Testimony of Rick Judson

On Behalf of the

National Association of Home Builders

Before the

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Committee on Banking, Housing and Urban Affairs

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"Housing Finance Reform: Essential Elements to Provide Affordable Options for Housing."

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Chairman Johnson, Ranking Member Crapo, and members of the Committee, I am pleased to appear before you today on behalf of the National Association of Home Builders (NAHB) to share our views on housing finance reform and the essential elements needed to provide affordable options for housing. My name is Rick Judson, and I am a builder/developer from Charlotte, North Carolina and NAHB's 2013 Chairman of the Board.

NAHB represents over 140,000 members who are involved in building single family and multifamily housing, remodeling, and other aspects of residential and light commercial construction. NAHB's members construct approximately 80 percent of all new housing in America each year, and many of our builders rely on the programs of the Department of Housing and Urban Development (HUD), (most involving the Federal Housing Administration, FHA) and the U.S. Department of Agriculture's Rural Housing Service (RHS) to help provide decent, safe, and affordable single family and multifamily housing to many of our fellow citizens.

We believe that an effective housing finance system must address liquidity as well as affordability and that those two elements are very closely related. Therefore, while it is important that the system provide housing credit at affordable terms as well as address specific housing needs, it is also essential that credit is consistently available on those terms regardless of domestic and international economic and financial conditions.

NAHB is a strong proponent of housing finance system reform and feels significant changes should occur in the conventional mortgage market, where Fannie Mae and Freddie Mac currently account for almost all activity. NAHB supports steps to increase the role of private capital but does not believe the market can rely exclusively on private sources. Recent experience demonstrates that private players are unwilling or unable to participate in periods of extreme economic and financial distress.

NAHB also believes that the future housing finance system must be viewed as more than the private conventional market. The array of federal government programs that have been developed over the years in response to identified needs are essential elements in ensuring that there are affordable options for providing housing. Thus, this testimony includes NAHB's position on how those programs contribute to the national housing finance system.

Demographic and Economic Overview

The underlying demographics of the U.S. forecast a continuing rise in demand for housing over the next two decades. A combination of record births and past immigration will produce over four million people moving into prime household formation ages every year for at least the next twenty years. These young people, primarily the children of the baby-boom generation, will form their own households as they age into the 25- to 34-year old cohort. These younger households were among the hardest hit by the economic recession, reducing household formation rates by more than most other age groups.

While older households have largely recovered from household arrangement setbacks, younger households are still struggling to return to pre-recession headship rates. And despite having lower headship rates than older segments of the population, these younger households are expected to add 2.4 million units to total housing demand over the next 10 years. Given their economic vulnerability, affordability will be key to recovery for these households.

Most newly formed households are just beginning their employment career and will not have large down payments or lofty credit scores. Current extra tight underwriting standards have made mortgage attainment even more difficult for younger families. Student debt responsibilities and lower starting salaries and wages compound the ability for younger individuals to transition to home ownership without access to affordable opportunities.

In addition to the oncoming demand, NAHB estimates that two million households did not form during the recession and represent an additional pent up demand that will come to the housing market as the economy improves and hiring returns to more normal levels. Many young and not so young individuals either did not launch into an independent household or returned to live with their parents, relatives or friends after losing their job or experiencing a significant reduction in income. NAHB expects these individuals to establish their own home and be in the market for an apartment or owned home as the economy expands.

Providing affordable homes will also present a challenge to home builders as the cost of ingredients rises. Builders are paying more for labor, land and building materials. As discussed later, builders continue to have difficulty accessing production credit from the traditional financial institution sources and have turned to non-traditional equity and debt sources that cost more.

Land development for homes ceased to take place during the Great Recession and building that capacity and process back up has taken time. In many revived and reviving markets, lots for single-family homes are very scarce, and prices have been bid up beyond what could be supported by current selling prices of completed homes. Construction workers found other sources of employment during the building collapse and can only be attracted back to home building with higher wages. Building material prices are back to or near the levels of 2005 when production was at two million homes. Production currently is less than one million, but while waiting for the material-producing industries to get back to capacity, prices have risen for the major building products like lumber, plywood and drywall.

<u>Current Restrictions and Gaps In the Market</u>

The ability of the home building industry to meet the demand for housing, including addressing affordable housing needs, and contribute significantly to the nation's economic growth is dependent on an efficiently operating housing finance system that provides adequate and reliable credit to home buyers and home builders at reasonable interest rates through all business conditions.

At present, home buyers and builders continue to confront challenging credit conditions weighed down by strict underwriting requirements and an uncertain future regulatory environment. For home buyers, while mortgage rates have fallen to record lows, access to mortgage credit is limited to those with pristine credit histories who can qualify for government-backed programs. Presently, FHA, VA, Fannie Mae and Freddie Mac (the Enterprises) account for more than 90 percent of mortgage originations.

<u>Credit Overlays</u>

Lender overlays in the mortgage credit process have been flagged as a major element in the greater difficulty potential home buyers are having in obtaining financing as lenders are imposing credit underwriting standards that are more restrictive than FHA, VA, Fannie Mae and Freddie Mac require. These credit overlays are employed due to heightened lender concerns over forced loan buy-backs on mortgages sold to Fannie Mae and Freddie Mac and/or greater required indemnifications on FHA-insured and VA-guaranteed loans.

While FHA and the Federal Housing Finance Agency (FHFA), which regulates Fannie Mae and Freddie Mac, have announced efforts to encourage lenders to refrain from excessive mortgage credit requirements, lender concerns about how federal agencies will implement repurchases and indemnifications continue to constrain credit availability. This is evidenced by the sharp increase in average credit scores for new Enterprise loans from about 720 in 2006 to 760 in 2012. For FHA loans, average credit scores have jumped from around 650 in the early 2000s to 756 in 2012. According to the 2013 State of the Nation's Housing Report, these trends largely reflect the evaporation of loans to borrowers with weaker credit histories. "In 2007, borrowers with credit scores below 620 accounted for 45 percent of FHA loans. By the end of 2012, that share was under five percent."[1] Similar trends are evidenced in the share of first-time home buyers which accounted for 28 percent of home sales in September 2013, well below the historical average of about 40 percent.

Regulatory Constraints

The regulatory environment for mortgage lending is undergoing significant changes as regulators implement new rules mandated by the Dodd-Frank Act. Uncertainty about the eventual regulatory landscape is another key factor that has tightened access to mortgage credit. Attempts by lawmakers and regulators to prevent a repeat of the housing boom/bust and the financial crisis by purging risk from mortgage lending has further tightened the credit box.

NAHB supports steps to ensure that mortgage lending occurs in a safe and sound manner, with appropriate underwriting, prudent risk management and sound consumer safeguards and disclosure. NAHB believes that loans should be carefully underwritten and adequately disclosed. NAHB also believes that it is critical that mortgage lending reforms are imposed in a manner that causes minimum disruptions to the mortgage markets, while ensuring consumer protections.

