From NLIHC's *Memo to Members* February 2, 2015

HUD Publishes NHTF Interim Rule

HUD published the long-awaited National Housing Trust Fund (NHTF) rule in the *Federal Register* on January 30. Instead of publishing a final rule, HUD issued an interim rule intending to solicit comments after states have gained experience administering the program. The interim NHTF rule adopts most of the provisions in the proposed rule and will go into effect on March 31. In a media release, HUD Secretary Julián Castro anticipates that states will receive their NHTF allocations by summer 2016.

This article reviews the most meaningful changes, including those suggested by NLIHC, as well as some suggested changes that HUD did not accept.

NHTF AND HOME

The NHTF rule is at 24 CFR part 93, a new part of the *Code of Federal Regulations*. The proposed rule established the NHTF rule as subpart N of the HOME Investment Partnerships program rule at 24 CFR part 92. NLIHC objected and HUD agrees that "it would be clearer to place the HTF regulations into a new 24 CFR part."

Where the NHTF statute does not prescribe specific features of the program, HUD uses the HOME regulations as a model for the NHTF regulations, especially since states, which are the NHTF grantees, "are already familiar with the HOME's basic compliance requirements." As part of HUD's intent to synchronize the NHTF and HOME regulations, major changes from the proposed NHTF rule include importing from the final HOME rule a number of definitions, extended affirmative marketing, displacement and relocation, conflict of interest text, and modified property standards text.

INCOME TARGETING

HUD proposed the formula for allocating NHTF to the states, the District of Columbia, Puerto Rico, and the four Insular Areas (Guam, Northern Mariana Islands, U.S. Virgin Islands, and American Samoa) on December 4, 2009. NLIHC fully endorsed the proposed formula because it was consistent with both the letter and spirit of the enabling legislation. The statute specifies four factors, which the interim rule contains along with mathematical weights. Two of the factors are data about need for rental housing affordable for extremely low income (ELI) households. These two factors have a combined weight of 75% of the formula. The statute defines ELI as the greater of 30% of AMI or the federal poverty level.

Another measure of the statute's emphasis on ELI renters is its provision that at least 75% of a state's NHTF money used for rental housing benefit ELI households, and that no more than 10% the state's NHTF be used for first-time homebuyer activities. The interim rule's income targeting provisions reflect the statute. They are a streamlined version of the proposed rule and introduce a new concept, establishing a $1 billion threshold for ELI targeting. For years in which there is less than $1 billion for the NHTF, states must use 100% of their allocation for the benefit of ELI households. For years with more than $1 billion available, states must use at least 75% of their NHTF for the benefit of ELI households, and may spend up to 25% for the benefit of VLI households. NLIHC estimates that during the initial years, there will be less than $1billion for the NHTF.

SMALL STATE MINIMUM

The statute provides that each state and the District of Columbia is to receive a minimum NHTF allocation of $3 million. The preamble to the interim rule notes that the statute does not envision a situation in which the NHTF would lack sufficient funds to award each state and the District of Columbia a minimum grant of $3 million. At the same time, the statute calls on HUD to distribute available funds. Therefore, the interim rule provides that in any year in which there are not sufficient funds to provide $3 million to each state and the District of Columbia, HUD will publish a notice in the *Federal Register* describing an alternate method of distributing available funds and seek comments.

OPERATING COSTS

With respect to rental housing, the statute provides that NHTF assistance may be used for production, preservation, rehabilitation, and operating costs. The interim rule increased the percentage of a state's allocation that can be used for operating costs to 33.3%; the proposed rule limited it to 20%. In the preambles to both the proposed and interim rule, HUD asserts, "The HTF is primarily a production program meant to add units to the supply of affordable housing for ELI and VLI households." In response to comments disagreeing with the 20% cap, HUD replies, "Analyses of the use of HTF funds for both development and operating cost assistance showed that the use of HTF funds for operating assistance could quickly consume each State's annual grant. This would deter the use of HTF funds for production of additional units, as well as preservation and rehabilitation of units targeted to ELI households – the primary purpose of the HTF." The one third cap applies to both amounts used for operating cost assistance as well as for funding an operating cost reserve.

The proposed rule stated that operating cost assistance could be provided for the entire affordability period, but could only be awarded in two-year increments from each NHTF grant. The interim rule changes this, allowing a grantee to commit funds from an NHTF grant received in a single fiscal year to provide funds for operating cost assistance over multiple years, as long as the funds committed in that single fiscal year are actually spent within five years. The proposed and interim rule requires all NHTF monies committed to be spent within five years.

The proposed rule would allow NHTF dollars to be used to fund an operating cost assistance reserve for a project, but would limit the amount of the reserve to the amount needed to provide operating cost assistance to NHTF-assisted units for a period of only five years. Based on a separate, federal government-wide statute, agencies are limited in their ability to commit future appropriated funds.

Developers of affordable housing for ELI households commented that the proposed rule's five-year limit on the use of NHTF for an operating cost reserve would make it difficult to increase affordability for ELI households. In the preamble to the interim rule, HUD indicates that it understands the need for capital (replacement) and operating reserves to be funded upfront for the present value of the entire amount needed over the minimum required affordability period of 30 years. However, appropriated federal funds cannot be drawn years in advance of their need; hence the proposed rule's five-year limit remains in the interim rule. However, for non-appropriated sources, such as the proceeds from the assessments on Fannie Mae and Freddie Mac as called for in the statute, the interim rule provides that an operating cost assistance reserve may be funded upfront for NHTF-assisted units for the amount estimated to ensure a project's feasibility for the entire affordability period. If this amount would exceed the 33% operating cost assistance cap, it could be funded in phases from future non-appropriated NHTF grants. This provision will be very helpful for development of rental homes at rents that ELI households can afford.

