TESTIMONY OF CHRIS POTTERPIN, PRESIDENT
COUNCIL FOR AFFORDABLE AND RURAL HOUSING (CARH)

"PERSISTENT POVERTY IN AMERICA: ADDRESSING CHRONIC DISINVESTMENT IN COLONIAS, THE U.S. TERRITORIES AND THE SOUTHERN BLACK BELT"

SUBCOMMITTEE ON HOUSING, COMMUNITY DEVELOPMENT AND INSURANCE
COMMITTEE ON FINANCIAL SERVICES

UNITED STATES HOUSE OF REPRESENTATIVES

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Chairwoman Waters, Ranking Member Hill, and members of the Committee, on behalf of the Council for Affordable and Rural Housing (CARH), we would like to submit written testimony in support of efforts to address chronic disinvestment in the Colonias, the Southern Black Belt and the U.S. Territories. CARH focuses on housing investment and providing affordable housing and that will be the focus of my testimony.

CARH is an industry trade association with headquarters in Alexandria, Virginia, representing the interests of for-profit and non-profit builders, developers, management companies, and owners, as well as financial entities and suppliers of goods and services to the affordable rental housing industry in rural America. My company, PK Companies, based in Okemos, Michigan develops, manages, and owns thousands of affordable housing units across the country. I am also the current President of CARH.

Affordable Rural Rental Housing Is A Necessity

Throughout, the Colonias, the U.S. Territories, and the Southern Black Belt, and other rural areas throughout the country, there continues to be an overwhelming need for both affordable and decent housing. The lack of affordable housing reflects the lack of investment in these localities more broadly. Rural renters are more than twice as likely to live in substandard housing compared to people who own their own homes. With lower median incomes and higher poverty rates than homeowners, many renters are simply unable to find decent housing that is also affordable. While the demand for rental housing in rural areas remains high, the supply, particularly of new housing, has decreased. The adverse effects of housing instability on the education and health of this country's greatest asset, our children, has been well documented. Neither the private nor the public sector can produce affordable rural housing independently of the other; it needs to be a partnership. There are several areas within the rural housing arena that Congress and the Administration should urgently consider as discussions continue on the infrastructure needs of rural communities. And, as our colleagues and CARH member, the Housing Assistance Council (HAC) has researched, these issues are even more acute in the Colonias, the Southern Black Belt

and the U.S. Territories. For example, we note HAC's Rental Housing for a 21st Century Rural America at https://ruralhome.org/reports/rural-america-is-losing-its-affordable-rental-housing/ .

Key Tools - Rural Development Rental Housing Programs and the Housing Credit Program

The United States Department of Agriculture's (USDA)/Rural Development (RD) Section 515 rural multifamily housing and Section 514 farm labor multifamily properties are a lynchpin for addressing affordable rural housing needs—both through preservation of those diminishing portfolios and through the need for new production funding and investment. Rental assistance under the Section 521 Rental Assistance (RA) program is essential for many family and elderly households residing in rural America. At the same time, most federally supported multifamily properties are 35+ years old and need modernization. These properties have suffered from federal funding shortages and statutory and regulatory barriers that make recapitalization either difficult or impossible.

Rural housing development and investment is largely dependent on only a few sources of funding for construction and preservation of the existing housing stock. The Low-Income Housing Tax Credit (Housing Credit) program is certainly a vital source for this important housing. The Housing Credit program has worked successfully since its creation in 1986. It helps to bridge the gap between what the market provides and what the market demands. In short, America's elderly, working families, civil servants, and working poor seek to live in or near their jobs, families, and communities. In much of rural America, this need cannot be met due to the lack of affordable housing options. Homeownership is often either out of reach or not financially viable. Furthermore, the cost of providing any new housing or rehabilitating existing housing to current standards without public-private assistance results in rents or other homeownership costs that are simply too expensive for most low-income Americans. In contrast, the Housing Credit program allows non-profit and for-profit companies to work together with local and state governments to raise private equity and to help bridge the financial gap. In turn, the savings are passed on to the residents in the form of lower rents and affordable rental housing. Approximately 43% of Section 515 properties are financed with Housing Credits.

