NATIONAL HOUSING TRUST

August 12, 2022

Ms. Marcea Barringer

Federal Housing Finance Agency

400 7th St SW

Washington, D.C. 20024

RE: Freddie Mac & Fannie Mae 2022-2024 Duty To Serve

Dear Ms. Barringer:

On behalf of National Housing Trust (NHT), thank you for the opportunity to provide comments on Fannie Mae and Freddie Mac's (together, "the Enterprises") 2022-2024 Duty to Serve (DTS) plans. **We are writing to urge the Federal Housing Finance Agency (FHFA) and the Enterprises to preserve the affordability of existing and future Low-Income Housing Tax Credit (Housing Credit) properties by upholding the Right of First Refusal (ROFR) and limiting the use of Qualified Contracts (QC).**

At NHT, we equip communities for a sustainable, equitable future by preserving and modernizing existing homes—and building new homes that stand the test of time. Our team of passionate experts and advocates brings resident services, lending, policy, sustainability, and development under one roof, giving us the tools to make real change possible for the people we serve. We believe in the power of learning and creating with the communities around us. That's why for over 30 years, we've partnered with residents, local experts, and national leaders to find the solutions that work. As both a mission-driven affordable housing developer and a respected policy advocate, we are well-positioned to help FHFA and the Enterprises support the long-term preservation of existing affordable housing so that everyone -- everywhere -- can be proud of where they live.

In previous years, NHT has provided detailed comments on FHFA's Duty to Serve proposed rule and the Enterprises' Underserved Market Plans. The following comments are in response to select questions of interest that were provided ahead of the July 11, 2022 DTS listening session on Affordable Housing Preservation, and limited to issues related to the nonprofit Right of First Refusal.

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NHT recommends both Enterprises to adopt language and practices that protect both existing and new Housing Credit properties by:

1. Identifying Housing Credit properties approaching Year 15;
2. Providing technical assistance to nonprofits;
3. Adopting stricter investor eligibility; and
4. Expanding language in Partnership Agreements to include:
    - Protective language that clarifies that the nonprofit ROFR;
    - Clear actions that trigger the ROFR;
    - Clear calculation of the ROFR purchase price; and
    - a Letter of Intent to vet investor eligibility.

NHT's recommendations, as discussed in greater detail on page 5, are informed by the impacts of disputes to the nonprofit partner's ROFR in addition to the investor tactics systematically challenging the nonprofit partners' ROFR.

Impacts of Disputes to the Nonprofit Partners' ROFR

As identified in Freddie Mac's DTS, in recent years, outside parties motivated solely by profits have acquired the control of investor partnerships in Housing Credit properties and begun systematically challenging a nonprofit general partner's exercise of the ROFR. These actions have wide-ranging impacts on the low-income residents who call Housing Credit properties home, in addition to nonprofit general partners who are committed to the long-term preservation of affordable housing communities.

For lower-income renters, many of whom face housing instability, housing provided through the Housing Credit program by mission-driven developers provides safe, stable, long-term affordable housing in addition to other supportive services. **Challenges to the nonprofit's right to exercise the ROFR threatens affordable housing and low-income residents by reducing supportive services, deferring much-needed property maintenance, reducing staff capacity, and creating uncertainty on the financial future of the affordable property.**

When mission-driven developers are forced to spend limited reserves on legal feels or to pay the private investor directly to remove them from the partnership, few resources are left to maintain low rents, provide

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wrap-around resident or supportive services, or ensure that the properties are maintained as high-quality housing. In these scenarios, it is the low-income renters who are most hurt. Meanwhile, staff resources are diverted to combat the partnership dispute rather than providing housing services. In some instances, mission-driven owners may be forced to sell the property. As a mission-driven nonprofit, NHT not only invests in the physical housing but also in supportive services, education/training programs, and partnerships with other local organizations that benefit community members outside of our own properties. When resources are depleted paying legal fees associated with transfer disputes, these services are the among the first to be cut.

