

April 10, 2006

Federal Housing Finance Board
Attention: Public Comments
1625 Eye Street, NW
Washington, DC 20006

Re: 12 CFR Part 951
Affordable Housing Program Amendments

Greetings:

The Federal Home Loan Bank of San Francisco (Bank) appreciates the opportunity to comment on the Proposed Rule published by the Federal Housing Finance Board in the Federal Register on December 28, 2005, proposing amendment to the Affordable Housing Program regulations at 12 CFR Part 951. The Bank strongly supports the efforts by the Finance Board to improve the efficacy of the AHP, as evidenced in this set of proposed revisions, and offers the following comments for your consideration.

Section 951.1 Definitions

- We support the expanded authority to define the term “sponsor” by the level of ownership interest and the inclusion of sponsors of loan pools and revolving loan funds.
- With regard to the terms “low- or moderate-income household” and “very low-income household,” we request greater specificity on how to use HUD statistics to calculate a family-adjusted income level, pursuant to the Bank’s regulatory interpretation request dated August 19, 2005, which we incorporate herein by reference.

Section 951.2 Required Annual AHP Contributions; Allocation of Contributions

- We support elimination of the acceleration authority (i.e., an FHLBank’s ability to borrow from future years to fund current competitive and set-aside rounds). We agree that acceleration is operationally difficult.
- We support the consolidation of separate program authorities under the set-aside programs.
- With regard to the proposed requirement that at least one-third of an FHLBank’s homeownership set-aside allocation be for first-time homebuyers, the Bank suggests that the Finance Board promulgate one or more first-time homebuyer definitions that would be acceptable for use in either the competitive or set-aside programs.

Section 951.3 AHP Implementation Plan

- The Bank offers the following comments on the proposed requirement to include “retention agreement requirements” in an FHLBank’s Implementation Plan:

The term “retention agreement requirement” is broad and may be interpreted in many different ways, and the Finance Board might not concur that all of these interpretations are appropriate. The Finance Board could clarify its intent or objectives in the preamble. The regulation should explicitly state the elements that the retention agreement is expected to cover.

With respect to loan pools, the Bank strongly supports the proposal to eliminate the 5-year retention agreement requirement for owner-occupied units assisted with subsidized advances (proposed section 951.5(c)(14)(iii)), recognizing that such retention agreements are unnecessary given that the homeowner receives subsidy in increments throughout the term of the advance. The Bank strongly supports the policy behind this change and urges the Finance Board to extend the same treatment to owner-occupied units assisted with a permanent mortgage loan whose interest rate is subsidized with AHP direct subsidy. (See additional comments relating to Section 951.9 Retention Agreements on p. 7 of this comment letter.)

Section 951.4 Advisory Councils

- The Bank supports moving the due date of the AHAC Annual Report from March 1 to May 1.

Section 951.5 Competitive Application Program

- The preamble indicates that the proposed provisions on feasibility and need-for-subsidy analysis will eliminate the need for RI 1999-03, which, in addition to the authority cited, has also allowed FHLBanks to present-value deeply discounted mortgage financing provided to homebuyers by the sponsor. This provision in the RI has enabled the Bank to approve funding for projects such as various Habitat for Humanity projects, which use deeply discounted mortgage financing. If the Finance Board eliminates the authority to present value such financing for purposes of evaluating the project’s sources and uses of funds, then the development budgets for these projects (including many Habitat for Humanity projects and other projects similarly financed) would indicate cash sources of funds in excess of cash uses, and would therefore be disqualified from receiving AHP subsidy. The Bank requests that the final rule explicitly allow FHLBanks to present-value deeply discounted financing provided by the sponsor in the determination of sources of funds to preserve the eligibility of these projects.

