation guidance. **No comment.**

Pages 45-46 Section 109 Assignment of Flex Sub Loans to "Qualified" Purchasers

Under the bill, a "qualified preservation owner" is defined as a for-profit or nonprofit organization that agrees to long-term use restrictions on property it purchases. This section authorizes HUD to forgive or assign any flexible subsidy loans it holds if a qualified preservation owner purchases a project subject to such a loan. However, this section is restricted to "nonprofit" organizations that are qualified preservation owners. It would facilitate the preservation of projects with flexible subsidy debt if all qualified preservation owners were accorded the benefits of this section. **We recommend deleting "non profit organization that is a" on page 45 and replace the words owner/purchaser with "qualified preservation entity."**

Page 46 Section 110 PBV rents in Tax credit projects

Formalizes HUD revised position to allow higher Sec 8 rents in tax credit properties w/project-based voucher units. Also establishes a rent floor. Similar provision included in the House passed SEVRA bill. **We support this provision.**

Page 47 Section 201 Replacement of State Agency Contracts

This provision presumably covers State agency section 8 projects not covered by section 105 of the bill, or perhaps it covers those as well with inconsistent terms. Essentially, it gives owners, locked into 30 to 40 year State agency contracts the opportunity, with a State agency's approval (not easy to get), to terminate the contract and renew under section 524, at more advantageous rents, if the owner executes a 20-year contract and commits to 40 years of affordability. **We have no objection to this provision.**

Page 48 Section 202 Transfer of HAPs

This section mirrors language in the current appropriations bill that provides for the transfer of Section 8 HAP contract (although the Section 8 statute also permits such transfers). The language could be improved by providing that use restrictions and interest reduction payments may be transferred also. Further, such transfers should be permitted to another project or <u>projects.</u> **We support this provision and encourage the language be revised as noted above. In addition, we suggest adding Section 303 of the Katrina bill (H.R.1227), which is more flexible in authorizing transfers of subsidy contracts in areas struck by hurricanes Katrina and Rita.**

Pages 54-55 Section 203 Transfer Information

Directs HUD to issue regs that make participation and certification procedures for sales and transfers of FHA or Section 8 properties the same as those for sales of HUD-owned projects, although it is not clear what the purpose is. Such properties and associated individuals are already required to be cleared under the 2530 process.

The provision also appears to say that HUD should provide a notice to the local government and residents when the owner applies to sell or transfer any FHA insured project or one with Section 8. HUD's current TPA process is very comprehensive and administratively burdensome. Additional rules are likely to cause unnecessary delays and increase the costs of transactions that generally bring new capital into the property. Such a requirement is not helpful or welcome.

Further, a "purchaser's record of noncompliance under housing, health and safety codes with respect to owner housing owned or managed by the purchaser regardless of location, shall be grounds for disapproval of the transfer." **This is much more complex that it appears and may result in good purchasers being denied an ability to preserve such properties. <u>We would recommend Section 203 be deleted.</u>**

Page 55 Section 204 Rehab grants using recaptured IRP

This section provides for recaptured Interest Reduction Payments (IRP) to be used to fund a grant/loan program to permit rehabilitation of properties. **No objection.**

*Page 56-57	Section 205 Budget-based rents*

This section would clarify current HUD policy on the approval of budget based rent adjustments to support the costs associated with the rehabilitation of a property that is being preserved as low income (a.k.a. post rehab rents). Rents would be established under MAHRA and would not exceed levels permitted under current law. There is no need to make this provision subject to appropriations. Changes in rent setting provisions do not require appropriation Act approval. Appropriations are provided for the overall cost of section 8 renewals, for example, but not for each modification in rent provisions. This draft bill has several provisions modifying rent setting provisions without requiring appropriations and should not do so for this provision.

Please remove (4) "be subject to the availability of sufficient amounts approved in appropriations Acts" Lines 19-22 on page 57 should remain to ensure that this provision is not interpreted to replace any other renewal provisions in current law. We support this provision.