The release of the final Ability to Repay (ATR) standard by the Consumer Financial Protection Bureau (CFPB), which will take effect on January 10, 2014, has alleviated some of the regulatory uncertainty by defining new requirements and liabilities on lenders, but will undoubtedly create new hurdles for borrowers. The ATR rule establishes standards for complying with the ability-to-repay requirement by making a "qualified mortgage" (QM). The CFPB included a safe harbor in the definition of a QM that would provide some assurance to lenders that they will not be subject to increased litigation if they use sound underwriting criteria. The safe harbor would apply to lower-priced loans that are typically made to borrowers who pose fewer risks. However, the CFPB also included a "rebuttable presumption of compliance" for higher-priced loans typically for consumers with insufficient or weak credit history. Additionally, the QM includes a three percent cap on points and fees, which is a new calculation that has to be incorporated into the mortgage approval process.

The ATR provides a new framework for all mortgage lending. To the extent that lenders will remain cautious during the transition and beyond, creditworthy borrowers may not have access

[1] Joint Center for Housing Studies of Harvard University, *State of the Nation's Housing 2013*, page 19.

to affordable mortgage credit, or may be left out of the credit box all together. Reports also are surfacing about the challenges that lenders are experiencing in preparing their systems for operation under the ATR and QM regulations.

NAHB was pleased in August when the six federal agencies responsible for implementing the credit risk retention requirements mandated by the Dodd-Frank Act re-issued a proposed rule with a revised definition of a "qualified residential mortgage" (QRM) that would equate with the definition of the QM. Aligning the QRM with the QM has many benefits. Establishing one streamlined regulation, instead of having two separate sets of underwriting criteria, will alleviate confusion in the marketplace and will provide clarity and transparency for home buyers, lenders, investors and other housing market participants. Additionally, the underwriting criteria and product limitations contained in the QM will promote more prudent lending and will provide investors with an assurance that the loans are sustainable.

NAHB is supportive of ensuring safe, well documented, and soundly underwritten loans without limiting the availability, or increasing the costs of credit to borrowers. Aligning QRM with QM levels the playing field, promotes liquidity in the mortgage market and allows access to credit for a diverse range of home buyers, particularly first-time and low- to moderate-income home buyers. If the QRM is too restrictive, this important group of home buyers will have to rely on government programs or potentially risky mortgage products for low downpayment options. Encouraging private capital to provide mortgages with reasonable terms to a broad range of home buyers is imperative to support a sustained housing market recovery.

Commercial Real Estate

The proposed credit risk retention rule also sets forth the underwriting standards for a "qualified commercial real estate loan" (QCRE), which is presumed to be a low-risk loan. In the revised proposed rule, the agencies made modifications to their originally proposed criteria.

NAHB appreciates and supports the agencies proposed modifications. However, NAHB remains concerned that the regulators did not make distinctions among the different asset types included in CRE loans (hotel, retail, multifamily, office, etc.) in setting underwriting standards, except for the debt service coverage and amortization period of the loan. NAHB believes that it is not appropriate to apply the same standards to different classes because there are significant differences in property features, lease structures, tenant characteristics, etc., that affect how a CRE property is underwritten.

NAHB believes the QCRE is an important component of the credit risk retention requirements and setting an appropriate QCRE standard will be key to minimizing the impact on borrower financing costs for multifamily borrowers. To the extent that risk retention requirements raise multifamily financing costs, there will be an impact on rents. Higher rents have an immediate impact on renter households' budgets. For aspiring homeowners, higher rents also mean that it will take longer to save for a downpayment on a home. In addition, for other types of commercial properties, higher rents affect companies' ability to grow, and thus negatively impact job creation.

NAHB is concerned that, if not properly implemented, the credit risk retention regulations will further restrain credit to the multifamily housing sector. In addition to the adverse impact on families seeking affordable rental homes, such disruptions in the market have the potential to slow down the job creation and monetary contributions to the economy that are currently fueled by multifamily construction.

Importance of Federal Government Backstop

As stated earlier, NAHB's priority in housing finance system reform is ensuring liquidity for the housing sector in all markets throughout the economic cycle. This is only possible if market participants know there is a federal government backstop that will maintain stability in catastrophic circumstances. While NAHB agrees that the current degree of government intervention is unsustainable, an ongoing, though more limited, government role must be maintained to avoid future interruptions in the flow of credit to mortgage borrowers.

NAHB recommends establishing a new securitization model for single family and multifamily mortgages where Fannie Mae and Freddie Mac would be transitioned to private housing finance entities that would aggregate mortgages into securities for sale to investors worldwide.[2] Private capital from mortgage originators and securities issuers would be in the first loss position but the principal and interest for investors in the mortgage-backed securities would be guaranteed through a privately capitalized, federally backed insurance fund. Only mortgages with reasonable and well understood risk characteristics would be eligible to serve as collateral for government-backed mortgage securities, and the system would be overseen by a strong and independent regulator.

The new housing finance system envisioned by NAHB is similar to that proposed in the *Housing Finance Reform and Taxpayer Protection Act of 2013* (S.1217, Corker-Warner bill) which NAHB largely supports. In contrast, NAHB opposes the House Financial Services Committee-passed bill, H.R. 2767, the *Protecting American Taxpayers and Homeowners Act of 2013* (PATH Act), which removes government support to the conventional mortgage market. While NAHB agrees that private capital must be the dominant source of mortgage credit, the future of the housing finance system cannot be left entirely to the private sector. The historical track record clearly shows that the private sector is not capable of providing a consistent and adequate supply of housing credit without a federal backstop.

NAHB believes federal support is particularly important in continuing the availability of the affordable 30-year fixed-rate mortgage (FRM), which has been a staple of the U.S. housing finance system since the 1930s. These loans are geared toward affordability; 30-year terms lock in low monthly payments, allowing households with average incomes to comfortably budget for their home loan. Knowing their monthly housing costs will remain the same year in and year out regardless of whether interest rates rise provides households with a sense of financial security and also acts as a hedge against inflation. Many young buyers know that as their incomes rise, their housing costs will stay constant and become less of a burden, enabling them to prepare for other long-term obligations, such as college tuitions and retirement savings. In most instances, all of the interest and property taxes borrowers pay in a given year can be fully deducted from their gross income to reduce taxable income. These deductions can result in

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[2] The full details of NAHB's housing finance system recommendations are contained in "A Comprehensive Framework for Housing Finance System Reform," published by NAHB on February 9, 2012.

thousands of dollars of tax savings, especially in the early years of a 30-year mortgage when interest makes up most of the payment.

The key to the sustainability of the 30-year FRM is a securitization outlet because originators (banks and thrifts) do not have the capacity to hold such long-term assets which are funded with short-term deposits. Currently, Fannie Mae and Freddie Mac provide the securities vehicle along with a government guarantee for investors. There are serious doubts on whether a private housing finance system would be capable of supporting this type of product without some government backing. At a minimum, the cost and terms of 30-year FRMs would be significantly less favorable under a totally private system.

