NCSHA

February 23, 2016

MEMORANDUM

TO: NCSHA Members

FR: NCSHA's Policy and Government Affairs Team

RE: Analysis of the Administration's Proposed FY 2017 Budget

Summary

The Administration sent Congress yesterday its Fiscal Year (FY) 2017 Budget, proposing funding for all federal programs, including HUD and the Department of Agriculture's (USDA) rural housing programs. The Budget proposes a total of $1.1 trillion in discretionary spending for FY 2017, abiding by the discretionary caps negotiated as part of the Bipartisan Budget Act of 2015. President Obama's final budget request of his presidency incorporates several policy proposals we've seen in previous years but also introduces new ones, including a ten-year, $11 billion mandatory spending proposal to combat family homelessness.

The Budget also contains the Administration's tax proposals. For the fourth consecutive year, the Administration proposes to allow states to convert a portion of their private activity bond (PAB) volume cap into Housing Credit authority. The FY 2017 proposal is identical to the bond conversion proposal the Administration made in its FY 2016 Budget, which also allowed states to convert up to 18 percent of their PAB volume cap into Credit authority.

The Administration again proposes to repeal the Mortgage Revenue Bond (MRB) program purchase price limit and refinancing restriction; create a new permanent American Fast Forward (AFF) Bond program, which would be an optional alternative to traditional tax-exempt bonds; and to cap the value of itemized deductions and other tax preferences, including the income exclusion of interest on tax-exempt bonds, to 28 percent.

NCSHA's analysis of the Budget's housing proposals follows.

HUD and USDA Highlights

The Administration proposes $48.9 billion in HUD gross discretionary budget authority, a $1.9 billion, or 4 percent, increase over the $46.9 billion provided in the FY 2016 omnibus spending bill the President signed on December 18, 2015. The Budget also proposes $11.3 billion in new mandatory spending over ten years, with an emphasis on ending family homelessness by 2020, supporting tribal communities, and making investments in communities to revitalize high-poverty neighborhoods.

The FY 2017 Budget proposes to fund HOME at its FY 2016 funding level of $950 million. The Budget also proposes spending increases to ensure enough funding for renewals in the Housing Choice Voucher (voucher), Project-Based Rental Assistance (PBRA), Section 202 Housing for the Elderly, Housing for Persons with Disabilities, and Housing Opportunities for Persons with AIDS programs. However, funding increases to expand authority are only seen in the voucher program. These include $88 million for 10,000 new vouchers for homeless families with children and $7 million for the Tribal HUD-VASH program. The voucher program also includes a significant increase for administrative fees under a new fee formula HUD will release in Calendar Year 2017.

HOME: The Budget proposes $950 million for HOME, equal to its FY 2016 funding level. The Budget sets aside $10 million of this total for the Self-Help Homeownership Opportunity Program (SHOP).

The FY 2017 Budget proposes several new statutory changes to HOME, including: eliminating the 24-month commitment requirement; eliminating the 15 percent Community Housing Development Organization (CHDO) set-aside requirement; and allowing recaptured HOME CHDO technical assistance funds to be reallocated as HOME technical assistance. The Administration renewed proposals in last year's Budget to establish a single qualification threshold of $500,000 irrespective of the appropriation amount and revise the current "grandfathering" provision so that participating jurisdictions that fall below the threshold three years during a five-year period are ineligible for direct formula funds.

HOME is part of the proposed Upward Mobility Project, an initiative first proposed in the FY 2016 Budget that would allow states and localities to blend funding across four block grants, including the Department of Health and Human Services' (HHS) Social Services Block Grant and Community Services Block Grant, as well as HUD's Community Development Block Grant and HOME. In exchange for more accountability for results, participating jurisdictions would be able to use the funds beyond the current allowable purposes to implement strategies for helping individuals succeed in the labor market and improving economic mobility, children's outcomes, and the ability of communities to expand opportunity.