*Page 58	Section 206 IRP Decouplings/Unit Conversions*

This provision clarifies that IRP payments should be made for the entire project when the number of units is reduced due to reconfiguration (in a 236 decoupling). **We support this provision.**

Pages 58-59 Section 301 No screening of tenants for enhanced vouchers

This section essentially provides that tenants eligible to reside in a property that is being converted (opt-out or prepay) will be eligible for the vouchers. Sometimes the PHA's screening criteria under the voucher program deem existing tenants ineligible. **We support this provision and agree with Legislative Counsel that the requirement does not need to be made part of the lease.** It would be inappropriate for the lease to address PHA selection standards.

*Pages 59-60	Section 302 One for one w/enhanced vouchers*

This provision would ensure that HUD provides vouchers for each unit in a conversion property regardless of whether the unit is occupied. The theory is that these vouchers while protecting current tenants are also replacing lost "units" in the community not protecting current tenants. **No objection.**

*Pages 60-62	Section 303 Ongoing Enforcement of HQS*

Provides that HUD "may" if a project has serious "violations" of HQS or "any other serious or repeated violations of other program requirements, including residents right to organize 1) abate all of part of HAP 2) withhold rent increases 3)use withheld payments to make repairs or 4) assume possession and management of the project.

HUD currently has the authority to address HQS and other violations so additional authority is not required. Further, using such sanctions for vague “other program requirements including tenants’ right to organize” is unacceptable.

The provision also would permit tenants to withhold their portion of the rent and if they do, HUD would withhold the HAP funds. **Withholding HAP money from the project only exacerbates repair issues to the tenants’ detriment. Tenants can currently voice their dissatisfaction with a property condition in a variety of ways – what is the intent here?**

In addition, the provision allows the tenants (at least 10 percent of them) or the local government to request that HUD conduct a mgmt review or a physical inspection. **Where is the funding coming from -HUD can’t get follow up REAC inspections that are necessary scheduled on a timely basis due to funding issues.** Management reviews are already conducted annually, a more frequent review is unlikely to yield different results and would increase the costs for project-based contractors – again this is a funding issue.

This whole section should be deleted or substantially revised to remove any references to management reviews (these are NOT physical inspections) and are conducted annually by HUD or the Contract Administrator. Further, this section should be subject to specific appropriations for this purpose and permit tenants to request a physical inspection only if the property has received a score of below 60 for the last two successive REAC physical inspections (and are not awaiting an appeal decision). HUD’s authority and the actions that HUD can take with regard to enforcing a HAP contract and/or regulatory agreement are formally established and do not need to be included in legislation.

Pages 62-63 Section 304 Third Party Beneficiaries

This provision provides for residents of housing projects and resident associations to be third party beneficiaries of various contracts between HUD and other parties, thus allowing them to litigate to enforce HUD requirements or to seek damages. The draft provision is incomplete and it is difficult to fully determine its intended scope.

We assume the requirement that HUD insert third party beneficiary clauses in various contracts is mandatory and not discretionary, and that it applies to new contracts executed after the effective date of the statute and not to existing contracts.

The provision would apply to a “contract for mortgage insurance” between HUD and an owner of a multifamily housing project. We assume the contract intended to be referred to is the Regulatory Agreement used in various forms in HUD’s multifamily mortgage insurance programs.

The provision also applies to an annual contributions contract between HUD and a public housing agency in connection with the section 8 housing voucher program. Finally, bracketed material in the draft indicates an intent to cover various agreements entered into under the Multifamily Assisted Housing Reform and Affordability Act of 1997, all of which involve section 8 project-based assistance**.**

We strongly oppose allowing residents or resident associations to enforce HUD requirements, and with their own varied interpretations of what statutory, regulatory and administrative provisions embodied in a contract mean. This additional enforcement potential could become burdensome, litigious and costly. It would be a disincentive for owners to participate or to continue their participation in HUD programs.

We recommend that this provision be stricken in its entirety.