Already Losing Valuable Affordable Housing

The existing rural multifamily programs were never intended as a one-time capitalization for low-income housing. The original intent was to allow properties to refinance out of the program and provide a market centric nucleus of decent housing in rural areas. In fact, USDA originally required owners to refinance out of the program at the first opportunity. However, the federal government changed the laws, rules, and basic operations when it changed the federal tax code, withdrew prepayment rights, and reduced Section 515 funding without any replacement mechanism.

In order to save the Section 515 program and its sister Section 514 farm labor housing program, RD's current demonstration efforts have shown preservation can be successful but the number of properties able to be preserved with current resources will nowhere near achieve portfolio-wide preservation in any reasonable time period.

The Section 514 and 515 portfolios are by and large more than 30 years old and at risk of becoming obsolete. In 2002, RD estimated that 4,250 Section 515 properties with 85,000 units "will physically deteriorate to the point of being unsafe or unsanitary within the next 5 years." At that time, RD estimated it would need $850 million to maintain just this portion of the portfolio, and that as much as $3.2 billion will be required for portfolio-wide rehabilitation. Overall, little progress has been made since 2002. Adjusted for inflation and continued obsolescence, the 2002 $3.2 billion estimate is now approximately $5.6 billion, and growing each year that aging assets are not rehabilitated. In 2016, RD contracted for its own updated capital needs study, which confirmed the existence of significant and continued deferred maintenance. At this current rate of affordable housing properties exiting the program, we encourage the prioritization of the preservation of existing properties ahead of new construction, as it is much more cost effective to complete a substantial rehabilitation compared to the cost of building new.

Maturing mortgages have overtaken prepayments as the most pressing issue. According to RD, approximately 77 properties with 1,759 units are maturing out of the mortgage programs over the next 18-24 months, and that number will only significantly increase past 2027. When a 514/515 mortgage ends, whether through prepayment or foreclosure or maturity, the Section 521 RA also ends, exposing below-market residents to market rents and turning assisted properties into market-rate properties. In 300 counties, Section 515 properties are the majority of project-based federally subsidized units and 90% of all Section 515 properties are in counties with persistent poverty.

Recommended Approaches to Help with Recapitalization and Preservation

CARH has several legislative recommendations that, working with RD and Congress, will help expand tools available to RD in preserving this much needed and at-risk housing.

Rental Assistance—An Essential Program

The Section 521 Rental Assistance (RA) program is an essential component of the Section 514/515 programs. RA provides deep subsidy to very low-income residents by paying the difference between 30 percent of a resident's income and the basic rent required to operate the property, subsidizing 63 percent of Section 515 units. The RA program must continue to provide sufficient funds for both current levels of RA and sufficient additional RA to support increasing program costs. RA budgets have been constrained for the last few years, even before the sequestration issues impacting the program at the end of Fiscal Year (FY) 2013. Historically, RA budgets on a per unit basis are about *half* of other rental subsidy programs. Much of that has been achieved by delaying needed repair and operating funds.

According to RD, the average household income in rural housing properties is $14,665 and the average income of RA households is $12,501. RA is sorely needed for these low-income residents. Indeed, there is more need than there is rental subsidy. Even though most RD properties receive either RA or the U.S. Department of Housing and Urban Development (HUD) subsidy through Section 8, many properties and residents do not. As many as 41,589 families in RD

programs have no rent subsidy, and yet are so extremely low income that RD still considers them to be rent overburdened.

