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RURAL MULTIFAMILY HOUSING POLICY PRIORITIES 2009

NAHMA will work closely with the new Obama Administration and Congress in order to address the major challenges to developing and preserving quality affordable multifamily housing. To that end, NAHMA has compiled a list of affordable multifamily rural housing policy priorities which we believe are necessary to improve owners' confidence in federal housing programs, streamline administration of the programs, and increase the choices of affordable communities of quality for low-income Americans. These priorities include:

1. Ensuring adequate funding for multifamily rural housing programs.
2. Reinstating the Section 538 interest subsidy removed from the program in the FY 2009 appropriations.
3. Advancing legislation to preserve the affordable multifamily rural housing portfolio.
4. Improving the process for and results of the improper payments audit.
5. Developing a policy within the management fee structure which uses financial incentives to reward management companies that exceed the minimum performance standards.

Please find more detailed descriptions of each NAHMA priority attached.

1. Ensuring adequate funding for multifamily rural housing programs.

NAHMA is disappointed that the Obama Administration's FY 2010 budget request has suggested flat-funding most of the rural multifamily housing accounts. We are concerned that Congress will not increase the funding levels for FY 2010, as evidenced by the current versions of H.R. 2997 and S. 1406, the FY 2010 Agricultural Appropriations bills. While the appropriations process is still ongoing, increases to the rural housing production and preservation programs will be modest at best. Additional funding for rural multifamily housing programs would produce additional units and preserve existing housing in rural markets, while also creating much-needed jobs and investment opportunities in these areas.

We are also concerned about the lack of interest subsidy for the Section 538 program in the FY 2010 budget request and current appropriations bills. The loss of the interest subsidy in FY 2009 reduced developers' ability to complete deals, provide additional capital for preservation projects, and improve the quality of tenants' lives. NAHMA urges RHS to request the interest subsidy in both the FY 2010 appropriations legislation and in the USDA's FY 2011 budget request.

Until recently, housing providers used the Low Income Housing Tax Credit (LIHTC) to help preserve, rehabilitate or construct rural apartment communities. However, the equity investment from the LIHTC program has become extremely sparse in rural America. It is more important than ever to have sufficiently-funded, well administered rural multifamily production and preservation programs to provide quality rental housing in rural areas.

NAHMA was pleased that the Obama Administration's FY 2010 budget request of \$1.09 billion for rural rental assistance would fund the contracts for their full 12-month terms at renewal. As of the last fiscal year, the terms of the rural rental assistance contracts changed to one-year contracts, requiring a much larger funding level than in years past. RHS should work with Congress to ensure adequate funding for rental assistance is provided in the FY 2010 appropriations cycle. It is imperative to avoid short-funding the contracts, which would significantly impede housing providers' ability to operate their rural properties.

Finally, we urge RHS to increase its funding requests for rural multifamily housing programs in the Administration's FY 2011 budget proposal. The economic and public policy arguments to invest in rural housing outweigh traditional budgetary concerns. Americans should have access to safe, quality, and affordable housing and good jobs, no matter where they live. We strongly urge RHS to request increased funding for its multifamily construction and preservation programs to stimulate investment in these often forgotten areas.

Therefore, NAHMA requests that RHS ask Congress to:

- **Provide adequate funding for rural housing programs that, at a *minimum*, match rising inflation and include Section 538 interest subsidies in the FY 2010 appropriations;**
- **Ensure adequate rural rental assistance funding to meet the needs of the contracts for their full 12-month terms at renewal; and**
- **Request increases in rural housing funding to at least match additional operational and inflationary costs and include Section 538 interest subsidies in the Administration's FY 2011 budget proposal.**

2. Reinstating the Section 538 interest subsidy removed from the program in the FY 2009 appropriations.

NAHMA members have said that without the Section 538 interest subsidy they are finding it harder to close deals. They no longer have the same opportunities the subsidy afforded them to increase capital and reserves for rehabilitation and property improvements.