Pages 63-64 Section 305 Resident Access to Building Information

This provision would require HUD to provide at the request of a tenant association rep, property owner information (including 2530s), financial information, subsidy contracts, correspondence, management reviews, mgmt contracts, etc. etc. **We believe this provision should not include sensitive information. In addition to concerns with privacy laws it would place individuals at risk of identity theft, etc. We would support this provision if it were amended to remove "shall" in line 17 and replace with "may" <u>and</u> if parts (1) (2) (3)(5) and (6) are removed and part (4) changed to part(1).**

Pages 64-66 Section 306 Transparency Regarding Building Information

Provision would require HUD to post information on its website like REAC inspections, LIHPRHA notices including plans of action, notice to terminate an insurance contract, requests to prepay, opt out notices, etc. **Again, we would have concerns about privacy and sensitive information. With regard to notices to opt out or prepay, the law currently requires such notices be provided to residents and others and should not need to be posted on HUD's already cluttered website.**

HUD currently posts REAC scores on the website and we do not oppose such posting. Further, we would also support the posting of management review ratings. We recommend removal (on page 65 and 66) parts (2)(3)(4) and (5) and add a new (2) "ratings from management and occupancy reviews for the property".

Page 66 Section 401 Maintaining Affordability Through Escrow of Rental Asst.

Prevents HUD from abating a Section 8 contract on a troubled Section 8 property when a transfer of the property is pending and permits HUD to escrow the HAP monies until the property is in compliance. **No comment.**

Page 67-72 Section 402 Multifamily Housing Foreclosure

The provision would amend the foreclosure laws to require, among other things, mortgages transferred by HUD to state/local governments to be foreclosed in the same manner as HUD held mortgages. This would grant HUD's non judicial foreclosure authority to units of local govt, who would then handle the disposition. **No comment.**

Pages 72-73 Section 403 Valuation of Property Dispo (Discount Sales)

This provision attempts to insert normal appraisal methodologies when valuations are done for property disposition deals. **No comment**

Pages 73-74 Section 404 UP Front Grants

The provision would restore upfront grant program that was eliminated a few years ago. **No comment.**

Pages 74-75 Section 405 Maintaining Project-Based Assistance for Property Dispos

Requires HUD to maintain Section 8 assistance when disposing of a HUD held property unless not feasible and then HUD can transfer the HAP. Rent adjustments after property disposition would fall under MAHRA. **No comment.**

Pages 75-77 Section 501 Affordability in LIHPRHA/ELIHPA Transactions

This provision provides flexibility in the renewal of Section 8 contracts in LIHPRHA/ELIHPA projects. Owners of ELIHPA/LIHPRHA projects could renew under any option (instead of just option 5) and the amendment also permits HUD to renew HAP contract terms for longer than the remaining term of the Plan of Action in ELIHPA projects. **We support this provision but suggest that in Section 501(a) the bracketed material should be included.**

Pages 77-80 Section 502 Mod Rehab Projects

This language is intended to level the playing field for mod rehab projects with regard to contract renewals. **We support this provision but would amend the title to read "Section 502. Encouraging Continued Participation in Assisted Housing Programs"**

Pages 80-83 Section 503Prepayment of FHA mortgages

This provision seems to add a paragraph that would not allow HUD to approve a prepayment/termination unless "such prepayment or termination involves (enactment/extension) of any low income affordability restrictions (as such term is defined in section 229 of the LIHPRHA Act of 1990 for the project for a period of not less than **___** " **The blank should be completed with "the remaining term of the original mortgage."**

Section 503(b) addresses HUD's practice of limiting the proceeds of nonprofits as a condition of prepayment approval despite the fact that the property will continue to be subject to use restrictions. **This provision achieves the same objectives as Section 401 of H.R.2930 that passed the House so may not be needed in this bill.**

Pages 83-84 Section 504 Treatment of Second Mortgages

This is the M2M provision that expands the 3 year window for NPs to receive assignment or forgiveness of M2M loan to 5 years. **We recommend changing the 5 years to 7 years to consider the timeframe for enactment of this language. Also, the heading is incorrect – the words "tenant organizations" should be removed and replaced with non-profit purchasers."**

Pages 84-85 Section 505 Rent Adjustments for Subsequent Renewals

Provision affirms that owners can renew under any option that they are eligible for; modifies HUD recent "interpretation" that "exception projects" must under go 'lesser of" test at each renewal instead of at initial renewal; and makes clear that projects that initially renewed under Section 524 and were not eligible for restructuring remain ineligible for mandatory restructuring. **We support the position but suggest including the bracketed language and delete the reference to (b)(3) since Section 502 of the draft repeals (b)(3).**