- We offer the following comments with regard to the use of AHP subsidy by revolving loan funds or loan pools:

Section 951.5(c)(14)(ii) of the proposed regulation requires the loan pool sponsor to purchase loans pursuant to a forward commitment and subject to the time limits on use of subsidy in the FHLBank’s AHP Implementation Plan.¹ We assume that the Finance Board means that this time period should begin to run from the time the forward commitment is issued (and should be specifically addressed in the AHP Implementation Plan). For

¹ This time limit also takes effect when loans are not purchased pursuant to a forward commitment, in which case it applies to the originator or holder of the loans. The Bank requests additional clarification from the Finance Board to expressly indicate when such time period begins to run.

example, the AHP Implementation Plan could provide an overall 4-year time limit on use of subsidy from the time the award is made, and an additional time limit specifying that a loan must be purchased within 3 years from the date of the forward commitment (or such other time period as long as it is within the overall limit specified in the FHLBank's Implementation Plan). If this is not what the Finance Board meant, we request clarification and greater specificity in the regulation.

The Finance Board has specifically requested comments on whether it should adopt a fixed regulatory time limit instead of the flexible approach specified in the proposed regulation. The Bank strongly supports the flexible approach taken in the proposed regulation of establishing the applicable time limit in each FHLBank's AHP Implementation Plan, thereby giving each FHLBank the ability to adopt limits that more closely reflect the funding needs applicable to the types of loan pool structures in place in their districts.

The Bank believes that the proposed language on loan pools in subsection 951.5(c)(14) is generally acceptable as drafted. As a point of clarification, the language in the preamble explaining this subsection refers to the time limit test as "the length of time a project sponsor would have, as specified in the forward commitment, to expend the full amount of the AHP subsidy." In a loan pool project where the subsidy is being distributed to the ultimate beneficiary (the homeowner) through a below-market interest rate loan, we assume that the subsidy can be distributed through a traditional fixed rate loan (where the borrower receives the benefit over the entire 30-year term if the borrower chooses not to prepay the loan); otherwise, a literal interpretation of the preamble language might mean that the awarded subsidy would have to be fully applied against the interest rate within the permissible time limit, resulting in a deeper interest-rate discount on the loan up front, but only for the number of years specified in the AHP Implementation Plan for initial disbursement of subsidy. Such an interpretation would in effect mandate the creation of a teaser rate product that had a very low rate for 4 years, based on the example above, and a market rate after that. We do not believe that is the intent of the Finance Board's proposal.

- We support allowing each FHLBank to implement variable-point scoring criteria either on a fixed scale or on a scale relative to the other applications that are to be scored in the same funding round. More flexibility for each FHLBank to design its own scoring methodology ensures that it can effectively meet the housing needs in its particular district.
- We support the increased flexibility in the requirements for monitoring progress towards use of AHP subsidies.
- We support the greater flexibility given to the FHLBanks in determining when it's necessary to re-verify compliance with eligibility requirements and application requirements.
- The Bank requests that the Finance Board collapse the two existing District Priorities – first and second – into one District Priority to be established at the discretion of each FHLBank. The consolidated priority could consist of one or more categories and projects could earn points in each category. We believe that this flexibility will enable FHLBanks to tailor their programs to under-addressed needs in their districts or in other areas served by their members.
- The Bank requests that the Finance Board revise the scoring criterion "Empowerment of the Poor" to expressly permit FHLBanks to give scoring credit for activities or services that help individuals stabilize or improve their economic *or personal* well-being. FHLBanks should be permitted to give scoring credit for a variety of supportive social, vocational, and technical services or programs such as, but not limited to, job training, long-term adult day

care, child day care, after-school youth activities, transportation, parenting skill training, chemical abuse counseling/treatment, credit and mortgage counseling, home maintenance/repair training, tenant assistance, homeownership/homebuyer counseling, resident involvement in planning and direct resident input into the operations of an AHP project. We believe supportive services that enhance or empower an individual's personal well-being can contribute directly to the likelihood of project success, as well as to the individual's chances of gaining greater financial self-sufficiency.