In the FY 2009 Agriculture Appropriations Act, Congress removed the interest subsidy from the Section 538 program. This change had been initially requested by the Bush Administration. The interest subsidy paid for 2.5 percent of the interest on a conventional loan with a Section 538 guarantee. For example, if the lender offered a 7 percent interest rate on a Section 538 guaranteed loan with interest subsidy, Rural Development paid 2.5 percent of the interest on that loan. The effective interest rate for owner on the loan would have been 4.5 percent, which increased the capital available to complete the deal, and made the loan more affordable.

The interest subsidy also allowed properties to carry higher leverage on the loans. Higher leverage gave borrowers the opportunity to carry a higher loan amount, which allowed for improvements to the project and a better quality of life for the residents. For example, housing operators could upgrade the roof tops, provide better appliances for the tenants, or make other improvements to their properties while keeping rents affordable.

Historically, the Section 538 loan guarantees worked well with low-income housing tax credits (LIHTCs). The combination of programs helped to free up additional capital for preservation. However, the financial crisis has dried up much of the equity for investment, and rural areas have been especially hurt.

Representative Shelly Moore Capito (R-WV) has introduced legislation (H.R.1989) in the House to reinstate the interest subsidy, but it has yet to receive consideration by the House Financial Services Committee. Furthermore, the interest subsidy was not included in either of the House or Senate FY 2010 Agricultural Appropriations bills.

NAHMA is requesting that RHS:

- **Support the inclusion of Section 538 interest subsidies in the FY 2010 Agricultural Appropriations;**
- **Request the Section 538 interest subsidy in the FY 2011 budget proposal; and**
- **Support H.R. 1989, providing for subsidies for interest on loans for rural multifamily housing guaranteed by the RHS for FY 2009.**

3. Advancing legislation to preserve the affordable multifamily rural housing portfolio.

NAHMA supports legislative efforts to preserve affordable multifamily housing. Preservation is a cost-effective way to prevent a net loss of affordable rental housing. To NAHMA, “preservation” means maintaining the current portfolio of privately-owned, federally-assisted apartments as affordable to low-income families through a public-private partnership which offers **voluntary** incentives to owners and ensures long-term sustainability of the properties, including the ability to recapitalize. We respectfully recommend that any multifamily housing preservation bill be guided by the following principles:

- **Ensure long-term financial and physical sustainability of preserved affordable properties.**
- **Recognize the essential role of the Section 42 Low Income Housing Tax Credit Program to preservation.** The equity provided through the LIHTC program has been essential for preserving and rehabilitating older assisted housing, including rural properties. Without the equity from the tax credits, many rural properties in need of preservation may opt-out, default on their mortgages, or fall into physical disrepair. Unfortunately, the usefulness of the LIHTC in rural areas has significantly diminished since investors’ demand for LIHTCs dropped significantly as a result of the financial crisis. It is essential for Congress to pass legislation that stimulates investment in this program as soon as possible. NAHMA also believes an interagency group should be established to resolve conflicting regulatory requirements in the major federal rental assistance programs in order to streamline the use of mixed-financing.
- **Extend tenant protections when owners prepay their mortgages and when mortgages mature.** Our members support the contractual right to prepay their mortgages. NAHMA also supports extending tenant protection vouchers to income-qualified tenants in affordable rural housing when owners prepay or when the mortgage matures (and affordability requirements attached to the mortgage expire).
- **Create incentives to encourage voluntary transfer and preservation of affordable properties.** NAHMA strongly supports “exit tax” relief for owners who sell their properties to buyers who will continue operating the projects as affordable housing. We also believe a grant program which provides gap financing to qualified preservation entities (whether for-profit or non-profit) would facilitate more successful preservation transactions.

