



Testimony of the National Leased Housing Association
Presented by Allan Isbitz
Hearing on Affordable Housing Preservation – July 15, 2009
Committee on Financial Services
Subcommittee on Housing and Community Opportunity

My name is Allan Isbitz. I am Chief Financial Officer and Vice President of Real Estate Development for Jewish Community Housing for the Elderly, a nonprofit that owns and operates federally assisted housing for the elderly. I am here today as the recently elected President of the National Leased Housing Association. My affordable housing experience covers a broad area in affordable housing, including eight years in public sector service at the state and local level, several years in private, for-profit development of mixed income housing and my current service in the nonprofit affordable housing arena

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

Madame Chair and members of the subcommittee, thank you for the opportunity to testify. NLHA has been working over the past two years with you and the committee staff to craft workable legislation that will facilitate the ability of our members to preserve the stock. We appreciate everyone's hard work as we know that many of these issues are narrow and highly technical. Preserving the scarce supply of federally assisted rental housing is imperative as the demand remains high and the supply is not being notably increased. Further, it is much more cost effective to preserve housing than to engage in new construction. Most preservation transactions involve between \$25,000 and \$45,000 per unit in rehabilitation. New construction would cost well over \$150,000 per unit.

A number of the provisions in the bill will be helpful in addressing current barriers to preservation activities, and we are pleased that the bill addresses the need to provide enhanced vouchers to residents when subsidized mortgages mature and will amplify the importance of this issue later in our testimony.

We also approve of efforts to enable properties to convert enhanced vouchers where necessary to project-based vouchers in order to retain the assisted housing stock as well as the provision permitting the transfer housing assistance payment contracts to other properties. However, we remain concerned that the revised draft includes provisions that will restrict or otherwise abrogate current housing assistance contracts or mortgage agreements. The ability for housing providers to rely on their contracts with the Federal Government is essential to their continued participation as partners in providing this housing. Further, there is an active and large community of preservation entities that have been in the business of

preserving older assisted housing properties for the last ten years therefore negating any need for forced preservation. We understand the draft is only a starting point and appreciate recent remarks by Chairman Frank confirming that it is not his intention to violate contracts and look forward to further revisions to the bill.

Due to time constraints, our testimony today is limited to a portion of the draft bill's many provisions. We will be providing the committee staff with substantive technical comments on all of the draft provisions as we did last year and look forward to a continuing dialogue.

HUD Policies

Many problems that have faced preservation entities and current owners of assisted properties in recent years are the direct result of inconsistent HUD policy application. There are quite a number of existing tools that used in tandem can accomplish preservation including the Low Income Housing Tax Credit program, the provision of enhanced vouchers, the use of project-based vouchers, the ability to decouple a 236 mortgage from the Interest Reduction Payment (IRP) and leverage the IRP as part of a refinancing, etc. However, the barriers that we have faced were often related to HUD inaction or lack of cooperation.

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

In that regard, we are very pleased that Secretary Donovan has recognized many of the barriers created by HUD in the past and his stated commitment to changing the way HUD does business in the future. The Secretary's vast experience in the housing arena and commitment to preservation is welcomed by the industry. Further, we applaud his appointment of Carol Galante as the Deputy Assistant Secretary for Multifamily Housing and look forward to working with her and Secretary Donovan to facilitate preservation efforts and ongoing operation of the assisted housing portfolio

Example of HUD Impact

I would like to spend my brief time today sharing an experience with a transaction where during the last several years, HUD's unwritten policy and inconsistent guidance proved a barrier to recapitalizing our current properties and investing in a new affordable building.

HUD approval is sometimes needed when a subsidized project is being sold or refinanced. Without statute or regulation, HUD over the last few years has arbitrarily limited the use of surplus sale or refinancing proceeds where the owner is a non profit sponsor, proceeds which the nonprofit could otherwise use for other subsidized properties or to further its mission.

In our case, in late 2006, we undertook a refinancing of a Section 236 elderly project last year, received an allocation of tax credits, etc to renovate the property and to use the other proceeds to build a community center for the residents and to subsidize rents in a mixed financed elderly project we were planning to build. The transaction needed HUD approval because the transaction was a decoupling of the 236 mortgage from the interest reduction payment (IRP decoupling) which requires prepayment approval. HUD withheld approval because it claimed the proceeds were "too high." HUD's position was incomprehensible because the transaction's proceeds were all generated via sale of the tax credits based

on the value of the property. Further, the transaction was structured in a way that would save HUD nearly \$5 million in Section 8 subsidies over the term of loan. HUD would only approve the transaction if Jewish Community agreed to a use restriction that put the proceeds from the “refinancing” into a Trust. HUD dictates how we are to use the funds limiting them to fund future Section 8 rent increases. While the terms were unacceptable, we were forced to sign the agreement in order to complete the transaction.