Section 951.6 Homeownership Set-Aside Programs

- With regard to the statement in the proposed rule that time of determination of income eligibility is at the time of enrollment by the member *and the FHLBank* in the AHP set-aside program, we support adding clarifying language stating that the member enrolls prospective homebuyers in the FHLBank's set-aside program and determines income eligibility at that time in accordance with the PMSA/MSA of the then-current residence of the prospective homebuyer at the time of enrollment. The Bank's current IDEA and WISH enrollment form is signed by the member and the homebuyer. The Bank receives and reviews the enrollment form at the time the member requests reimbursement of funds from the Bank. We support the proposed requirement provided that it is made clear that the Bank is not required to receive and review any enrollment forms at the time the member initially enrolls a participant in the program, but instead the Bank may obtain the enrollment form at the time the member requests reimbursement from the Bank. We would not support this provision if it requires the Bank to receive the enrollment form at the time that the member enrolls the homebuyer in the Bank's program.
- The preamble states the Finance Board's expectation that the FHLBanks' income-qualification policies "preclude use of the program by individuals whose low- or moderate-income eligibility is a temporary condition, such as students who would ordinarily have a reasonable prospect for a substantial increase in income upon entering the workforce." We do not support the policy rationale behind this proposed restraint on the use of AHP subsidy as it appears arbitrary on its face, is extremely difficult to measure and define, and makes generalized presumptions about future events that may or may not occur. For example, depending on their chosen field of work and location, graduating students could very likely remain eligible at less than or equal to 80% AMI following graduation. Also, the program does not apply a similar check on changes in income for other AHP subsidy recipients, nor should it. In view of this, the Bank strongly urges the Finance Board to eliminate this stated expectation with regard to income-qualification policies from the preamble. If this expectation remains, then the regulation should include workable and clear standards for the FHLBanks to follow in implementing such a standard in its policies.
- The Finance Board specifically requests comments on the financial incentives requirement with respect to the homeownership set-aside programs:
 - 1) Should the regulation require all originators of AHP mortgage loans to provide financial or other incentives in connection with the mortgage financing irrespective of whether the originator is a member or non-member?

No, the Bank does not support extending the financial incentive requirement to nonmembers, and we believe further that the member financial incentive should be made discretionary (see below). This would achieve the same policy objective of leveling the playing field. If third-party mortgagees were required under the program to provide financial incentives to the subsidy recipients, the sponsoring member, who is passing through the set-aside subsidy, would then need to monitor the mortgagee and its incentives for adherence to the Bank's

guidelines. The Bank does not support placing members in the position of monitoring, or of being responsible for, the behavior of other lenders. That would be a disincentive for members to participate in the program.

- 2) Should the current financial incentive requirement remain as mandatory or be made a matter of discretion for the Bank as a preferential selection criterion for its homeownership set-aside program?

It should be made a matter of discretion for the FHLBank, or eliminated.

- 3) Should additional incentives be required such as matching funds requirements, member-provided financing or preference to a member working in partnership with a nonprofit sponsor assisting first-time homebuyers to qualify for a mortgage?

No, the Bank does not support the requirement of additional incentives. We believe the local needs can be best met by allowing each FHLBank as much flexibility as possible in designing its set-aside programs to include whatever incentives the FHLBank determines, after consultation with its Advisory Council, best meet the objectives of its program.

- The Bank supports the provision requiring that “progress shall be made towards draw-down and use of the AHP direct subsidies by eligible households” as long as this refers to the member’s progress towards use of its set-aside allocation.
- The Bank recommends, with regard to “eligible uses of AHP direct subsidy,” that manufactured housing be added as a type of owner-occupied unit, in addition to condominiums and cooperative housing units.
- The Bank requests, with regard to the “no cash back to household” provision, that the Finance Board clarify that, in addition to the member, *the homebuyer* can apply cash back toward the payment of the principal of the mortgage loan or reasonable closing costs *that do not appear in the settlement statement*. In a similar vein, the Bank requests that the proposed rule clarify that repayment of consumer debt, through the loan closing process, that appears on the settlement statement would not be considered “cash back” if it occurs pursuant to satisfying a condition of loan approval imposed by the mortgage lender and if the homebuyer’s own funds are applied toward such payment.