A government role is also essential for multifamily mortgage programs which also play a critical role in the overall health of the U.S. housing finance system. More than one-third of Americans live in rental housing and demand for rental housing in the future is expected to increase. As discussed further below, the multifamily sector performed much better than the single family housing market during the recent downturn. Multifamily loans held or guaranteed by Fannie Mae and Freddie Mac have very low default rates and the multifamily segments of both Enterprises are profitable. FHA also provides support to the multifamily market through the FHA multifamily mortgage insurance programs. Private market financing is not readily available for all segments of the multifamily market. Thus, there is a need to maintain a viable, liquid and efficient secondary market for multifamily rental financing where the federal government continues to play a role.

Future Cost of Housing Credit

In a future housing finance system, where several layers of private capital stand in front of a government backstop for catastrophic circumstances, the relative cost of housing credit would increase from current levels as home buyers ultimately bear the charges needed to attract the private capital and cover the cost of the government guarantee. However, NAHB believes that such a system would entail lower housing credit costs than one that relied exclusively on private players. Also, as mentioned previously, a completely private system likely would be subject to inconsistent credit availability.

With the prospect of higher mortgage borrowing costs, NAHB believes it is extremely important to make every effort to ensure that mortgage interest rates and fees do not increase more than is absolutely necessary to safely sustain the new system. The requirement in S.1217 (Corker-Warner bill) that first-loss capital providers hold capital of 10 percent of their risk exposure is excessive and would unnecessarily increase mortgage borrowing costs. A capital cushion of four to five percent would have been sufficient for Fannie Mae and Freddie Mac to sustain all of their losses during the recent decline in home prices and their current, more restrictive, book of business would require only a two to three percent capital under such a drop in collateral values.[3]

Guarantee fees or insurance premiums for the catastrophic government backstop could be subject to similar inflation. It is important to base federal guarantee/insurance charges on the

[3] Laurie S. Goodman and Jun Zhu, “The GSE Reform Debate: How Much Capital is Enough?” Urban Institute Housing Policy Center Paper, October 23, 2013.

universe of mortgage products and underwriting requirements that will be in place in the future rather than on products and protocols that are no longer in existence. Careful study should be undertaken to determine the level of private capital and federal guarantee/insurance charges that are needed for a safe, sound and sustainable future housing finance system.

A Multifaceted Housing Finance System is Needed

NAHB believes that the U.S. housing finance system should be multifaceted with both competing and complimentary components, including private, federal and state sources of capital liquidity. To ensure all markets are served, broad market participation should be encouraged. Barriers to entry to the secondary market should be a low as possible while balancing safety to the system. Compliance with regulatory requirements should not be more burdensome for smaller lenders – recognizing the unique role many small lenders have carved out for their communities.

To-Be-Announced (TBA) market

The to-be-announced (TBA) market plays a critical role in maintaining a liquid secondary market for mortgage-backed securities (MBS). Fannie Mae, Freddie Mac and Ginnie Mae securities make up the TBA market, and liquidity in these agency mortgage-backed securities is key to an efficient marketplace and affordable interest rates. Agency MBS are comprised of relatively homogenous mortgage loans with known underwriting criteria and standard documentation.

This well-defined marketplace supports the necessary fungibility to allow investors to buy and sell without the due diligence applied to non-TBA market securities and leads to the liquidity that is vital. TBA securities allow mortgage originators to lock-in interest rates to consumers by using the TBA securities to hedge their exposure to an increase or a decrease in interest rates before the mortgage loans close.

Reforms to the secondary market system should take into account the potential impact on the securitization of mortgage loans and the issuance and trading of MBS to insure the liquidity of the TBA market is not negatively affected.

Federal Home Loan Bank System

The Federal Home Loan Bank System (FHLBank System) is composed of 12 member-owned regional cooperatives chartered by Congress to provide reliable funding for housing and economic development to their members. Membership in the FHLBank System includes community banks, thrifts, credit unions, insurance companies and Community Development Financial Institutions (CDFIs). Each day the Federal Home Loan Banks (FHLBs) lend billions of dollars to member institutions through secured loans called "advances" to support the credit and financial needs of their members. Combined, the FHLBank System has 7,600 member institutions.

NAHB believes the Federal Home Loan Banks should continue to exist and provide their member institutions access to housing credit and liquidity. The FHLBs offered the housing market significant stability during the mortgage credit crisis when many banks were unwilling or unable to provide mortgage credit. NAHB has advocated for the FHLBs to capitalize on their acknowledged solid performance and risk management strength and seek to expand their role in housing finance as housing finance reform is considered.

Currently, the FHLBs can purchase mortgage loans from their member institutions but have only limited leeway to manage the resulting portfolios. NAHB believes the FHLBs would benefit from being allowed to aggregate loans from their members for sale to investors. A statutory change to allow the FHLBs to issue conventional mortgage-backed securities would significantly increase their value to members seeking enhanced access to the secondary market. In particular, small lenders would benefit from increased options for selling their loans to FHLBs rather than selling to large aggregators that may be less responsive and more expensive.

In fact, NAHB was very pleased to see the recent announcement by the Federal Home Loan Bank of Chicago that it will begin issuing Ginnie Mae securities backed by mortgages originated by its member institutions. This is extremely innovative and will provide the access to the secondary market that many of its member institutions currently lack.

Reform to the housing finance system must carve out a role for the FHLBs. NAHB would support an expanded role as long as any new lines of business, new mortgage programs or statutory changes to the FHLB charters are considered carefully in order to avoid unintended consequences that might conflict with the FHLBs' existing authorities and primary activity of providing advances to members.

As we think about ensuring affordability in a reformed housing finance market, the Federal Home Loan Banks should continue to support affordable housing through their Affordable Housing Program (AHP). Since 1990, each FHLBank has been required by statute to put aside 10 percent of its net income each year toward grants for affordable housing. The AHP is designed to be local in nature. It is administered regionally by each FHLBank through its financial institution members and each member's community-based partners to insure the programs are designed to meet the specific needs of local neighborhoods.

<u>Access by Community Banks</u>

While not having the dominant share of mortgage originations, community financial institutions originate a significant volume of mortgage loans. During the first quarter of 2013, $435 billion of mortgages were originated nationwide. Community banks and thrifts with less than $10 billion in total assets originated $55 billion of residential mortgage loans during the first quarter of 2013[4].

As the name implies, community banks offer financial services designed to meet the specific needs of their unique local markets. They are known particularly for serving rural areas and traditionally underserved markets. In the current environment of increased regulatory compliance requirements, tighter underwriting standards, and overall less availability of mortgage credit, it is important to be vigilant about the impact of housing finance reform on community banks and the mortgage borrowers they serve. Meeting the needs of their communities can mean these institutions are not originating standard products that can be sold in the secondary markets. This inability or difficulty to sell their loans to the secondary market can restrict their primary market activity.