Rural housing preservation legislation (H.R. 2876 and Representative Barney Frank’s draft housing preservation bill) would offer much-needed tools to help preserve the USDA-subsidized rural housing portfolio. The bills would require each USDA-RHS property to create long-term viability and financial restructuring plans, as well as physical needs assessments, and provides property owners with additional preservation incentives. NAHMA also supports making tenant protection vouchers available to income-eligible households when the affordable use requirements on rural properties expire.

Although NAHMA supports many provisions in the rural preservation bills, we have serious concerns about specific sections. NAHMA strongly opposes language in these bills which makes owners ineligible for rural housing restructuring if they are involved in ongoing civil action to authorize the prepayment of the Section 515 loan or a damages action against the Emergency Low Income Housing Preservation Act of 1987, unless they agreed to repay a portion of the damages. This language would violate a court settlement agreement and penalize owners who exercised their legal rights to prepay. Additionally, we believe the proposed 30-year capital needs assessment is too far into the future to create a substantial outline of the property’s needs for the period. We would recommend creating a capital needs assessment for 20 years in order to refinance and restructure.

NAHMA urges RHS to work with Congress to achieve a workable rural multifamily housing preservation bill. We specifically request that RHS:

- **Oppose language in any rural housing preservation bill which prohibits owners from participating in a rural restructuring program if they have received court-awarded damages related to prepayment rights, or are involved in ongoing civil action related to prepayment, unless they agree to repay a portion of the damages;**
- **Support language in any rural housing preservation bill which authorizes a capital needs assessment period of 20 years;**
- **Support the Affordable Housing Preservation Tax Relief Act of 2009 (H.R. 2887), which will encourage the voluntary transfer of affordable properties to preservation entities through exit tax relief; and**
- **Take actions within RHS' existing regulatory authority to encourage preservation of the rural affordable multifamily portfolio.**

4. Improving the process for and results of the Section 521 rental assistance program improper payments audit.

The RHS Rental Assistance (RA) program is subject to reporting under the Improper Payments Information Act (IPIA) due to the size of annual appropriations and outlays. The IPIA audit is designed to determine if the appropriate RA subsidy is being paid on behalf of tenants. The basis for this determination is a review of the tenant's file and income verification documentation collected by the property manager. If documentation is missing, insufficient, or the subsidy calculated incorrectly, the subsidy payment is determined to be in error.

Since learning the results of the FY 08 IPIA audit, NAHMA has taken initiatives to help reduce errors in RA subsidy calculations. The initial results indicated an error rate exceeding 8 percent of RA payments. With the industry's help in getting the word out to our members about the importance of the audit, the final adjusted error rate was reduced to 3.95 percent. NAHMA sent grassroots action alerts strongly urging members to respond to the audit if their properties had been selected. We also strongly urged management companies to adopt policies and procedures that improve compliance training for on-site staff, including using checklists for required tenant file documentation. Likewise, NAHMA advocated for a change in the law which would allow the Enterprise Income Verification (EIV) system to be used to certify the income for tenants assisted through RA. EIV would allow rural housing providers to check reported income against Social Security (SS), Supplemental Security Income (SSI), new hires (W-4), and wage and unemployment compensation records. EIV would help ensure the right amount of RA is provided to qualified families. It would also help discourage fraud and create savings for the Section 521 program. We have continued emphasizing the need for these improved documentation and verification procedures to our members and to Congress.

RHS has acknowledged a substantial improvement in the final error rate in the audit of FY 09 RA payments, compared to the FY 08 results. The final adjusted error rate of 2.06 percent is the lowest rate since the agency began reporting six years ago. However, NAHMA understands that RHS remains concerned about income calculation differences on SSI and wages, medical deductions that did not match documentation, and lack of documentation in the files.

In May 2009, RHS informed NAHMA that the following measures would be put into place to reduce the error rate:

- a. "Establish a working group with the property management business partners and the Agency to continue providing educational opportunities for the industry regarding the importance of the IPIA process and the types of errors that were identified."
- b. "Implement a new management agent performance assessment review that will reward consistently compliant management agents and reduce management fees paid to noncompliant management agents. Errors made on tenant certifications will be one of six criteria used for determining reduction in management fees paid."
- c. "The National Office will continue to pursue access to the HHS New Hires data and HUD's Enterprise Income Verification System to be shared with State Offices and management agents."