Section 951.7 Monitoring

- We strongly support replacement of the current long-term monitoring provisions with a risk-based scheme.
- We do not support retaining the project owner certification requirement from the existing regulation as part of long-term monitoring. Since the institution of this provision in 1998, our experience has been that this is a paper- and labor-intensive process with little or no positive influence on the long-term compliance of a project. The Bank believes that the program goals would be better served by focusing efforts on the proposed risk-based long-term monitoring requirements, which should adequately address compliance over the 15-year retention period and, at the same time, streamline management of the program.
- We support deletion of the word “habitability.”

- We support replacement of the one year and 120 day timeframe for completion of initial monitoring with a “reasonable” timeframe, as this will streamline management of the program.
- With respect to the proposed provision that FHLBanks must review back-up documentation regarding household income and rents at initial monitoring, the Bank strongly urges the Finance Board to allow the FHLBanks to fulfill this requirement through a review of a sample of the units in each project. To require review of back-up documentation on income eligibility for every homebuyer or renter would add enormously to the administrative burden and cost of monitoring and thus run counter to the Finance Board’s goal of streamlining the program.
- The proposed regulation and accompanying explanation in the preamble give FHLBanks expanded authority to rely on other monitoring entities, such as tax credit agencies, as long as those agencies monitor projects to the minimum AHP eligibility standard, which is that at least 20% of the units are targeted to very low-income households (referred to in the preamble as “substantively equivalent”). While we strongly support reliance on other agencies to fulfill long-term monitoring requirements, we oppose holding rental projects that do not fit the criteria for monitoring by another entity to stricter requirements – that is, to the income targeting commitments made in the original application. We urge the Finance Board to extend the same “substantively equivalent” income-targeting standard to all rental projects.
- The proposed regulation would require the FHLBanks to review “back-up documentation” as part of long-term monitoring. Proposed section 951.7 (a)(2)(ii)(C) states that “a Bank may use a reasonable risk-based sampling plan to select the rental projects to be monitored, and to review the back-up documentation received by the Bank.” The Bank requests that the Finance Board clarify that the FHLBanks would not be required to collect back-up documentation on every unit in each project being monitored, but may instead allow the FHLBanks to collect documentation only for the units selected pursuant to the sampling plan utilized. To require the FHLBanks to gather documentation that would not be subject to review would result in unnecessary administrative burden and cost for program participants as well as for the FHLBank. This provision in its current form would run counter to the Finance Board’s goal of streamlining the program.
- The proposed regulation would require FHLBanks to include “populations served” in their policies and procedures for long-term monitoring. We strongly urge the Finance Board not to increase the scope of long-term monitoring, which under the current regulation is limited to a review of “tenant rents and incomes for compliance with income targeting commitments made in the original AHP application.” If it is the Finance Board’s intent to increase the scope of long-term monitoring by including “populations served” in the review, we request that the Finance Board define the term, and clarify its expectations.
- Although we strongly favor a less prescriptive approach to monitoring in the competitive program, we believe that this section of the proposed regulation, as drafted, leaves substantial questions open to possible misinterpretation, and therefore, we do not support the changes as proposed. We urge the Finance Board to address the following issues in the final rule:
 - The rule does not make clear what type, or frequency, of report from another monitoring entity would satisfy the requirement under long-term monitoring. The Bank requests that this reporting requirement be eliminated.
 - The rule does not make clear whether the other monitoring entity would be required to monitor for “populations served.” The Bank requests that this element be removed from the long-term monitoring requirements.

- The proposed rule does not make clear whether the FHLBanks can apply a risk-based sampling plan on projects subject to monitoring by another monitoring entity. The Bank requests that the Finance Board either expressly permit the FHLBanks to sample projects for monitoring, or eliminate the reporting requirement (thus obviating the need to sample).

Section 951.8 Remedial Actions for Non-compliance

- We support the authority for the FHLBanks to recover subsidy directly from project sponsors or owners.
- We support delegation of the authority to approve disputed claims from the Board of Directors of the Finance Board to the Finance Board staff.
- The Bank requests that the amendment include express language reflecting the long-standing policy that an FHLBank is not required to seek repayment of subsidy in circumstances where the estimated cost of attempting to recover the subsidy would exceed the amount of subsidy at issue.