[4] ABA Federal Home Loan Bank Member Insights, October 10, 2013, Vol.4, No. 1

Over the years, community banks have sold their loans to large aggregators, including Fannie Mae and Freddie Mac, and have paid higher fees based on smaller volumes. In a new housing finance system, access and pricing should not be based on the volume of business or size or geographic location of the selling institution.

Recently, community banks have been increasing their secondary market activity. Loans delivered to Fannie Mae and Freddie Mac by community banks have increased significantly from 2007 to 2012. For example, in 2007, only 3.6 percent of loans delivered to Freddie Mac came from outside the top 100 lenders. In 2012, this increased to 15.1 percent of all loans at Freddie Mac[5]. Access for community banks should be a priority when considering housing finance system reform.

The Corker-Warner bill acknowledges the importance of providing access to the secondary mortgage market to community banks. As proposed, Corker-Warner would create the Federal Mortgage Insurance Corporation (FMIC) which would be required to ensure that credit unions and community and mid-sized banks have equal access to the common securitization platform. The FMIC is authorized to create the Mutual Securitization Company to purchase, pool and securitize loans from insured depositories having less than $15 billion in assets or a non-depository mortgage originator having a minimum net worth of $2.5 million. NAHB supports Corker-Warner's provision to create a Mutual Securitization Company, which would be an approved issuer. However, as an issuer purchasing from small entities, its ability to compete with larger issuers should be carefully monitored to ensure a level playing field.

Housing Finance Agencies

NAHB believes state and local housing finance agencies should play an expanded role in providing housing funds. These agencies have proved critical in helping communities meet the needs of consumers who have faced hardships in the face of tight credit conditions.

State and local housing finance agencies utilize tax-exempt and taxable bonds as well as state and federal resources to offer a range of single family and multifamily housing programs. These agencies are uniquely positioned to assess community housing needs and should play an even more prominent housing finance role through the development of new programs for new, for-sale housing and multifamily rental homes. This should include partnering with federal and private providers of housing capital.

Single Family Housing

Retain Capacity of FHA to Meet Its Vital Housing Mission

The FHA single-family mortgage programs are a unique and vital component of the housing finance system, providing access to homeownership for underserved communities, primarily first-time homebuyers, minorities and those with limited downpayment capabilities. During the recent mortgage crisis, FHA demonstrated how invaluable its counter-cyclical role was in

[5] Statement of Sandra Thompson, Deputy Director for the Division of Housing Mission and Goals, Federal Housing Finance Agency; Subcommittee on Securities, Insurance, and Investment, U.S. Senate Committee on Banking, Housing, and Urban Affairs, July 23, 2013, pp. 4-5.

providing mortgage market liquidity as FHA's share of the market jumped from three percent during the housing boom to a high of almost 30 percent early in the crisis. Nearly 80 percent of FHA's purchase loans have been to first-time home buyers. This dramatic shift is evidence that FHA is performing its mission of providing the federal backstop to ensure that every American has access to a stable mortgage product. In times of crisis, private sources of mortgage credit have demonstrated they are unable or unwilling to meet housing capital needs.

NAHB supports efforts to reform FHA and understands that this is not a simple undertaking. However, reform must be approached with caution. Since 2010, FHA has implemented a series of policy changes, including higher mortgage insurance premiums, tighter underwriting requirements, stricter mortgage lender enforcement, and improved risk assessment, all intended to strengthen the performance of the Mutual Mortgage Insurance Fund (MMIF) and rebuild the capital reserve ratio. These changes are the most sweeping combination of reforms to credit policy, risk management and lender enforcement in FHA history. Further changes to FHA's programs cannot be separated from the larger discussion of reforming the complex housing finance system to ensure homebuyers have affordable financing solutions.

NAHB urges Congress to proceed carefully and not significantly alter FHA's role of providing affordable single family financing. We are concerned that several of the provisions in H.R. 2767 (PATH Act) would greatly reduce the scope and reach of FHA's programs. In particular, NAHB opposes provisions in the PATH Act that would limit FHA's single family programs to first time or low- and moderate-income home buyers, increase downpayments, and reduce the minimum FHA mortgage limit or floor. These proposals would have a detrimental impact on FHA's ability to serve its mission and facilitate the flow of mortgage credit to its targeted borrowers.

<u>Provide a Reasonable Menu of Conventional Mortgage Products</u>

America's future housing finance system must be designed to ensure that creditworthy borrowers have access to a reasonable menu of conventional mortgage products that are prudently developed and appropriately underwritten. While standardized product features and underwriting requirements are necessary to ensure liquidity, these mortgage products must also have practical flexibilities to meet the diverse financial needs of first-time homebuyers, minorities, buyers with limited downpayment capabilities and move-up buyers.

Research suggests that the greatest obstacle faced by potential first-time homebuyers, especially low-income, minority individuals and families, is not the ability to make monthly mortgage payments, but rather the ability to assemble enough funds to pay the downpayment and closing costs. Because of the financial downturn, many more potential homebuyers will have the ability-to-repay but will need affordable downpayment conventional mortgage products.

<u>Maintain Role of Mortgage Insurance Industry</u>

Private mortgage Insurance (MI) companies provide a vital component of our country's residential mortgage finance system by protecting mortgage investors from credit losses. Mortgage insurance also benefits home buyers by helping them achieve homeownership earlier with low downpayment loans.

Mortgage investors require healthy counterparty risk mortgage insurance partners, and both will need to continue to form strong partnerships to serve borrowers with well underwritten, competitively priced and flexible MI programs to ensure the availability of 95 percent loan-to-value (LTV) mortgage products.

Another benefit to this type of counterparty risk arrangement is that the loan is underwritten by both the mortgage investor and the MI company. This due diligence helps to ensure the consumer's ability-to-repay. MI companies are also providers of homeowner assistance programs that go well beyond the initial purchase of their home

Preserve Rural Housing Service and Veteran's Administration (VA) Loan Programs

The federal government historically has played an important role in providing mortgage credit to rural areas. The National Housing Act of 1949 authorized the Farmers Home Administration to issue mortgages for the purchase and repair of single family homes in rural areas and to provide financing and rental assistance for multifamily rental housing. Later legislation moved this function to the Rural Housing Service (RHS), which is part of the U.S. Department of Agriculture (USDA).

Section 502 housing loan guarantee programs provide well underwritten loan programs to low- and moderate –income individuals and families without having to make a downpayment because they may borrow up to 100 percent of the appraised value of the home. Since a common barrier to owning a home for many is the lack of funds to make a downpayment, this program makes the possibility of owning a home a reality for many Americans in rural communities.

The VA home loan guarantee program is an integral component of housing finance and is an outstanding example of a how a low- to no-downpayment program can perform even in difficult economic markets. The VA attributes its track record of success to strong principles of underwriting loans and high-touch service for its veterans throughout the mortgage process.