NAHMA respectfully requests that RHS pursue the following recommendations to achieve further improvements in the IPIA audit results:

- **Inform the industry working group when the audit begins, so that we can inform our members to look for the letters announcing their project has been selected;**
- **In addition to contacting the on-site property manager, RHS should also contact the headquarters of the property management company responsible for the site;**

- **There is frequent staff turn-over at the site level. NAHMA believes contacting the property management company headquarters will offer greater assurance of a response , especially when the on-site property staff are new or inexperienced;**
- **Achieve greater consistency in field office policy and procedures;**
- **Refrain from adding unpredictable, punitive changes to the management fee structure; and**
- **Continue to pursue a statutory change which would allow the EIV system to be used for income verification in the RA program.**

5. Developing a policy within the management fee structure which uses financial incentives to reward management companies that exceed the minimum performance standards.

On August 7, 2009, Public Notice 431 announced the management fee schedule for FY 2010. The management fees will be effective January 1, 2010. The fee increases vary substantially from state to state. Texas received the largest increase of \$10.50 per unit per month, followed at a distant second by Nebraska's \$5.50 per unit per month increase. Seven states, Alabama, Idaho, Indiana, Michigan, Minnesota, Ohio and Wisconsin, will receive *no* increase in FY 2010 management fees. Our members are seriously concerned about the methodology RHS used to determine the fee schedule--particularly in states that are receiving no increase. It is unrealistic to assume that management costs will not increase in these seven states, especially considering the dismal economic conditions in those states. We strongly urge the agency to revise this fee schedule and to provide an appropriate, fair increase to management companies in all states.

Fairness was also a theme in NAHMA's comments about the Portfolio Management Division Draft of the Property Management Performance Assessment Review (PAR). We understand that many of the proposed changes are intended to reduce subsidy calculation errors and regulatory noncompliance. NAHMA is interested in working with RD to develop a policy which would use financial incentives to reward management companies that exceed minimum performance standards. We believe a positive, incentive-based approach is more likely to achieve the compliance that RHS seeks. On the other hand, we strongly oppose the redundant and counterproductive penalties proposed in the discussion draft. We strongly urge RD to remove the performance-based management fee penalties from the PAR, and instead, work with the industry to create a successful incentive-based system.

Furthermore, NAHMA strongly urges RD to convene a solution-oriented occupancy working group with its industry partners. Including occupancy factors in the criteria for the base management fee and penalties is a misguided approach. First, filling vacancies in the rural environment, especially without Rental Assistance, is very difficult. Many times, factors that cause vacancies are beyond the management agent's control. Secondly, RD *already* has a sanction for vacancies included in the management fee. Management agents are only paid for *occupied* units. A more prudent approach for RD is to work with owners and managers to identify ways that the regulations, handbooks and servicing tools can be improved so they can effectively address the factors that cause vacancy problems.

In matters concerning changes in the management fee schedules and structures, NAHMA respectfully requests that RHS:

- **Revise the FY 2010 management fee schedule to provide an appropriate, fair increase to management companies in all states;**
- **Refrain from adding unpredictable, punitive changes to the management fee structure;**
- **Convene a solution-oriented occupancy working group with industry partners to identify ways to improve the regulations, handbooks and servicing tools so they can effectively address the factors that cause vacancy problems; and**
- **Work with industry partners to create a successful incentive-based management fee system that would reward managers who exceed the minimum standards. We strongly believe an effective incentive-based management fee policy would:**
 - **Start with a minimum standard and build incentives into the management fee structure for those who exceed them;**
 - **Create objective, realistic performance standards that are attainable even for troubled properties;**
 - **Acknowledge the differences between fee-management and owner-management; and**
 - **Promote financial incentives for energy conservation and training for staff.**