CARH supports full funding of all RA contracts, with specific direction to expend all funds each year. RD should also be instructed to use any funds available after RA renewals and all recaptured RA for affordable housing preservation. The Administration's proposed budget would fund the Section 521 RA program at **$1.602 billion**, an increase from **$1.45 billion** in FY 2022. The **$1.602 billion** funding would be allocated as follows: **$1.564 billion** for existing RA contracts, including the **$100 million** in RA that was added in the American Rescue Plan; **$40 million** that would carry over into FY 2024 (a policy that CARH has supported that ensures that funds are available for RA contracts funded in the first few months of a new fiscal year, should a full year appropriation bill not be completed); **$38 million** for Section 542 rural housing vouchers (moved from the Multifamily Housing Preservation and Revitalization demonstration program account to RA); and **$6 million** for RA that would be available for new Section 515 housing.

Over the next decade, as much as three-quarters of all Section 515 mortgages will mature, and with it the end of related Section 521 RA contracts, stranding approximately 250,000 families and elderly persons and leaving them without the ability to house themselves. Under current law, when a Section 515 mortgage expires, Section 521 RA also expires. There is no budget authority to replace these mortgages. The budget also includes statutory language that will address some of the maturing mortgage issues facing the portfolio in the next several years. The language would provide RD with authority to decouple RA from the Section 515 program, allowing RD to continue offering RA to certain properties that no longer have a Section 515 loan. Currently, with RA tied to the Section 515 loan, in order to protect residents to the maximum extent, owners have to run through the complex processing of RD mortgage loan assumption, even when it makes little financial sense to maintain the Section 515 loan. While decoupling the Section 521 from the Section 515 loan is different than what HUD calls decoupling, it would put the RA contracts on the very logical path to being an important preservation tool. **CARH supports S. 4872, Strategy and Investment in Rural Housing Preservation Act of 2022, that has been introduced by Senators Jeanne Shaheen (D-NH) and Tina Smith (D-MN) that would permit the permanent decoupling of Section 521 RA from the Section 515 loan, thus allowing RA to continue to protect residents and fund affordable housing past the expiration or prepayment of the multifamily mortgage loan. CARH also supports companion legislation H.R. 1728, also entitled Strategy and Investment in Rural Housing Preservation Act, introduced by Representative Cynthia Axne (D-IA).**

Furthermore, the Administration's FY 2023 budget also includes the important concept of decoupling RA but it does not include language that was included in the FY 2022 appropriations that would allow for RA contracts to be 20 years, subject to annual appropriations. CARH has supported this 20-year provision, but thus far RD has not implemented it. RA contracts tend to be less well known to non-Section 538 lenders and to Housing Credit equity providers and the one-year term is often an issue. RD's consistent funding has been a strong due diligence point for lenders and investors. However, it isn't lost on developers that these financing entities price in the costs of risk and due diligence, increasing costs of development, much of which could be solved

with the 20-year subsidy contract like HUD uses. **CARH supports including again language renewing RA contracts for 20 years, subject to annual appropriations**.

A Substantial portion of Section 515 properties also have project-based Section 8 subsidy and residents with tenant-based Section 8 housing choice vouchers. **CARH also supports a strong project-based and tenant-based set of Section 8 programs.**

The Traditional Programs Work—We Need a Preservation RA Designation

The traditional rural rental housing and rent subsidy programs work and work as a program that can attract other forms of public and private assistance. But Congress needs to be clearer and instruct RD to use financing on hand, specifically Section 521 RA for preservation. In past years when Congress specifically provided funding for preservation, RD processed that specific amount. Without that clarity, the last two Administrations have allowed other priorities, including holding on to reserves of RA, to take priority over preservation transactions. While we welcome a greater appropriation of RA, more important than even that is a specific direction to RD to spend all funds on hand each fiscal year.

Continue Efforts to Modernize the Housing Credit

Rural housing construction and preservation projects have access to only a few funding sources. The Housing Credit program is a vital source for this important housing. The Housing Credit program is narrowly targeted and represents the best of the public-private partnership between government, local communities, and the private sector. The program is the most successful affordable rental housing production program and its place in the tax credit code is an essential part of its long-term success. Indeed, the Housing Credit has been so successful that it has become the model for subsequent programs.