Appraisal System Reform

The current residential appraisal system is impaired due to inconsistent and conflicting standards and guidance; inadequate and uneven oversight and enforcement; a shortage of qualified and experienced residential appraisers; and, the absence of a robust and standardized data system. NAHB believes these problems must be addressed in order to restore confidence in the residential real estate market and to establish a foundation for sustainable growth of the U.S. economy. This can only be accomplished through sound valuation practices, policy, and procedures that produce more credible valuations under all economic circumstances.

In 2012, NAHB formed an Appraisal Working Group (AWG), consisting of home builders and representatives from the financial and appraisal sectors, to develop recommendations for comprehensive appraisal reform and produced a White Paper with specific recommendations.[6] In this process, there was extensive dialogue with all stakeholders in the residential appraisal

[6] "A Comprehensive Blueprint for Residential Appraisal Reform", National Association of Home Builders, February 2013.

process. The AWG continues to meet and discuss the importance of appraisal reform and below are their key recommendations:

- *Reform the regulatory framework for real estate valuation to more effectively oversee standards, guidance and enforcement.*

The goal is to better integrate and streamline the jumble of existing entities to ensure the valuation of collateral in housing finance transactions occurs in a coordinated and effective manner. This would contribute to uniform and consistent standards and avoid the current multitude of conflicting and confusing requirements. In particular, urgent steps should be taken to improve the effectiveness and consistency of state appraisal oversight.

- *Develop and build a real estate data superhighway with a national real property registry and supporting networks.*

The development of a real estate database would facilitate the safe and efficient transfer of real property. The reformed regulatory system would be responsible for the establishment of standards for data, methodology and practice. Stakeholders would be able to view all valuations, and secondary market participants would have access with proper rights established. Access rights would be granted to any registered purchaser, securitizer or servicer.

- *Establish a single, consistent set of rules and guidelines for appraisers and appraisals and set standards to ensure the engagement of an appraiser who has the training and experience necessary for the assignment.*

The establishment of a single set of rules and appraisal forms should be incorporated as a high priority as part of housing finance system reform. Currently, Fannie Mae and Freddie Mac impose de facto appraisal authority through the guidelines they have established for appraisals on the mortgages they purchase and the forms they use to collect appraisal information. These Enterprise appraisal rules tend to restrict appraisers' ability to pursue approaches that could result in more accurate valuation. In addition, confusion arises in how to interpret the Enterprise appraisal guidelines in relation to the rules established by The Appraisal Foundation (TAF) in the Uniform Standards of Professional Appraisal Practice (USPAP) and the appraisal regulations of the banking regulators.

In addition, there have been reports of appraisal problems due to appraisers not being familiar with the area in which the subject home is located and not having experience in valuing the type of property in question. This is a particularly acute issue for builders and purchasers of newly constructed homes, which normally require more extensive analysis and research. Standards and processes should be established to ensure appraisers have the training and experience needed to provide an accurate property valuation.

- *Develop a workable process for appealing inaccurate or faulty appraisals.*

It is extremely important to establish a timely value appeals process that is fair, balanced and appropriate to allow all parties of the transaction to appeal appraisals that do not meet USPAP standards or are based on inaccurate data or assumptions.

Today's residential appraisal system remains in a state of uncertainty. The current patchwork system cannot continue indefinitely. A key consideration must be to establish stability and restore confidence in the system that determines the value of mortgage collateral. NAHB remains committed to residential appraisal reform and looks forward to working with industry stakeholders to address the problems and implement solutions to the current U.S. residential appraisal system.

Multifamily Housing

Future Conventional Multifamily Finance System

NAHB and several of the most prominent trade associations representing multifamily developers, owners, property managers and lenders have prepared a set of principles under which we believe the future multifamily finance system should be framed. (The set of principles accompanies this statement.)

Key principles include:

- The nation's multifamily housing finance system should rely primarily on private capital.
- The federal government is the only entity that can ensure the availability of liquidity in all market cycles, and the appropriate mechanism to do that is through a catastrophic backstop role.
- The government guarantee-related market should be subject to strong and independent regulatory oversight and risk-based capital requirements.
- Policy makers should protect and preserve existing resources, as well as support greater transparency, during the transition to an overhauled housing finance system.

NAHB cautions against over-reaching in regard to reforming the multifamily finance system. This component of the nation's housing finance system has performed, and continues to perform, very well. NAHB does not believe it is necessary to take draconian steps that are not needed to "fix" an unbroken system. Such steps would include setting income or rent restrictions on loans as a condition of access to a federal government backstop, standardizing products, or requiring only one securitization platform. Again, NAHB believes that the critical consideration in a new system is broad and continued liquidity during all economic cycles and for all geographic areas.

Preserve Successful Infrastructure, Products, Programs from Conventional Market

As noted earlier, in spite of the crisis affecting single family housing, the multifamily sector has performed well. Multifamily loans held or guaranteed by Fannie Mae and Freddie Mac have very low default rates, and both businesses are profitable. Both of the Enterprises' multifamily businesses involve risk-sharing with private capital, and both businesses have practiced disciplined underwriting. In addition, because of the range of products and business lines employed by the Enterprises, a wide range of multifamily rental properties that provide housing for very-low to middle income households can be financed in the conventional market. NAHB strongly supports retention of the successful infrastructure, products and programs that have been built over the years by the Enterprises and which are used as the core of most of the major financial institutions providing multifamily debt financing.

NAHB is thus alarmed at recent actions taken by FHFA related to the Enterprises' multifamily businesses. In an August 2013 press release, FHFA stated it was seeking input on strategies for reducing the Enterprises' presence in the multifamily housing finance market in 2014. FHFA's Strategic Plan for Enterprise Conservatorships, released in February 2012, included a goal to contract the Enterprises' presence in the market while simplifying and shrinking certain operations. The 2013 conservatorship Scorecard included reducing their volume of new multifamily business by 10 percent relative to 2012. FHFA expects this reduction to be achieved this year through a combination of increased pricing, more limited product offerings and stronger underwriting standards. FHFA stated its intention to continue a path of gradual contraction of the multifamily businesses while awaiting a legislative resolution to the conservatorships.

It is disturbing to NAHB that FHFA is taking these steps in the absence of direction from Congress. NAHB believes that the FHFA's directive to the Enterprises to reduce their multifamily businesses is arbitrary and unnecessary. In fact, NAHB strongly believes that it is critical that the Enterprises retain their ability to provide broad liquidity to the market, which includes having a diversified line of products and the ability to address financing for a large range of multifamily property types.

This critical aspect of the Enterprises' mission – to provide liquidity during all economic cycles – should not be regulated by the conservator; that is the job of Congress. To lose any of the successful products or business activities at this point in time – before decisions are made by Congress as to the future of the multifamily housing finance market – means they may have to be rebuilt at a future point. NAHB has urged FHFA not to take unwarranted actions that will result in damage to the multifamily market now and in the future, and NAHB urges members of Congress to convey the same message to FHFA.