Housing Choice Vouchers: The Budget proposes $20.9 billion for the voucher program, 7 percent more than the FY 2016 appropriation. This includes $18.4 billion for expiring voucher renewals, $765 million more than the FY 2016 appropriation. The voucher program funding also includes $2.1 billion for public housing agencies' (PHA) administrative costs, 26 percent, or $427 million, more than the FY 2016 appropriation. The Budget indicates that this increase will "fully fund" administrative fees under a new fee formula that HUD plans to implement in Calendar Year 2017. The Budget also indicates that the increased funding for PHA administrative fees will also ensure that PHAs have resources to promote mobility for families with vouchers.

In addition to funding all existing vouchers, the Budget proposes $88 million for 10,000 vouchers for homeless families with children. This is intended to complement an $11 billion mandatory proposal to end family homelessness. The Budget also proposes $7 million for a new Tribal HUD-Veterans Affairs Supportive Housing (VASH) voucher program. The Budget does not propose new separate funding for the traditional VASH program.

Finally, the Budget proposes $15 million and statutory authority to implement a Mobility Counseling Demonstration program to help families with vouchers to move to and stay in areas of opportunity. These funds would be used to pay for counseling, landlord outreach, portability coordination, security deposits, and other administrative functions.

The Budget proposes legislative reforms to the voucher program, including increasing the threshold used to determine deductions for unreimbursed medical expenses from 3 to 10 percent of family income; improving the process for establishing Fair Market Rents; simplifying the calculation for the 20 percent project-based voucher cap by basing the maximum on units rather than funding level; implementing a new formula to allocate administrative fees; and extending the maximum term of Family Unification Program vouchers issues to youths aging out of foster care from 18 to 60 months.

Homeless Assistance Grants: The Budget proposes $2.7 billion for Homeless Assistance Grants, 18 percent, or $414 million, over its FY 2016 funding level. This account includes targeted discretionary funds to create 25,500 new units of permanent, supportive housing; 8,000 new units of rapid rehousing; and $25 million to test innovative projects targeted to youth experiencing homelessness.

The Budget also proposes $11 billion in mandatory spending over the next ten years to end homelessness among families by 2020. The Budget indicates that its proposed "Homeless Assistance for Families" program would serve 550,000 families with additional vouchers, permanent supportive housing, and rapid rehousing assistance.

Section 8 Project-Based Rental Assistance (PBRA): The Budget proposes $10.8 billion for Project-Based Rental Assistance (PBRA), of which $400 million is an advance appropriation to be available in 2018. The Budget continues to support the program's calendar year funding cycle and provides 12 months of funding for contracts that are renewed from January to December 2017.

The Budget proposes $10.5 billion to renew expiring Section 8 project-based contracts, a 2 percent increase from the FY 2016 appropriation. The PBRA program also includes $235 million for performance-based contract administrators' (PBCA) administrative fees, $20 million more than appropriated in FY 2016.

The Budget includes a proposal to expand HUD's authority to seek double the specified financial damages when PBRA project owners fail to maintain their properties in accordance with program requirements. This proposal would also apply to Section 202 and Section 811 properties. The Budget indicates this is part of a larger effort being undertaken by HUD to evaluate and strengthen enforcement authorities across its portfolio of assisted properties, including a potential rulemaking to update Real Estate Assessment Center (REAC) physical inspection criteria.

Housing Opportunities for Persons with AIDS (HOPWA): The Budget proposes $335 million for HOPWA, equal to its FY 2016 appropriation. The Budget also proposes legislative reforms that would update the distribution formula to reflect cases of persons living with HIV instead of cumulative cases.

Housing Trust Fund: The Budget anticipates the launch of the Housing Trust Fund in calendar year 2016, estimating that $182 million will be allocated to the HTF this year. HUD's budget includes an assumption that $12 million of this will not be obligated to States by the end of FY 2016, so it will get carried over in to the next year's allocation. NCSHA expects to learn the exact HTF figure in the coming weeks when the GSEs report the amount they will transfer for HTF. The Budget also estimates HTF funding at $136 million for FY 2017.

Federal Housing Administration (FHA) Single-Family Insurance Program: The Budget estimates that FHA's Mutual Mortgage Insurance Fund (MMIF), which supports FHA's single-family and home equity conversion mortgage (HECM) programs, will meet its statutorily mandated 2 percent capital ratio for the first time since 2008. The Budget requests a $400 billion cap on loan guarantees for MMIF programs. The Administration projects that, in FY 2017, FHA will insure $204 billion in single-family loans and $18.5 billion in HECMs.