Pages 85-87 Section 506 Budget Based Rent Adjustments

This section provides that projects that have undergone M2M restructuring can request budget based rents instead of OCAF (HUD regs permit discretion but HUD has not permitted and only refers to OCAFs in HAP contract). The provision would also allow HUD to address rehab needs of early M2M projects that were underwritten too tightly through a 2nd (but simplified) restructuring or through rehab assistance under section 236(s) of NHA. **We support this provision but recommend the budget based language be amended to make it clear this provision applies not withstanding the rent adjustment language in the Section 8 HAP contract.**

Page 87 Section 507 Independent Appraisal for Divergent Rent Studies

The provision addresses HUD's sometime unfair resolution of divergent rent comp studies. If HUD and owner appraisals differ by 15 percent or more a third appraiser selected (and compensated) by HUD and owner jointly to do another study that will be binding on both parties. **We support but recommend that "Secretary's appraiser" (line 18) be deleted and replaced with "Secretary." HUD often deviates up or down, from its appraiser's determination. Also, on line 19 after "15 percent or more" please insert "of the Secretary's determination" and strike "differs" and insert "differ." Guidance needs to be provided as to the base to which the 15 percent is to be applied.**

Page 88 Section 508 Extension of HAP contract

Requires HUD when requested by an owner with an existing HAP to provide a 20 year term (or shorter as requested) in connection with a sale or refinancing. **We support this provision.**

Page 89-90 Section 509 Otherwise Eligible Projects

This provision would permit Section 8 projects with rents below market to apply for debt restructuring. It is limited in scope and requires owner to be fully on board. **We support this provision as drafted as it represents a compromise that we brokered with HUD.**

Page 90-91 Section 510 Period of Eligibility for Nonprofit Debt Relief

This is repetitive of Section 504 that addresses three to five year window for NPs to purchase projects that have been through restructuring, but 504 has an additional provision re: forgiveness of debt if tax credits or local funds are used. **One or the other section should be used.**

Pages 91-95 Section 601 Tenants Capacity to Organize

Permits technical assistance grants to tenant groups etc. **No comment**

Pages 95-104 Section 701 Preservation Database.

Requires HUD to create or amend its databases to include information about each assisted project and make info available to the public. HUD already has a Section 8 database on the web, but assume this would add information about other assisted properties. Asking that the REAC scores be posted is redundant (HUD already does that) – we would oppose Financial info being posted (plus owners do not even know the "financial score"). Requests that notices, plans of action etc be posted was already provided in Section 305 and Section 306 of this draft (we would oppose). The language further requires that HUD give grants if monies available to states/localities to use HUD's database and add info about state/local assistance. **We recommend that this provision be made optional on HUD's part and subject to specific appropriations for this purpose. HUD has existing data systems that are in dire need of upgrading including the Section 8 disbursement systems. We do not want HUD using scarce funds for a new database before it repairs its current systems.**

Items Not Addressed in the Draft

<u>Late Hap Payments:</u> The industry proposal includes a provision to require HUD to pay a late fee to owners when HAP payments are delayed; requires HUD to notify owners when payments will be late; and permits owners to tap reserves to make mortgage payments, etc without prior HUD permission. The legislative language is found in

Section 114 of our proposal. This provision was also included in the Mark to Market bill that was approved by the Financial Services Committee. **We request that this provision be added to the draft.**

Unexpected Cost Increases: Section 113 of the industry proposal attempts to address situations where the Operating Cost Adjustment Factor (OCAF) does not reflect actual cost increases (e.g. utilities, taxes, unreimbursed expenses from natural disasters, etc). We are disappointed that the provision was not included in the March 14 committee draft. We request your consideration that this provision be inserted in any future draft. Our colleagues at NAHMA are the originators of the specific provision and we anticipate they will comment extensively on the importance of this provision to preservation efforts.

Other Issues: A few preservation-related concerns came to mind while formulating our comments which may result in the submission of several technical amendments. We anticipate sending several additional comments/recommendations to the Committee staff over the next two weeks.

Questions concerning these comments should be directed to Denise B. Muha at NLHA 202/785-8888 or dmuha@hudnlha.com

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