TERM OF AFFORDABILITY

NLIHC urged that the final rule adopt a 50-year affordability period, with preferences for projects that have longer affordability periods. The interim rule retains the proposed rule's minimum of 30 years, allowing states to impose longer periods.

RENT SETTING

NLIHC urged that the final regulations use the Brooke rule, limiting an assisted household's rent payments to 30% of their adjusted household income. The proposed rule set maximum tenant rent plus utility payments at the greater of 30% of the federal poverty line or 30% of a hypothetical family whose annual income equals 30% of AMI. The preamble to the proposed rule acknowledged that with the proposed fixed rent maximums, some assisted households would be rent-burdened, paying more than 30% of their income for rent and utilities, However, fixed rent maximums would be necessary for project financial underwriting purposes. The interim rule does not adopt the Brooke rule.

PERMANENT HOUSING

The proposed rule would allow NHTF funds to be used for transitional housing. NLIHC urged that NHTF not be allowed to be used for transitional housing because the statute declared that NHTF's purpose is to increase and preserve the supply of rental housing for ELI households, strongly implying that permanent housing is the goal. HUD agrees and transitional housing is no longer an eligible housing type in the interim rule.

ADMINISTRATIVE COSTS

The preambles to both the proposed rule and the interim rule indicate that only 80% of a state's NHTF allocation must be used for rental housing because up to 10% may be used for homeowner activities and up to 10% may be used for a state's administration and planning costs. NLIHC's comments to the proposed rule asserted that the statute implicitly requires 90% of a state's NHTF allocation be used to benefit renter households because it limits homeowner activities to 10%. HUD did not agree.

PUBLIC HOUSING

The statute and proposed rule defined "recipients" of NHTF dollars to be organizations, agencies, or other entities (including nonprofits and for-profits) that receive funds from grantees (states) to carry out NHTF development projects. The definition did not include public housing agencies (PHAs). NLIHC suggested that the rule specifically include PHAs so that PHAs could use NHTF for non-public housing developments. In the preamble to the interim rule, HUD asserts that PHAs are already eligible entities and the interim rule adds PHAs to the list of potential NHTF recipients.

The proposed rule explicitly prohibited the use of NHTF resources for public housing. NLIHC commended HUD for taking that position, commenting that using NHTF to rehabilitate or operate public housing units would not increase housing opportunities for ELI households and could result in an overall loss of resources for housing if Congress reduced appropriated resources for public housing due to the availability of NHTF resources.

The interim rule will allow NHTF use for two categories of public housing:

1. RAD. NHTF funds can be used to rehabilitate existing public housing units that are converted under the Rental Assistance Demonstration (RAD) to project-based rental assistance. Currently up to 185,000 public housing units may be converted under RAD, and HUD continues to seek Congressional approval to allow all public housing units to be converted.
2. CNI and LIHTC. NHTF resources may be used to rehabilitate or build new public housing as part of the Choice Neighborhoods Initiative (CNI) or to rehabilitate or build new public housing units that have been allocated and will receive Low Income Housing Tax Credit assistance. Public housing units constructed with NHTF must replace public housing units removed as part of an CNI grant or as part of a mixed-finance development under Section 35 of the Housing Act of 1937. The number of replacement units cannot be more than the number of units removed. Public housing units constructed or rehabilitated with NHTF must receive Public Housing Operating Fund assistance, and may receive Public Housing Capital Fund assistance.

NLIHC is extremely concerned about these new provisions, as they could divert NHTF away from expanding rental housing and be used to simply maintain the public housing stock.. While RAD-converted public housing units are technically no longer "public housing," because they are no longer "ACC" units, part of the PHA's Annual Contributions Contract, the PHA must maintain a controlling interest in them and their financial viability is dependent upon continued appropriations of either sufficient amounts for Project-Based Vouchers or Project-Based Section 8 Rental Assistance.

The intent of the NHTF always has been to expand the supply of rental housing affordable to ELI households. The statute declares that the purpose of the NHTF is "to increase and preserve the supply," and thus sanctions preservation of affordable housing. However, the primary purpose of the NHTF is to increase the supply in order to close the gap in rental housing units both affordable and available to ELI households – a gap that is currently at 7.1 million units. The intent with respect to preservation was to preserve affordable units privately owned and operated, units that had been leaving and continue to leave the affordable housing stock as private owners opt out of Section 8 contracts or as their 40-year HUD-assisted mortgages mature.

The Interim NHTF rule is at http://www.gpo.gov/fdsys/pkg/FR-2015-01-30/pdf/2015-01642.pdf

NLIHC's comments regarding the October 29, 2010 proposed rule are at http://nlihc.org/sites/default/files/NLIHC_Comments_NHTF_Proposed_Rule_1.pdf

The National Housing Trust Fund
c/o The National Low Income Housing Coalition
727 15th Street, NW • Suite 600 • Washington, DC 20005
202-662-1530 • www.nlihc.org/issues/nhtf

NATIONAL LOW INCOME HOUSING COALITION