The Budget requests $160 million for costs associated with administering MMIF programs, a $30 million increase over FY 2015. In addition, the Administration asks Congress to give FHA the authority to charge lenders an administrative fee for each loan FHA insures through FY 2019. HUD says that it is requesting this additional funding to pay for a series of new initiatives that will allow it to improve the fund's efficiency, including improvements to its information technology and contract administration.

The Budget also indicates that the Administration will pursue legislation to give HUD additional authorities to minimize FHA's future losses. These include the authority to seek indemnification for failed loans from direct endorsement lenders; the authority to terminate underperforming lenders' approval to originate FHA-insured loans on a broad geographic basis; and the authority to revise FHA's Compare Ratio to provide greater clarity and certainty for lenders.

Ginnie Mae Securitization of FHA-HFA Risk-Sharing Program Loans: In 2015, FHA established a partnership with the Federal Financing Bank (FFB) to provide FFB financing for multifamily loans guaranteed by FHA under the FHA-HFA Risk-Sharing Program. The Budget indicates that this financing is available on an interim basis until Congress approves its FY 2017 proposal to permit Ginnie Mae securitization of such mortgages. This legislative proposal, supported by NCSHA, also was included in the Administration's FY 2013, FY 2014, FY 2015, and FY 2016 Budgets.

Rental Assistance Demonstration (RAD): The FY 2017 Budget indicates that HUD will continue efforts to preserve and improve public and assisted housing through RAD, as authorized by the FY 2012 Appropriations Act. Under RAD, HUD offers PHAs and other owners of rental properties assisted under the Public Housing, Moderate Rehabilitation (Mod Rehab), Rent Supplement (Rent Supp), and Rental Assistance Payment (RAP) programs the option to convert their subsidies to long-term project-based Section 8 contracts that can leverage private financing for capital improvements.

HUD says it will continue to process no-cost conversions in FY 2017. The Budget also requests $50 million for a targeted expansion of RAD to enable Section 202 Housing for the Elderly Project Rental Assistance Contracts (PRACs) the option to also convert to Section 8 contracts. HUD would prioritize properties located in high poverty neighborhoods, including designated Promise Zones, and conversions of Section 202 PRAC properties that have significant recapitalization needs in high need areas, as well as other criteria, including properties with service coordinators for frail and elderly residents.

The Budget also contains four proposals to facilitate additional conversions of HUD-assisted properties, including: eliminating the 185,000 unit cap on Public Housing conversions; eliminating the Section 30, 2018 deadline for RAD application submissions; standardizing ownership and control requirements for converted properties in situations where Housing Credits are used or where foreclosure, bankruptcy, or default occurs; and protecting tenants' rights to continue occupancy under "second component" RAD conversions.

Housing Counseling: The Budget proposes $47 million for housing counseling, the same amount it received in FY 2016. The Administration's request is a notable decrease from its FY 2016 Budget, when the Administration requested $60 million for counseling programs.

FHA Multifamily Programs: The Budget proposes a limitation of $30 billion on loan guarantees for FHA's General Insurance and Special Risk Insurance (GI/SRI) fund, which finances FHA's affordable multifamily and health care facility loan insurance programs.

<u>Ginnie Mae</u>: The Budget requests $500 billion in loan authority for FY 2017 for Ginnie Mae. HUD predicts that the agency will ensure $336 billion in new mortgage-backed securities in FY 2017. HUD also requests that Ginnie Mae receive $23 million for administrative and salary expenses. Ginnie Mae has been asking Congress for more funding in recent years to help it hire more staff and update its infrastructure.

<u>USDA Rural Housing Programs:</u> The Budget recommends funding the Section 502 unsubsidized guaranteed loan program at $24 billion, equal to its FY 2016 funding level. The Budget also proposes to allow direct endorsement, whereby approved lenders may make loans under the program without USDA pre-approval of each loan.

The Budget proposes $900 million for the Section 502 single-family subsidized direct loan program, the same amount it received in FY 2016.

The Budget also proposes:

- $33 million in funding for the Section 515 rural rental housing loan program, $5 million more than its FY 2016 funding level.

