Homeownership Alliance

Homeownership Alliance Comments on FHFA Comprehensive Review of FHLB System

The Federal Home Loan Bank System (FHLB System) was created during the Great Depression to provide reliable liquidity to financial institutions responsible for supporting home mortgage lending and community investment. Consistent with this vision, the Federal Home Loan Banks (FHLBs, FHLBanks or Banks) delivered significant mission benefits that advanced affordable homeownership and community investment as part of the broader U.S. housing finance system over time. In particular, the FHLBs have provided important access for its Members and nonprofit housing development partners to essential capital, liquidity, gap-filler subsidies and homebuyer assistance, which in turn, has made many affordable housing projects feasible that otherwise would not have been.

However, the financial institutions that the system was originally designed to support (Savings & Loans) no longer exist, and the majority of home mortgage lending and related mortgage liquidity functions now occur outside of the FHLB framework. Today, the primary role of the FHLBs is to provide secured loans (advances) at preferential rates to their 6,800 Members, a significant portion of which are commercial banks and insurance companies that do not do mortgage lending as a core activity or at all. At the same time, the severe underproduction of housing over the past decade[1], coupled with acute and worsening affordability, has resulted in a true national housing crisis. Fewer and fewer lower income households can attain the benefits of homeownership (e.g., housing cost stability, housing security, and equity appreciation); and more lower income families are housing-cost burdened and housing insecure. These problems are especially acute for Black and Latino families.

In this context, and after taking into account the statutorily-mandated contributions of the FHLBs, such as to the Affordable Housing Program (AHP),[2] as well as voluntary contributions to other affordability initiatives, **the sustained level of FHLB System profitability suggests that the public benefit commitment of the FHLBs could be increased without compromising system safety and soundness or other important member considerations.** In 2021, for example, mandatory contributions to AHP by the Banks totaled $201 million[3], and AHP awards totaled $354 million[4]; whereas the combined net income of the FHLBs in 2021 totaled $1.77 billion (after AHP contributions)[5], and dividends paid to Members totaled $1 billion[6]. **FHLBanks *can and should* do more to advance their public benefit purpose and mission outcomes at year 90 and beyond. As the FHFA conducts a comprehensive review of the system, we call upon the FHLBanks to do so.**

The need for increased mission investments by the FHLBs is especially pronounced in underserved low and moderate income (LMI) communities, where non-depository CDFIs focus their work but many other financial institutions do not. By increasing the number of non-depository CDFI Members across the system, and scaling innovative partnerships - both through the CDFI-FHLB Working Group and as proposed below- FHLBs can generate significantly greater mission impact in ways that also strengthen core business activities and bottom line profitability. The Homeownership Alliance[7], a policy collaborative of 31 CDFIs and leading nonprofit affordable housing developers from 19 states offers the following recommendations for consideration by the FHFA and the FHLB System.

Recommendations

As the FHFA and Congress appropriately consider requiring a higher mandatory mission contribution by the FHLBs, there are a range of mechanisms that the Banks could employ to respond proportionately to the national housing crisis, while still focusing on local and regional priorities. We urge the FHFA and the Banks to consider implementing the following recommendations, which would also create more demand for core FHLB products and services, and strengthen the System overall.

- **Create an FHLB Reinsurance Pool to Offset Collateral Valuation Risk and Expand Non-Depository CDFI Members' Access and Impact**
  The collateral valuation methodologies and related *haircuts* applied to Advance requests from non-depository CDFIs today are a significant impediment and consistent obstacle to the participation of these Members in FHLB system. The haircuts range from 10% to 90% and vary over time. While these policies are designed to offset credit risk[8] introduced by non-depository CDFI collateral, they also significantly limit lending and investment potential in LMI communities, as well as FHLB mission-impact and reach.