Section 951.9 Agreements

- The Bank requests an additional change in the proposed provisions generally applicable to the retention agreements for owner-occupied units (which are incorporated by reference into the loan pool provisions). The general retention agreement provisions currently provide for repayment of the pro-rata portion of the subsidy payable out of any gains realized upon a sale or refinancing “unless the unit was assisted with a permanent mortgage loan funded by an AHP subsidized advance.”² Proposed section 951.9(a)(7). The Bank believes that public policy would be better served if the language were revised to read “unless the unit was assisted with a permanent mortgage loan funded at a below-market interest rate.” The Bank believes that the ultimate beneficiary’s method of receiving the subsidy, and not the funding vehicle (direct subsidy or subsidized advance), should drive the retention and repayment requirement. The Bank believes that a 5-year retention agreement should always be applicable if the homeowner of an owner-occupied unit receives AHP subsidy in a lump sum payment to cover closing costs and/or a reduction in the loan principal balance (achieved through down payment assistance). On the other hand, if the homeowner receives the subsidy in the form of a below-market interest rate loan, the Bank strongly believes that 1) repayment and retention tools are built-in as “natural” elements of the subsidized mortgage financing when subsidy is used to reduce the interest rate on the loan, and 2) no repayment provision retention agreement is required because the subsidy automatically stops when the below-market interest rate loan is prepaid. Alternatively, if the Finance Board prefers not to alter its general retention agreement provisions as described above, we request that the special loan pool language incorporating such provisions be revised to read as follows:

Each AHP-assisted owner-occupied unit receiving AHP direct subsidy in the form of a lump sum payment to cover either closing costs and/or a reduction in the loan principal balance (achieved through down payment assistance) shall be subject to a standard five-year retention agreement.

- The Bank requests clarification of the intent of the proposed requirement that an FHLBank set forth specific monitoring policies and procedures in its agreements. The Bank suggests that the rule make it clear that the

² The pro-rata part that must be repaid relates to the number of years remaining until the 5-year period expires.

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agreement should make reference to the FHLBank's monitoring policies and procedures. The Bank opposes a requirement to include detailed procedures in the agreement, because they are subject to change during the project's retention period.

- We support the requirement that participants be notified of program requirements and policies, but we are uncertain as to the Finance Board's intent in adding this provision. We would support a provision requiring a formal education process for program participants as a condition of their receipt of subsidy, but not inclusion of detailed procedures in the agreement.
- The Bank finds problematic the new provision related to the sale or refinancing of a rental project prior to the end of the retention period, where subsidy does not have to be repaid as long as households are relocated to "another property made subject to the terms of the approved AHP application as well as a deed restriction." The Bank believes that while this provision is intended to create more flexibility in the program, it will create uncertainty and potential inconsistency in the monitoring process if the relocated project has different characteristics than those of the originally approved application. Therefore, without additional clarification, or relief from its obligation to monitor, the Bank is reluctant to support this provision.
- To enable use of AHP subsidy on Native American lands or other restricted-use properties, we would support provisions to allow FHLBanks more flexibility in determining legally enforceable retention mechanisms. We would suggest amending the regulation to allow substitution of loans within a pool or other alternatives to meet the requirements of a legally enforceable retention mechanism where standard mechanisms, e.g., deeds of trust or liens, are impractical for an efficient operation of an otherwise deserving affordable housing initiative.

Thank you for this opportunity to comment on the proposed changes to the regulation. The Bank strongly supports the efforts of the Finance Board and its staff to increase the efficacy of the AHP. Notwithstanding the Bank's specific comments indicating improvements in the proposed regulation that the Bank believes are desirable, the Bank supports the overall thrust of this proposed regulation and commends the Finance Board and its staff for undertaking this effort.

Sincerely,



Dean Schultz,
President and Chief Executive Officer