- $34 million for the Multifamily Preservation and Revitalization (MPR) demonstration program, a $5 million decrease from its FY 2016 funding level.

- $230 million for the Section 538 multifamily loan guarantee program, an $80 million increase from its FY 2016 funding level.

- $18 million for the Section 542 rural housing voucher program, a $3 million increase from FY 2016.

- $1.4 billion for the Section 521 Rental Assistance program, a $16 million increase from FY 2016.

The Budget also recommends that USDA provide quarterly reports to the Committees on Appropriations on the number of rental assistance renewals approved, the amount of rental assistance available, and the anticipated need for rental assistance the remainder of the fiscal year.

Other Budget Proposals Relevant to Housing

<u>Government-Sponsored Enterprises (GSEs):</u> The Budget calls on Congress to advance comprehensive GSE reform legislation that winds down Fannie Mae and Freddie Mac. The Administration pledges to work with Congress on developing reform legislation. While the Budget does not propose as specific plan, it does list the Administration's key principles for housing finance reform, which include: requiring more private capital in the system; ending

Fannie Mae and Freddie Mac's dominant role in the housing finance market; ensuring broad access for all creditworthy families to sustainable products like the 30-year fixed-rate mortgage in good times and bad; helping ensure that sustainable rental options are widely available; and supporting a steady stream of funding for programs such as the Housing Trust Fund and Capital Magnet Fund. The Budget cites bipartisan GSE reform legislation (The Housing Finance Reform and Taxpayer Protection Act, also known as the Johnson-Crapo bill) that the Senate Banking Committee approved in 2014, which the Administration says took a "meaningful step" towards meeting its goals for housing finance reform.

The Administration also pledges, in the absence of housing finance reform legislation, to continue taking action to reduce taxpayer risk from the GSEs, including encouraging Fannie Mae and Freddie Mac to enter into more risk-sharing transactions with private investors and supporting the development of a new single-family common securitization platform.

Housing Credit: To help states finance more developments than they currently can within existing Housing Credit authority, the Budget again proposes to allow states to convert up to 18 percent of their annual private activity bond (PAB) volume cap into Housing Credit authority. For every $1,000 of PAB volume cap it converts, a state would receive 9 percent Credit authority equal to $1,000 times the 30 percent present value (4 percent) Credit percentage for the previous December times two.

The Administration included bond conversion proposals in its FY 2014, FY 2015, and FY 2016 Budgets, but Congress has not enacted them. The FY 2017 proposal is identical to the bond conversion proposal the Administration made in its FY 2016 Budget, which also allowed states to convert up to 18 percent of their PAB volume cap into Credit authority. The Administration has estimated this would enable states to increase their Housing Credit caps by 50 percent. The FY 2015 and FY 2014 Budgets limited the amount of PAB volume cap states could convert to 8 percent and 7 percent, respectively.

The Budget also repeats a proposal included in each of the last three year's Budgets, but not enacted, to provide an alternative method of qualifying for 4 percent Housing Credits. Under the proposal, developments would be eligible for the Housing Credit without financing at least 50 percent of a building with tax-exempt PABs, provided that a bond issuer allocated bond authority to the project and the state's PAB volume cap was reduced as if the tax-exempt bonds had been issued.

The FY 2017 Budget includes a new provision that would establish an allocation preference for projects that affirmatively further fair housing. Currently, the Internal Revenue Code requires state Qualified Allocation Plans (QAP) to give preference to projects serving the lowest income tenants, those serving qualified tenants for the longest periods, and projects located in qualified census tracts that would contribute to a concerted community revitalization plan. This proposal would add a fourth allocation preference to that list.

To encourage the preservation of federally assisted affordable housing, the Budget re-proposes adding to the ten QAP selection criteria currently required under the Internal Revenue Code an eleventh criteria for preservation of federally assisted affordable housing. This proposal was included in the FY 2014, FY 2015, and FY 2016 Budgets but was not enacted.