Since its inception in 1986, the Housing Credit program has created homes for approximately 2.4 million families. For each 100 apartment units, 116 jobs are created, generating more than $3.3 million in federal, state and local revenue. This important housing resource creates a positive, broad-based economic benefit that includes jobs (particularly construction jobs), income and taxes in industries such as manufacturing, trade, and services, in addition to construction. Income includes business profits as well as wages and salaries paid to workers. Affordable housing not only creates jobs directly, but also facilitates job growth. Affordable housing shortages prevent workers from meeting job demand in rural areas with limited housing options.

Affordable Housing Credit Improvement Act

CARH believes it is critical that both the Housing Credit and Housing Bond programs continue and that legislative proposals to modernize the Housing Credit and Housing Bond programs like the Affordable Housing Credit Improvement Act, H.R. 2573 introduced by Representative Suzan DelBene (D-WA-1) and companion legislation S.1136 introduced by Senator Maria Cantwell (D-WA) should be enacted into law. While we understand that this Committee does not have jurisdiction with tax measures, your support is paramount to further strengthening and expanding the Housing Credit and Housing Bond programs so that rural housing preservation and new

construction can take place. The bills would increase the housing credit authority by 50%, phased in over two years. In addition, states would have the ability to provide up to a 30% basis boost to properties in rural areas if needed for financial feasibility by qualifying rural areas as Difficult Development Areas (DDAs). Both provisions are integral to furthering preservation for the rural housing portfolio.

Community Reinvestment Act

CARH seeks a community development investment test that preserves the importance of participation in the Housing Credit. The Housing Credit's efficacy is at risk today due to two well-meaning changes currently contemplated. One change is the modernization of the Community Reinvestment Act (CRA). There is a general notion in the housing and banking industries that the 1970s-era CRA needs a 21st Century makeover. As fair as that may be, the current proposed changes issued jointly by the banking agencies present certain problems. Large banks are the key purchasers of Housing Credits, and the proposed CRA rules convert the existing three-part test for large banks to a combination of retail and community development tests.

Global Minimum Test

If the 15% global minimum tax were put in place, it would remove a major portion of the value of the Housing Credit. We understand that Treasury Assistant Secretary for Tax Policy Lily Batchelder shared in remarks to the D.C. Bar Association that "...because of the way [general business credits] are structured and accounted for, the income or loss and the income tax consequences of those investments typically will be excluded from the effective tax rate calculation — so those credits generally should not be impacted." This is good news, but it is an informal policy statement only. CARH supports a formal codified position that the Housing Credit, which creates a public benefit of affordable housing, will not be impacted by the Global Minimum Tax.

Preservation of the Existing Multifamily Mortgage Portfolio

The rural multifamily programs were never intended as a one-time capitalization of low-income housing. The original intent was to allow properties to refinance out of the program and provide a market centric nucleus of decent housing in rural areas—indeed USDA originally *required* owners to prepay and leave the program at the first opportunity. The federal government changed the laws after the fact to remove prepayment rights to keep properties in the program but then reduced Section 515 funding without any replacement mechanism that would allow properties to function inside the program long-term.

The Section 515 direct loan program and its one percent effective interest rate provides a unique tool. The Administration has proposed $200 for the Section 515 program versus 50 million in funding in FY 2023. Ongoing funding on the current small level, at a minimum, is needed to address at least some housing finance needs in impacted communities and provide a lifeline resource to help existing properties.

In 2002, RD estimated that 4,250 Section 515 properties with 85,000 units "would physically deteriorate to the point of being unsafe or unsanitary within the next 5 years." At that time, RD estimated it would need $850 million to maintain just this portion of the portfolio, and that as much as $3.2 billion will be required for portfolio-wide rehabilitation. Little progress has been made since 2002. As was demonstrated by a report issued by RD in July 2016 entitled, "*Multi-Family Housing Comprehensive Capital Needs Assessment*," the 2002 $3.2 billion estimate is now approximately $5.6 billion. As a result, in FY2021, the Section 514 and Section 515 portfolio consisted of 13,215 apartment complexes containing 412,176 units and is decreasing every year.