In addition to being detrimental to low-income renters and the financial stability of an individual affordable housing community, the systematic challenges of the ROFR also affects the financial viability of a nonprofit general partner. While a ROFR dispute with an investor is taking place (sometimes over a number of months or years due to protracted negotiations or litigation), prudent management of the property is essentially frozen as the investor limits the general partner's ability to secure loans or otherwise raise funds to maintain quality affordable housing. As property reserves erode, a nonprofit partner experiences higher levels of debt and hits to their balance sheet. Private, profit-motivated investors know that most nonprofit general partners do not have the resources to litigate ROFR contractual issues in court. While it may seem well-meaning to help a nonprofit avoid expensive litigation, private investors instead ask for a profitable cash payment (essentially a payout) or force the sale of the affordable property in return for leaving the partnership. Depending on the legal fees or payments to be made to the private investor, some owners may have to sell their affordable housing portfolio and exit the affordable housing market altogether, bringing about further housing instability for low-income residents. Further, as real estate prices have soared across the country, these forced sales are reaping hundreds of millions of dollars of profits for investors who exploit the ROFR.[1]

These actions are both detrimental to the affordable housing industry *and* contrary to the original intention of Congress.

[1] *Investors Mine for Profits in Affordable Housing, Leaving Thousands of Tenants At Risk*, WBUR (April 2021). https://www.wbur.org/news/2021/04/29/investors-low-income-housing-boston-south-end

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Investor Tactics for Systematically Challenging the Nonprofit Partners' ROFR

In 1989, Congress amended the Housing Credit program to permit Housing Credit partnership agreements between property owners to give nonprofits a ROFR to obtain full ownership of an affordable housing property after Year 15. **Congress took this action to encourage ownership by nonprofits for the purpose of maintaining rent affordability restrictions into perpetuity.** For most of the program's history, limited investor partners have exited the partnership at the end of the 15-year compliance period, as expected, and allowed the nonprofit general partner to obtain full ownership and continue to maintain the affordable housing in line with their mission.

As outside parties motivated solely by profits acquire control of investor partnerships in Housing Credit properties and begin to systematically challenge nonprofit general partner's exercise of the ROFR, they are taking advantage of the ambiguity that exists in the federal ROFR statute to challenge the ROFR. Limited partners can and have interpreted the ambiguous language in the federal ROFR statute to their benefit, extracting profits from affordable housing communities and precipitating a decline in the quality of housing for low-income families and individuals. Since 2016, there have been at least 47 instances of litigation on Year 15 / ROFR disputes across the country.[2] Some tactics typically used to disrupt the free exercise of the nonprofit ROFR include:

- Taking the position that the Section 42(i)(7) ROFR is the same as a common law right-of-first-refusal, including in the calculation of the ROFR purchase price and a bonafide third party offer;
  - A ROFR is not unique to the Housing Credit program and is often used in common real estate transactions, when afforded by a local ordinance. In these instances, the purchase price is calculated by the market. The ROFR in the Housing Credit program differs in that the price is set by the federal statute, not market price. This clearly establishes it as separate from the common law ROFR, with the statute identifying the ROFR purchase price as the sum of the property's outstanding debt plus taxes, yet disputes over the ROFR purchase price still occur.
  - Similarly, limited partners state that they are not required to recognize the rights established in the partnership agreement without a bonafide offer from an unrelated third party. As clearly

[2] *LIHTC Court Rulings*, Novogradac (2022). https://www.novoco.com/resource-centers/affordable-housing-tax-credits/lihtc-court-rulings#rofr; in addition to written information provided by BC Davenport.

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stated in Section 42(i)(7), a nonprofit partner holds the right to purchase the building through a ROFR after the close of the building's 15 year compliance period thereby negating any serious or "bonafide" offer to purchase by a third party.

- Disputing the conditions and scope of transfer rights;
- Delaying, obstructing, and disagreeing with related valuations;
- Refusing consent to refinance, either outright or by placing significant conditions on consent;
- Disputing fee calculations;
- Arguing over typographical errors;
- Asserting alleged breaches of partnership duties from many years prior, including by arguing that rents should have been set higher to maximize profits; and
- Alleging breach of fiduciary duty by the nonprofit general partner.

NHT Recommendations to the Enterprises to Strengthen Nonprofits' ROFR

In light of these conditions, we are glad to see Freddie Mac's intent to better support non-profit ownership at the end of the Housing Credit compliance period and the inclusion of language in partnership agreements that protects nonprofits' ROFR. NHT agrees that it will largely only affect new transactions.

To best address the growing problem, we urge both Enterprises to adopt language and practices that protects both existing and new Housing Credit properties. The following policy and programmatic recommendations were developed in partnership with state and local Housing Credit allocating agencies from across the country.

For existing properties, NHT recommends that the Enterprises:

1) Support early intervention to identify properties approaching Year 15. This should include but not be limited to encouraging Housing Finance Agencies, in collaboration with nonprofit developers and advocates, to identify Housing Credit properties between years 10 - 14 and whose ownership partnership includes certain profit-motivated private investors.