Private Market Participants are Selective Investors

It is important to understand that not all private market sources of capital for multifamily financing are available for all segments of the multifamily market. Each has strength in specific niches and markets and thus moves in and out of the market as economic conditions and their investment goals change. Life insurance companies typically target low-leverage, high-quality deals in the strongest markets (usually urban) and typically serve the highest income households. Once they meet their own portfolio investment targets, life insurance companies retract their lending. Banks do not provide long-term financing and are subject to significant restrictions in terms of capital requirements. Banks also have significant exposure to regulatory pressure that influences their lending decisions, including obligations under the Community Reinvestment Act (CRA). While the commercial mortgage backed securities (CMBS) market was significant at one time, it has not recovered from the financial crisis and is not expected to resume its past levels of volume.

These facts point to the need to maintain a viable, liquid and efficient secondary market for multifamily rental financing where the federal government continues to play a role. In addition, the secondary market must be structured to ensure that the appropriate range of products is available to provide the capital needed to develop new and to preserve existing rental housing, as well as to refinance and acquire properties. An adequate flow of capital will ensure that demand for rental housing is met and that affordable options are available for a range of households and communities.

Legislative Proposals

NAHB appreciates that S. 1217, the *Housing Finance Reform and Taxpayer Act of 2013*, introduced by Senators Corker and Warner, recognizes the importance of the Enterprises' multifamily businesses. The bill would transfer both multifamily businesses to the newly created Federal Mortgage Insurance Corporation (FMIC). However, NAHB does not believe it is practical for the regulator to absorb and run the multifamily businesses. A more practical option is to transition the Enterprises' multifamily businesses to private entities, which would then be allowed access to the federal government guarantee through FMIC.

The House Financial Services Committee-passed bill, H.R. 2767, the *Protecting American Taxpayers and Homeowners Act of 2013* (PATH Act), does not address the multifamily conventional market at all, which is a major omission.

<u>Maintain FHA's Multifamily Capacity</u>

FHA historically has played an important role in the financing of multifamily rental housing, and it was especially important during the economic crisis. FHA provides an explicit federal government guarantee on multifamily loans for which borrowers pay a mortgage insurance premium set by HUD. The FHA multifamily loans have performed well with low default rates (as published by HUD in May 2013), and the programs generate significant revenue to the federal government in the form of a negative credit subsidy, generating positive cash flow to the U.S. Treasury.

In 2008, FHA endorsed just over $2 billion in multifamily loans (excluding health care programs), which grew to $18.3 billion (excluding health care programs) in FY2013. This unprecedented increase in FHA multifamily loan volume occurred as other private market sources of multifamily financing withdrew from the market when economic conditions worsened. FHA, along with Fannie Mae and Freddie Mac, became the primary sources of multifamily financing as the recession deepened. Like in the single family market, the FHA multifamily mortgage insurance programs are fulfilling the function and mission for which Congress originally intended.

NAHB has long-supported these programs, notably Section 221(d)(4) and Section 223(f), which have enabled the construction of new affordable and market rate rental housing units, as well as the acquisition, refinance, and rehabilitation of the nation's existing stock of rental housing. Of importance, FHA financing is often used in smaller markets where Fannie Mae, Freddie Mac and other market participants are less active, and FHA has filled the niche that local banks and thrifts have retreated from in recent years.

Risk Management Protocols

It is important to note that over the last three years, HUD has instituted new risk management protocols for the FHA multifamily mortgage insurance programs. The new protocols tightened underwriting requirements, created a national loan review committee, and strengthened policies related to large loans, sponsor creditworthiness and experience. There is closer scrutiny on market strength and FHA presence than before the economic crisis. In 2012, for the first time in 10 years, HUD raised the mortgage insurance premiums (MIPs) for programs in the General Insurance/Special Risk Insurance (GI/SRI) fund. All of these actions were intended to strengthen risk management practices related to the FHA multifamily mortgage insurance programs, ensure the health of the GI/SRI fund, and attract high quality borrowers, without taking market share from the private sector or endangering taxpayers.

HUD's most recent step towards increasing efficiency and standardizing policies across field offices was the announcement of a major restructuring of the Office of Multifamily Programs. The restructuring in the Office of Multifamily Programs will consolidate its program Hubs and field offices and reorganize the offices within its headquarters in Washington, D.C. The goal of the restructuring is to allow more consistent, efficient processing of loans and servicing of existing assets.

NAHB has testified previously that, as important as these steps have been towards increasing risk management, the FHA multifamily field offices continue to struggle because of inadequate staffing and resources. NAHB is supportive of HUD's efforts to address these difficult issues, and we urge members of Congress to ensure that the department has the resources it needs to safely and properly manage its large portfolio and to ensure that the programs remain strong and viable.

Commitment Authority

NAHB recently expressed strong concern to members of Congress that the uncertainty related to the availability of commitment authority for the FHA multifamily programs creates the potential for major disruptions in financing much needed affordable and market-rate rental properties, as well as health care facilities, which are also included under the GI/SRI fund. FHA exhausted its commitment authority for FY2013 in mid-September, which forced borrowers to wait until new authority became available before they could be assured of a loan commitment. As a result, affordable housing construction and other related jobs have been delayed, and in some cases, may not even go forward. The government shutdown only made the situation worse, as the queue of loans waiting for commitment authority accumulated rapidly and is now in excess of one-half billion dollars.

NAHB suggests that an area of reform for the FHA multifamily and health care insurance programs is to consider giving FHA multi-year commitment authority, as is the case with the FHA single family programs. Another option would be to devise an automatic trigger of additional commitment authority if certain conditions are met to ensure the uninterrupted operation of the programs during all economic cycles.

Legislative Proposals – the PATH Act

NAHB is concerned about proposals to more narrowly limit FHA's current mission. The PATH Act would allow FHA to provide mortgage insurance for residential properties having five or more dwelling units – multifamily rental housing – subject to occupancy and rent restrictions applied during the life of the mortgages. The bill restricts occupancy to families having incomes no greater than 115 percent of area median income (AMI). It allows for higher income limits (up to 150 percent of AMI) in high cost areas. The bill gives FHA the discretion to establish lower occupancy, income and rent restrictions.

NAHB does not support setting occupancy and rent restrictions based on AMI for the FHA multifamily mortgage insurance programs. The Census Bureau's 2012 Rental Housing Finance Survey shows that an overwhelming majority of tenants in properties with FHA-insured mortgages have incomes of 115 percent or less of area median income. However, the FHA multifamily mortgage insurance program is also a key source of liquidity, so the imposition of income limits would impede that portion of FHA's mission, particularly in higher-cost markets.

The FHA multifamily mortgage insurance programs are subject to statutory mortgage loan limits, which effectively serve to focus the provision of FHA multifamily mortgage insurance on affordable and workforce rental housing. Imposing burdensome provisions that require developers, lenders and property managers to track and document incomes and rents on unsubsidized properties is costly and unnecessary, given that the proposed targeted population is already being served by the programs.