  For example, a non-depository CDFI in the Southwest offers a $10 million portfolio of Single Family loans as collateral for a $10 million advance request. The FHLB of Dallas applies a 40% discount, and provides a $6 million advance at a significantly reduced LTV. However, if the identical asset were offered as collateral by a federally-regulated and federally-insured Member, no discount would apply and -all else being equal- the FHLB would issue a $10 million advance at a significantly higher LTV. As a result, the non-depository CDFI Member accesses significantly less capital through the System for use in underserved target markets.

  To enable non-depository CDFIs to qualify for full Advances while also meeting important safety and soundness standards across the system, we ask the FHFA and FHLBs to consider the following alternative. *FHLBanks should establish and fund a shared insurance / reinsurance pool that would serve as a first loss back-stop on advances to non-depository CDFIs.* This mechanism would allow for valuation discounts to be eliminated or significantly reduced. FHLB resources used to capitalize such a pool should count as a mission contribution in the year that the commitment is made, and thus provide an offset against any mandatory minimum contributions above the current 10%. To further define and operationalize this concept, we recommend dialogue among CDFI-FHLB Working Group members.

- **The FHFA should encourage or require each FHLBank to create an *Affordable Homeownership Strategy and an additional dedicated funding stream* specifically to ensure that more entry-level homes are produced and made available to LMI homebuyers.** This is key to solving the national housing crisis; for without a major increase in the production and preservation of affordable homes, many LMI families will continue to be priced out of the home sales market – including by institutional investors and all-cash buyers- and will instead be forced to pay rising rents that their incomes cannot sustain.

  In addition to enhanced access to advances and other forms of flexible and favorable capital stack financing, nonprofit developers need additional and *deep(er) development-side subsidies from FHLBs* in order to finance, build and price more starter homes at levels that LMI families can afford. To ensure that these resources reach homeownership projects that are prioritized locally but that may not score competitively in the already oversubscribed AHP program[9] [10], each FHLBank should allocate and award these dedicated funds separately from AHP funding pools and processes.

  The need for deeper development subsidies, and the production potential they can achieve is exemplified by two recent Homeownership Alliance member projects from different markets.

  - **23-Unit Permanently Affordable Condominium Project in Stamford, CT** - The Housing Development Fund (HDF), a certified CDFI[11], is nearing completion on *Washington Crossing*, a 23-unit affordable condo project serving homebuyers at or below 50% of Area Median Income (AMI) in the South End neighborhood of Stamford, CT, an extremely high cost market. Purchase prices of these 2- and 3-bedroom homes range from $240,000 to $310,000. By comparison, the median value of condos / coops in Stamford, CT as of September 2022 was $337,557 (+9.3% year-over-year).[12]

    Hard and soft development costs totaled approximately $447,000 per unit. Delivering these homes to mortgage-ready households at or below 50% AMI required HDF to raise $4.5 million (or approx. $196,000 per unit) in development-side subsidies to absorb forty percent of total building costs. Additionally, purchasers qualified for and received an average of $68,500 in Down Payment and Closing Cost assistance, as well as favorable mortgage financing offered through HDF's SmartMove Connecticut program. All 23 of the homes at Washington Crossing will remain permanently affordable through the use of a Community Land Trust / shared equity ownership model.

- **20-Unit New Construction Shared Equity Condominium Development in Winooski, VT -** Champlain Housing Trust (CHT) recently completed the *Butternut Grove Condominiums*, a 20-unit, urban infill development in Vermont's most densely populated city. Development costs totaled $7.8M, and included $4.4 million (or $206,000 per unit) in deep subsidies to make all of these 2- and 3-bedroom homes (a mix of flats, townhomes and row houses) affordable to homebuyers at or below 100% AMI (or $96,000 for a family of three) with an average purchase price of $169,000. Additionally, eligible purchasers accessed up to $25,000 in Down Payment Assistance through CHT's Homeownership Equity Program, a special purpose credit program.

  The affordability of these homes is permanently preserved through CHT's Shared Equity Homeownership program, which –over 35 years- has made 671 homes affordable for over 1,200 LMI owners. The median price of all condominiums and town homes sold in Crittenden County in September 2022 were at $272,500 (+9.9% year-over-year) and $427,250 (+44.3% year-over-year),[13] respectively. In this market context, Butternut Grove represents a rare affordable ownership opportunity; and all homes have been sold or are under contract.