Under the proposed FY 2023 budget, the MPR program would receive $75 million, an increase over the FY 2022 level of $34 million. The Administration has acknowledged that there is a need for additional money because of the backlog in commitments for the Multifamily Housing Preservation and Revitalization (MPR) Demonstration Program. **There are about four years of approved transactions either waiting to close or closing on a temporary workout status. Therefore, we continue to support efforts that would provide $1 billion for this program.** Funding for this portfolio will not only provide for the extremely low-income families and elderly residents but will also improve infrastructure and create jobs throughout rural America.

At the same time, while MPR is a good concept, it has been implemented in various ways, and many strategies have not been successful. **We continue to urge RD to schedule stakeholder meetings and again confer with the Senate Banking, Housing and Urban Affairs Committee, and the House Financial Services Committee on what has been successful and what has not worked in the rural preservation arena.**

Expanding Multifamily Loan Credit Through Section 538 Guaranteed Loan Program

CARH greatly appreciates the support shown for a fee-based, revenue neutral Section 538 Guaranteed Rural Rental Housing program. We believe that the Section 538 is proving to be an important housing tool, at no cost to the government. There are also multiple regulatory changes that CARH has requested of RD which will greatly improve program efficiency. CARH further supports legislative change to prompt RD to allow the Section 538 program to be used to refinance existing mortgage loans used to pay for prior construction and acquisition costs. **CARH supports the Administration's proposal that would provide $400 million in loan authority for the Section 538 program in FY 2023**. Expanding the program will preserve the pipeline, and more than that, it will allow lenders and borrowers to look at the program as having material capacity to help expand their rural housing credit needs.

HOME Partnership Program

Also, key to rural housing recapitalization is maintenance of the HOME Partnerships program, administered by HUD. HOME uniquely empowers state and localities to respond to the housing needs they judge most pressing, allowing them to serve the whole spectrum of need from homelessness to rental to disaster recovery assistance. HOME is flexible and can be used in rural or non-rural areas.

The HOME program is a vital resource in financing numerous affordable housing developments, many of which would not be able to go forward and many of which would not provide housing for low-income families without this important program. HOME does not replace other financing resources committed to rural areas but is an important gap financing program. States and localities leverage HOME by generating almost four dollars of other public and private funding. to HUD. **CARH supports the Administration's request of $1.95 billion for program in FY 2023.**

Administrative Steps Needed

Technology Upgrades Needed for RD

Additional monies are proposed for IT upgrades throughout RD. Specifically, the last Administration's FY 2021 budget proposed $5 million for the Program Loan Accounting System and $5 million for the Automated Multi-family Accounting System. CARH continues to be supportive of RD's efforts to obtain funds to upgrade its very outdated IT systems and keep current with customer's needs.

Increased staffing for the Multifamily Housing (MHF) office

CARH strongly supports increased staff resources for RD's MHF office. The MFH staff is comprised of dedicated, committed professionals doing their best under very difficult circumstances. Our members interact constantly with the MFH staff, and it has been clear that MFH teams need additional resources to address rising workloads, retiring staff, and the increasing need for tools that will provide funding for the preservation of the existing portfolio. Staffing issues have created customer service problems vis-à-vis delays and processing inaccuracies. The mission under the MFH realignment is encouraging to us as it has introduced a number of very good, stakeholder supported process improvements. We will not realize the benefits of these efforts if staffing remains below the levels requested. We are encouraged that recently some additional staff have been added to the MFH office but understand that there remains a need for further hires. We hope that the agency will be able to employ those needed individuals in the near future.

On behalf of CARH, we again thank the Committee for this opportunity to discuss rural housing issues with you today. With a few relatively minor changes, Congress can provide the tools needed to continue the successful public/private partnership for affordable rural housing. We welcome the opportunity to work with you, RD and our fellow stakeholders to formulate such changes and improvements.