The PATH Act also requires the Director of FHFA to set capital reserve requirements for the GI and SRI funds. The bill does not specify target reserve ratios. Currently, there are no statutory requirements for capital ratios for either the GI or SRI funds. While NAHB understands that members of Congress and the Administration are focused on strengthening the risk management practices for both the single and multifamily FHA programs, NAHB strongly urges that an in-depth analysis is conducted to determine any impact on the mortgage insurance premiums for the FHA multifamily programs before any reserve requirements are considered. NAHB does not believe that it is appropriate to use the type of capital reserve ratios used for the MMIF for the GI/SRI fund, because the nature of the multifamily portfolio is significantly different from the single family portfolio insured under the MMIF.

The implementation of a capital reserve on the GI/SRI funds could have significant impacts on MIPs. Higher MIPs will lead to higher costs for borrowers and renters who are served by the FHA multifamily programs. A key example is the Section 221(d)(4) program where a higher MIP will raise the required borrower debt service and/or equity contribution, resulting in a lower mortgage amount at a higher rate of interest. These higher costs would be passed along in the form of higher rents to the low- and moderate income families who reside in rental units financed through the program or could result in properties not being built or rehabilitated because of the higher equity contribution required.

Need to Address Rural and Small Rental Projects

Over the years, NAHB has discussed with FHA and the Enterprises the need to develop more options for small multifamily financing (typically defined as 5 to 49 units) and to address credit needs in rural areas. According to HUD, almost a third of the nation's renters, more than 20 million households, live in small, unsubsidized housing. These properties tend to be owned by individuals ("mom-and-pop owners), as well as small businesses. Rents charged at such properties are typically more affordable to low-and moderate income families.

Owners of small multifamily properties do not have many options for financing acquisitions and/or rehabilitation work. Many lenders view such loans as high risk, and the costs of underwriting the loans are more expensive for both the lender and borrower. In addition, servicing costs for such loans are high, reducing lenders' incentive to make them. Small loans are not easily securitized, as it takes too long to accumulate the volume needed to issue a security.

The Enterprises have struggled with this type of loan, and FHA has not been successful at developing a viable small loan program. Although many local commercial banks are active in lending for small multifamily properties, the availability of financing is not very consistent. Large banks without a presence in rural areas have no Community Reinvestment Act (CRA) incentive to invest in such properties. Some state housing finance agencies address this need through set-asides for rural areas, where many small multifamily properties are located. A few NAHB members have been successful in refinancing a small portfolio of properties into one loan, which helps reduce costs.

HUD is currently exploring an expansion to its FHA risk-sharing program that would allow mission-based financial institutions to enter into risk-sharing arrangements with FHA to provide acquisition and rehabilitation financing for small multifamily properties. HUD is seeking a legislative change that would allow Ginnie Mae to securitize such loans. NAHB believes there is potential in this effort and has participated in several discussions with HUD and other stakeholders. NAHB urges Congress consider the legislative changes that are needed to develop a viable program.

As mentioned previously, the Corker-Warner bill acknowledges the importance of providing access to the secondary mortgage market to community banks. The proposed Federal Mortgage Insurance Corporation could provide opportunities for small multifamily lending.

Reform and Adequately Fund HUD's Rental Assistance Programs

HUD provides rental assistance to over five million households. Sixty-five percent of HUD-assisted households are elderly or disabled, and HUD-assisted families had an average income of $12,500 in 2012. Just one in four families that needs rental assistance is able to receive it because there are not enough resources to help everyone. The rental assistance programs have been under stress due to rising costs and the difficult economy. There are many potential areas for reform, yet agreement on how to proceed remains elusive. A major problem is the whipsaw of funding levels, which creates great stress on property owners, public housing agencies and residents.

Section Eight Housing Choice Voucher Program

NAHB has long supported the Section 8 Housing Choice Voucher program, which provides rental subsidies to approximately two million very-low income households who obtain housing in the private rental market. The program, which is intended to broaden the range of housing choices for families seeking affordable housing, has proven to be effective in helping low income families find decent, safe and affordable housing. In addition, the rental vouchers can be leveraged to build or rehabilitate additional affordable housing, a necessity in today's tight rental markets.

In recent years, the program has been the subject of policy discussions because of its growing costs and strain on the HUD budget. Funding levels have fluctuated, causing public housing agencies (PHAs) to struggle to maintain assistance to current tenants. A major reform bill first introduced in 2004 has been revised and debated without moving to passage. The goals of the most current House version, the Affordable Housing and Self Sufficiency Improvement Act of 2013 (AHSSIA), are to reduce taxpayer costs within HUD's rental housing programs and facilitate greater private-sector participation in affordable housing. Streamlining aspects of the program will reduce costs and improve the delivery of services to the households seeking affordable housing. Private property owners will be more amenable to participating in HUD's affordable housing programs, as well, as the administrative burdens are eased and costs to participate are lowered.

NAHB, along with a large group of industry stakeholders, has identified a core set of reforms to the program. Included are reforms that would streamline various processes, including: unit inspections; rent calculations; income determinations; and tenant screening. Other reforms would improve the voucher funding allocations to make them more stable and predictable while still permitting appropriators to set overall annual funding levels. While some additional improvements could be included, NAHB and stakeholders agree that it is important to move forward quickly on these consensus reforms.

Section 8 Project Based Rental Assistance Program (PBRA)

The Section 8 Project Based Rental Assistance Program (PBRA), which provides rental subsidies directly to property owners for specific properties, is at risk due to inadequate funding while costs are rising. The budget sequester that became effective on March 1, 2013, resulted in a cut of $470 million for the PBRA program in FY2013. HUD had to issue a letter to owners outlining its plans to manage the program due to the reduced funding, which included providing less than 12-months of funding to owners with expiring contracts. The short-fall becomes worse in FY2014 when 15,900 contracts (1.1 million units) will be up for renewal. HUD acknowledges that all contracts will be have to be less than 12-month funding due to an anticipated short-fall of over $1 billion.

The consequences of this funding uncertainty every year are many: property owners may stop participating in the program because of the uncertainty revolving around appropriations; property owners who continue may have to defer needed maintenance or reduce contributions to reserves, which means residents may lose good quality housing; lenders may be reluctant to provide financing for the rehabilitation of these properties because of the uncertain revenue stream. NAHB strongly supports adequate and predictable funding for the PBRA program.

USDA Rural Housing Service (RHS) Multifamily Programs

The USDA administers multifamily housing programs that help finance rental housing in rural areas. The Section 515 direct loan program provides long-term, low interest loans to non-profit and for-profit developers to support the construction, acquisition and rehabilitation of multifamily housing for low- and moderate-income renters. The program has financed over 15,500 properties with 443,150 units, with the average property consisting of 28 units. The USDA's Section 521 Rental Assistance (RA) program is project-based and provides rental subsidies to properties that were financed through USDA's Section 515 multifamily direct loan program. The majority of residents living in these properties are elderly, and average annual incomes are below $11,000.