There is no basis in law or in regulation for HUD’s actions and as a result a number of needed renovations were scaled back and efforts to complete the development of a new building are currently being affected because HUD will not approve the release of our funds to us to complete the new property. Again, HUD has no authority to restrict the proceeds, yet they did so as a condition of approval of the prepayment. We are working with the staff of the new HUD administration and they have expressed a willingness to work with us. We are hopeful that a resolution will be forthcoming to enable us to complete our new development. However HUD’s actions in recent years remain an issue for other nonprofits so it will be helpful for Congress to clarify this issue. The current draft includes language that attempts to address the issue, but is not retroactive. We prefer the language that was included in Section 401 of H.R. 2930 that passed the House last year and request that it be substituted for Section 503 of the current draft.

Preservation Vouchers

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

The current statute needs to be amended (as proposed in the draft bill) to address two situations that were not contemplated in 1996. Firstly, it was not necessary to address mortgage maturations in the context of enhanced vouchers as the Section 236 properties or Section 221(d)(3) BMIR properties were at least ten years from their mortgage maturation (original mortgage terms 40 years and owners in most cases had a right to prepay the mortgage after 20 years). When the mortgages mature, the accompanying affordability requirements expire (including ELIHPA projects). In January 2004, the GAO issued a study on such mortgage maturations and projects that 11,267 mortgages will mature through 2013. The first such maturations have already occurred, and will peak after 2008.

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

Treatment of Ownership Entities

Any legislation designed to preserve the assisted housing inventory must recognize the complexity of preservation transactions and present opportunities for both for profits and nonprofits. The current draft bill appears to favor nonprofits although some definitions have been revised from the previous draft. NLHA represents both nonprofit and for profit developers and has always believed that the industry benefits from the participation of any entity that has the commitment and expertise to provide quality affordable housing. Further, many transactions are the result of partnerships between the public and private sector. It is our belief and experience that the distinction between nonprofit and for-profit participants should be blurred with the focus on good stewardship of the housing.

Access to Information

The draft bill includes several provisions to increase HUD's collection of data and make that data more accessible via HUD's website. There is no disagreement that HUD's data systems leave a lot to be desired and that the information available on its website is often hard to find, however the draft bill appears to request information be made available on the web that should be protected under privacy laws (home address of investors, 2530 forms which contain social security numbers, etc.). We would oppose any attempt to provide the public with access to private information. We understand that the goal is to provide information to the residents and the public about the condition of the buildings. However that can be accomplished without exposing participants to identify theft or other harms caused by the release of private information. HUD currently posts information about the physical condition of properties along with information concerning any enforcement actions resulting in suspension or debarment.

Issues Affecting the 202 Program

We are pleased that the subcommittee has included provisions in the draft to facilitate the preservation of Section 202 properties for the elderly. As with the preservation of other properties, the sticking points have often been at the HUD level. For example, HUD had determined that a 202 loan could not be refinanced if there was no corresponding decrease in debt service. There is no statutory prohibition for such a restriction and it is certainly not realistic. Further, HUD has administratively (through a change to its Section 8 guidebook) limited rents achievable through a refinancing when tax credits are being utilized and rents are set using a budget-approach. The goal of a refinancing is to generate proceeds to recapitalize the property. The 202 provisions in the draft preservation bill would revise current HUD policy and will result in the renovation and preservation of many more properties.

Tax Law

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

The enactment of such exit tax relief would provide an immediate stimulus to the economy. The House has introduced bills legislation that would accomplish such preservation. We urge the Committee to encourage the Ways and Means Committee to take action on H.R. 2887.

Further, the Low Income Housing Tax Credit (LIHTC) program is the primary vehicle for recapitalizing properties as part of preservation transactions. The current equity climate has reduced the number of transactions that can be finalized but we are hopeful that the tax credit exchange program enacted as part of the stimulus bill will spur activity in this arena in the next year. However, with the economy still in a recession, it may be necessary to enact other short term tax changes that will bring investors back to the table. NLHA is working with its industry partners on several items that we believe will have an impact on raising equity which we will share with this Committee along with the House Ways and Means committee for review and comment.

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