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2) Provide technical assistance to nonprofits. This should include reviewing partnership agreement language to ensure that nonprofits are aware of and better understand their rights and ability to exercise ROFR; creating a checklist for review ahead of a property reaching Year 15 of how to prepare to exercise and execute the ROFR; and providing support and resources if a dispute arises.

3) Adopt stricter investor eligibility. If equity providers who have actively sought to interfere with or defeat a ROFR face regulatory sanctions impeding their ability to do new business with a state or the Enterprises, this should cause them to consider modifying their practices with respect to existing properties. Therefore Enterprises should cease to conduct business with entities that have challenged a nonprofits right to exercise the ROFR in any state or jurisdiction within the United states.

For future partnership agreements, NHT recommends that the Enterprises:

1) Strengthen protections through language that makes clear that the nonprofit ROFR cannot be conditioned upon receipt of a bona fide offer from any party, including a third party. This should include clarification that the ROFR outlined in Section 42(i)(7) is not the same as a right of first refusal under statutory, court-interpreted, or common law.

2) Incorporate language that provides the general partner or managing member, on behalf of the partnerships/company after the end of the compliance period, the power and authority, without the need to obtain the consent of the investor, to take any actions that could trigger and accept the nonprofit's right to purchase under the ROFR and to close on the sale of the property to the nonprofit.

3) Clarify that the ROFR purchase price is calculated as the minimum purchase price permissible under Section 42. This ROFR Purchase Price should not automatically include unpaid fees or loans and should be calculated by the project accountants and deemed final other than due to manifest error.

- This is important because it is a common tactic of recalcitrant investors to object to the calculation of the ROFR price as a means of stalling consummation of the ROFR and leveraging a payment by the general partner. The amended language would preserve that right while

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removing a point of investor leverage to object to the accountant's calculation of the ROFR Purchase Price.

4) Require a Letter of Intent to vet investor eligibility that includes written acknowledgement by potential investors or syndicators at the beginning of a Housing Credit partnership that they have never sought to achieve early termination of a Housing Credit extended use agreement through the qualified contract process, nor have they sought to undermine the exercise of the nonprofit ROFR.

To date, eight allocating agencies[3] have adopted language like that outlined above to ensure nonprofits can exercise the ROFR to protect long-term affordability, and we encourage the Enterprises to do the same. NHT has closely supported Virginia Housing in developing a specific ROFR agreement and New York City Housing Preservation and Development to require a Letter of Intent (LOI) from a qualified equity provider that must include eight listed features that protect the interests of the nonprofit ROFR grantee. The remaining six allocating agencies have included varied clarifying language in their QAPs or other policy documents.

In addition, NHT would also like to acknowledge our long-standing support of policies and actions taken to limit the loss of affordable housing through the qualified contract (QC) process. In the July 11th listening session, the National Council of State Housing Agencies (NCSHA) noted that, as of the end of calendar year 2021, more than 100,000 Housing Credit homes had already been lost from the affordable housing inventory because of QC.

We support NCSHA's recommendations and encourage Fannie Mae and Freddie Mac to set policies of investing only in properties in which the owners have waived the right to a qualified contract, consider preservation concerns such as qualified contracts as part of the criteria used to determine which loans to purchase, and assist preservation-oriented buyers willing to make an offer to purchase a property at the qualified contract price.

[3] These specific allocating agencies are: District of Columbia Department of Housing and Community Development, Indiana Housing and Community Development Authority, Massachusetts Department of Housing and Community Development, New York City Housing Preservation and Development, Oregon Housing and Community Services, Pennsylvania Housing Finance Agency, Virginia Housing and Washington State Housing Finance Corporation.

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NHT encourages the Enterprises to recognize in writing both qualified contracts and challenges to the nonprofit ROFR in their respective DTS plans to demonstrate a commitment to the long-term preservation of existing affordable housing. We would also encourage Fannie Mae and all investor partners of both Enterprises to adopt the language that Freddie Mac has developed, in addition to our recommended suggestions, in partnership agreements involving nonprofit general partners. We believe that the Enterprises can play an important role in protecting the long term affordability of these properties by limiting the availability of qualified contracts and strengthening the nonprofit ROFR.

Finally, NHT acknowledges that the ultimate cure to both QC and ROFR challenges is federal legislation that closes the QC loophole and affirms a nonprofit ROFR. Such legislation has been drafted and was included in the 2021 Build Back Better Act, but has yet to gain the broad support necessary for passage. Support from FHFA and the Enterprises would help in highlighting these critical issues to Congress.

Thank you for the opportunity to share our expertise.

Sincerely,

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