- **As part of a new *Affordable Homeownership Strategy*, each FHLB should also commit substantially more resources for Closing Cost and Down Payment Assistance, favorable financing, and innovations that overcome barriers for LMI homebuyers to purchase an entry-level home in difficult market conditions.** This could include interest rate buy-downs and alternative credit evaluation including products classified as *Special Purpose Credit Programs*.

  An October 2022 analysis from *CoreLogic* found that the average down payment for low-tier homes (those priced at less than 75% of the median sales price) increased to an all-time high of $30,186 in June 2022, up from $26,314 in June 2021 and $11,403 in June 2010.[14] This challenge applies to many LMI homebuyers who qualify for low down payment mortgage programs. For example, 25% families who recently completed one Homeownership Alliance member's homebuyer readiness program lack adequate cash resources to cover down payment and closing costs. As housing supplies remain constrained and as costs continue to escalate, this barrier to homeownership will continue to grow. The FHLBanks could help to meet this need in ways that would generate additional mortgage origination and servicing opportunities for their Members.

- **FHLBs should also expand the supply of affordable housing at scale by building on existing partnerships with CDFI Members and advancing new CDFI-FHLB partnership opportunities.** The CDFI-FHLB Working Group, which includes approximately 30 CDFI Members and representatives of all 11 Banks[15] met in 2020 and found common ground on several fronts including the possibility of developing standardized products designed specifically for CDFIs that would be available in every region. They also discussed moving forward with several pilots. All 11 banks agreed with these preliminary ideas, but the effort paused during Covid. *<u>The Homeownership Alliance asks the FHLBs to recommit to this process now and to move it measurably forward in 2023.</u>*

- **As also discussed by the CDFI-FHLB Working Group in 2020, FHLBs should develop and facilitate matchmaking opportunities between non-depository CDFIs and other bank Members that are in need of CRA credits.** The system should facilitate increased access to capital and FHLBank advances for non-depository CDFI Members by pairing them with CRA-eligible Members, many of which have excess capital that could address the non-depositories' needs while generating CRA credit. By putting non-depository CDFIs and CRA-eligible Members together, both parties could benefit.

<u>Additional Input for Consideration</u>

- **Importance of Scale –** The ability of housing practitioners to respond proportionately to the national housing crisis today requires scaling systems, capital, subsidies, and partnerships accordingly. Successful partnerships with FHLBs have allowed non-depository CDFIs and nonprofit developers to achieve such scale with specific programs and initiatives. <u>We urge the FHLBs to seize opportunities to invest in- and leverage the capacity of these mission partners in order to deliver mission outcomes at the scale needed today and going forward.</u>

- **Importance of Regional FHLB System Structure –** The FHLB System's regional configuration is key to the success of FHLB partnerships and to meeting the unique needs and priorities of local markets in innovative ways. <u>We urge the FHFA to maintain the current regional framework and focus of the FHLB system and of the FHLBs.</u>

- **Member Advances - Usage Data and Evaluation of Outcomes** - We encourage the FHFA to collect and evaluate data from the FHLBs on the use of Member Advances, similar to its evaluation of AHP, the Community Investment Program (CIP) and the

Community Investment Cash Advance Program (CICA). Better understanding direct and indirect benefits of Member advances would be helpful for assessing the overall mission contributions of the FHLBs. It would also provide additional overall transparency to a complex, taxpayer-supported system.

Conclusion

The FHLBs are important partners that non-depository CDFIs and nonprofit housing developers count on to deliver needed capital and subsidy resources for housing investments in underserved communities. **However, the system *can and must* do more to fulfill its public purpose mission and to address the nation's severe housing crisis today.**

We urge the FHFA and Congress to require and incent FHLBs to do deliver substantially more resources to support increased affordable homeownership opportunities at scale and commensurate with national needs. We also urge FHLBs to reduce barriers that limit non-depository CDFI Members' access to advances. Finally, we urge the FHFA to encourage the FHLBs to expand the membership of- and partnerships with non-depository CDFIs, which can yield substantially greater mission outcomes in 2023 and beyond.