Yet this valuable source of affordable rental housing for low-income rural families is in jeopardy of being lost. Section 515 funding has been cut drastically; the Section 521 RA program is experiencing a shortfall of funds due to sequestration, causing some property owners to have to take drastic steps to find funds to cover the shortfall for FY2013. It is very possible another shortfall will occur in FY2014, absent Congressional action. Property owners will not be able to maintain their properties without the RA funds and may be forced at some point to exit the program.

NAHB believes it is critically important that Congress take action to provide the funding needed to preserve this important portfolio of rural rental housing and to ensure that residents will continue to have affordable, decent and safe housing. However, funding is not the only issue; legislative action is needed to authorize a viable preservation program for the portfolio, as well as to consider what steps need to be taken to ensure the RA program can be sustained over the long term.

National Housing Trust Fund and Other Government Funding Programs

Housing Trust Fund

S. 1217 includes provisions to fund the National Housing Trust Fund (HTF) and to make some modifications to its purpose and eligible uses. The HTF was first created by the Housing and Economic Recovery Act of 2008 (HERA) and was to be funded by the Enterprises. However, the Enterprises went into conservatorship shortly after passage of HERA, and the conservator determined it was not in the interests of safety and soundness to allow the Enterprises to transfer funds to the HTF.

S. 1217 imposes fees on single and multifamily securities accessing the federal guarantee through the proposed Federal Mortgage Loan Corporation (FMIC), which would be transferred to the HTF. Eligible activities would include grants and loans that support sustainable homeownership and rental housing for households for a range of households. S. 1271 also includes a provision to ensure rural areas get proportionate shares of money and that states give priority to non-entitlement areas (population less than 20,000).
These provisions are consistent with NAHB's position on the purposes and uses of a national housing trust fund. NAHB believes that the purposes of a HTF should be broadly defined to include allowing a significant spectrum of eligible activities and with income targeting requirements that allow grantees and grant recipients to meet the fullest range of critical housing needs. It is important that the funds also meet the needs in rural and underserved areas. Also, NAHB believes that the statutory and regulatory framework of the HFT must allow for the effective and efficient use of trust fund monies in conjunction with other federal and state housing programs, particularly the HOME Investments Partnership Program and the Low Income Housing Tax Credit (LIHTC) program.

Finally, NAHB strongly believes that eligible recipients must include both for-profit and nonprofit developers, and all recipients must be able to demonstrate that they have the necessary experience and capacity to carry out proposed projects. Adequate standards of experience and capacity for grant recipients should be required, along with results-focused allocation criteria, to ensure the best possible use of these valuable resources.

<u>Role of the Home Investment Partnerships Program and Community Development Block Grants</u>

NAHB has long supported the HOME Investment Partnerships Program and Community Development Block Grant (CDBG) programs. These two programs provide invaluable support to cities, counties and rural areas in meeting their affordable housing and community development needs. The HOME program has been essential in providing gap financing for affordable rental housing financed with Low Income Housing Tax Credits, as well as for homeownership for first-time and low-income homebuyers. CDGB funds may be used to provide needed infrastructure that supports housing, such as sidewalks and streets, but also community centers, day care centers and other important community assets.

Both programs have suffered deep budget cuts. NAHB has consistently supported adequate funding for both programs and has also supported reforms that would ensure the funds are spent efficiently and effectively. NAHB has also supported efforts to streamline the use of HOME funds with other federal housing programs, especially those administered by state housing finance agencies (such as the LIHTC) and the USDA RHS.

<u>Low Income Housing Tax Credit Program</u>

The Low Income Housing Tax Credit (LIHTC) is the most successful affordable rental housing production program in U.S. history. It was created as part of the Tax Reform Act of 1986 as a more effective mechanism for producing affordable rental housing. Since its inception, the LIHTC has produced and financed more than two million affordable apartments. As LIHTC properties must generally remain affordable for 30 years, they provide long-term rent stability for low-income households around the country.

However, the demand for affordable housing is acute and exceeds the availability of financing through the LIHTC program. According to the most recently available annual survey released by the National Council of State Housing Agencies (NCSHA), state housing finance agencies generally receive $2 in requests for every $1 in LIHTCs available. At the same time, the supply of private, affordable housing stock is rapidly shrinking. Of the 6.2 million vacant or for-rent units with rents below $400 in 1999, 11.9 percent were demolished by 2009. Upward filtering to higher rent ranges, conversions to seasonal or nonresidential use, and temporary removals because of abandonment added to the losses. On net, more than 28 percent of the 1999 low-cost stock was lost by 2009.[7]

NAHB strongly urges Congress to maintain this critical affordable rental housing program.

[7] "America's Rental Housing: Meeting Challenges, Building on Opportunities" Joint Center for Housing Studies of Harvard University, 2011. Page 6.
http://www.jchs.harvard.edu/publications/rental/rh11_americas_rental_housing/AmericasRentalHousing-2011.pdf

Importance of a Reliable Supply of Affordable Acquisition, Development and Construction Credit

A significant factor in the availability and cost of homeownership and rental housing is the cost and availability of the credit required to produce such housing. This credit is referred to as land acquisition, development and construction (AD&C) financing. Affordable housing needs cannot be met by solely through utilization of the existing housing stock. This is particularly true if affordability is defined to include the cost of operating a home. Builders of new housing are required to meet increasingly stringent energy efficiency standards, which make new homes considerably less expensive to live in than older existing units. Also, new home construction occurs to satisfy consumer demand driven by lifestyle and location preferences such as urban living, multi-generational homes and fifty-plus communities. Therefore, significant levels of production of new homes will be needed to meet future housing needs in choices.

Since the affordability of newly constructed homes is affected by the availability and cost of AD&C loans, it is important to ensure that this form of financing is available at reasonable rates and terms. The home building industry is predominantly made up of small businesses and, currently, these companies are having difficulty in obtaining AD&C loans. These home building companies have traditionally relied on community banks for AD&C loans, but those institutions have been under severe regulatory pressure to curb their AD&C lending and reduce the concentration of such loans in their portfolios.

NAHB appreciates the efforts of Senator Robert Menendez (D-NJ) and Sen. Johnny Isakson (R-GA) for introducing The *Home Building Lending Improvement Act of 2013 (S. 1002)* that would address several of these regulatory barriers to sound construction lending. NAHB looks forward to working with this committee to advance regulatory reform in this area. Going forward, it does not seem likely that community banks will again resume the levels of AD&C lending previously undertaken unless some form of secondary market outlet is created to allow these institutions to sell their AD&C output and obtain liquidity for additional lending.

Conclusion

NAHB thanks the Committee for the opportunity to submit its views on essential elements to provide affordable options for housing. Whether they rent or own, Americans want to choose where they live and the type of home that best meets their needs. Given the significant role that housing plays in the economy, we urge Congress to take a long-term, holistic approach to housing finance reform. NAHB also urges Congress to carefully consider the differences between the single family and multifamily market and not apply solutions to one piece of the market that are not appropriate for the other. NAHB thanks the Committee for its leadership on this important issue, and stands ready to work with you to achieve such reforms and provide much-needed stability for this critical sector of the economy.