The Budget re-proposes modifying the program's income limits to allow development owners to serve families with incomes above 60 percent of area median income (AMI), as long as the average income of at least 40 percent of the units in a development is not greater than 60 percent of AMI. None of these units could be occupied by an individual with income greater than 80 percent of AMI, and any units with income limits less than 20 percent of AMI would be treated as being at 20 percent of AMI. The proposal would allow existing tenants in HUD- and USDA-assisted developments, whose incomes have increased above 60 percent of AMI but are less than 80 percent of AMI, to remain in the development without jeopardizing the development's eligibility for Credit financing. Under current law, units occupied by tenants with incomes above 60 percent of AMI do not qualify for Credit assistance. The Administration has included this proposal in each of its annual Budgets since FY 2012, but Congress has not enacted it.

The FY 2016 Budget again proposes to provide HUD additional flexibility for designating Qualified Census Tracts (QCT) by removing the current limit that caps the aggregate population in census tracts designated as QCTs at 20 percent of each metropolitan statistical area's (MSA) population. QCTs would continue to be defined as census tracts characterized by a poverty rate of at least 25 percent or in which at least 50 percent of the households earn 60 percent or less of AMI. The Administration argues that the change is necessary because under the current system, tracts with otherwise qualifying levels of poverty are kept from attaining QCT status by the presence of similarly distressed areas in the same MSA.

To help enforce provisions of the Violence Against Women Reauthorization Act of 2013, the Budget again proposes requiring protection for victims of domestic violence in Housing Credit extended use agreements. The proposal also clarifies that occupancy restrictions or preferences that favor persons who have experienced domestic abuse would qualify for the special needs exception to the general public use requirement. This proposal was included in the FY 2015 and 2016 Budgets but was not enacted.

The Budget does not include a proposal that was part of the last three Administration Budgets and would modify the formula for calculating the rates for the 9 percent Credit and the 4 percent Credit on the grounds that the current discounting formula does not function well when rates are particularly low or high. The Administration had supported this change to the Housing Credit discount rate as an alternative to setting minimum Housing Credit rates. However, Congress in 2015 passed legislation permanently establishing a minimum 9 percent Housing Credit rate. This may have contributed to the Administration's decision not to re-propose modifying the Housing Credit discount rate.

<u>Housing Bonds:</u> The Budget again proposes to limit the tax rate at which upper-income taxpayers can use itemized deductions and other tax preferences, including interest on tax-exempt bonds, to reduce their tax liability to a maximum of 28 percent. This limitation would reduce the value of the specified exclusions and deductions that would otherwise reduce taxable income in the top three individual income tax rate brackets of 33, 35, and 39.6 percent to 28 percent. This proposal was included in the President's previous four Budgets but was not enacted.

The Budget proposes to repeal the Mortgage Revenue Bond (MRB) purchase price and refinancing limitations. It would retain other targeting requirements, including the MRB income limits and targeted areas requirement. These proposals were included in the last five Budgets proposed by the Administration but were not enacted.

<u>America Fast Forward (AFF) Bonds</u>: The Administration proposes again to create a new permanent America Fast Forward (AFF) Bond program, which would be an optional alternative to traditional tax-exempt bonds. The AFF program would expand on the expired Build America Bonds (BAB) program, under which Treasury made direct subsidy payments (called "refundable tax credits") to state and local governmental issuers of taxable bonds in a subsidy amount equal to 35 percent of the coupon interest on the bonds. Housing was not an eligible activity under the BAB program.

AFF Bonds would be conventional taxable bonds issued by state and local governments. The federal government would make direct payments to state and local governmental issuers of these bonds at a 28 percent subsidy rate. The Budget says this rate would make the proposal revenue-neutral in comparison to the federal tax losses from traditional tax-exempt bonds. The proposal would be effective for bonds issued on or after December 31, 2016.

Allowable eligible uses would include all PAB-eligible activities, including housing, subject to applicable state bond volume cap authority for PABs. The Administration argues that the AFF program will provide a more efficient means of supporting state and local governments than tax-free municipal bonds.

The Administration's proposal would prevent payments to state and local governments through the AFF program from being reduced through sequestration. Such payments under the BAB program are not protected from sequestration, which has reduced the amount of federal refunds state and local governments have received. The Administration has included this proposal in its Budgets each year since FY 2014, but Congress has not enacted it.