The Homeownership Alliance appreciates the opportunity to provide these comments. For follow up questions, please contact David Hunter at dhunter@stabilizationtrust.org or Kristin Siglin at ksiglin@stabiliztiontrust.org.

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[1] https://upforgrowth.org/apply-the-vision/housing-underproduction/

[2] The Federal Home Loan Bank Act requires each FHLB to annually contribute to its AHP program the greater of 10% of annual net income or a prorated amount that, when combined with the contributions from the other FHLBs, totals at least $100 million for each year. Source: *12 USC Section 1430 and Section 1430(j)(5)(C)*.

[3] On a combined basis, mandatory contributions to the AHP program totaled $201 million in 2021, $315 million in 2020 and $362 million in 2019. Source: *Federal Home Loan Banks Combined Financial Report for Year Ended December 31, 2021. Pages 80 and 89-90 (Figure 31)*.

[4] On a combined basis, the FHLBanks awarded a total of $352.4 million from AHP programs in 2021, which supported 32,000 LMI housing units. Note that total AHP funds *awarded* annually may include adjustments from previous year contributions to AHP by FHLBs or accelerated amounts for future year contributions. From 1990 to 2021, the FHLBs contributed approximately $7 billion the AHP. Source: *FHFA Report 2021 Low-Income Housing and Community Development Activities of the Federal Home Loan Banks.* Pages 2-4 and 5-7.

[5] On a combined basis, FHLBank net income (after AHP assessments) totaled $1.77 billion (2021), $2.79 billion (2020), and $3.19 billion (2019). Source: *FHLBanks Combined Financial report for Year Ended 12/31/21.* Pages 80 and F-8.

[6] On a combined basis, dividends paid by the Banks to Members totaled $1 billion in 2021, $1.55 billion in 2020, and $2.12 billion in 2019. Source: *FHLBanks Combined Financial report for Year Ended 12/31/21*. Page 47.

[7] https://www.stabilizationtrust.org/homeownership-alliance/

[8] Federal Home Loan Bank System Lending and Collateral Q&A for 2021 Q4. Page 6. Issued March 25, 2022. https://www.fhlb-of.com/ofweb_userWeb/resources/lendingqanda.pdf

[9] For 2021, the FHLBs approved, on average, 45% of AHP Competitive Program Applications Received. Source: FHFA Report *2021 Low-Income Housing and Community Development Activities of the Federal Home Loan Banks*. Page 8, Figure 3.

[10] For all AHP competitive application program projects funded between 1990 and 2021, 63% (12,093) were rental projects, and 37% (7,050) were owner-occupied projects. Correspondingly, 79% (609,409) of the units were rental, 21% (164,067) were owner-occupied units. Source: FHFA Report *2021 Low-Income Housing and Community Development Activities of the Federal Home Loan Banks*. Page 52, Figure B.

[11] The Housing Development Fund is not a CDFI Member of the Boston FHLB. It is precluded from membership because HDF's President and CEO serves as an independent director on the Boston FHLB Board.

[12] Zillow Home Value Index as of September 30, 2022. Condo/coop $337,557. 1-year Value Change: +9.3%.

[13] Redfin Sales Data for Chittenden County Housing Market, September 2022.

[14] An October 2022 analysis from CoreLogic. The analysis shows that the average down payment percentage for low-tier homes was about 12% of the sales price, up from 11% in June 2021 and 9% in June 2010. (Sales price tiers are based on the median price of all home sale transactions at a metro level in a given month. The size of required down payments are determined in part by the purchase price of a home. With increases in home prices over the last few years, average down payments have followed suit.)

[15] FHLB-CDFI Working Group; 2020 Presentation.