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MORTGAGE BANKERS ASSOCIATION

June 17, 2019

The Public and Regulatory Analysis Division
Office of Policy Development and Research
Department of Housing and Urban Development
451 7th Street NW, Room 8216
Washington DC 20410-0500

Re: Review of HUD Policy in Opportunity Zones (Request for Information)

Dear Ladies and Gentlemen:

The Mortgage Bankers Association is pleased to respond to the Request for Information (RFI) of the Department of Housing and Urban Development (HUD), regarding Review of HUD Policy in Opportunity Zones.[1]

I. BACKGROUND

The 2019 Tax Cuts and Jobs Act created new tax incentives to make investments within designated Opportunity Zones, to spur economic development and job creation by encouraging long-term private-capital investment in economically distressed communities.

MBA supports this objective. We also recognize that the Opportunity Zone incentives for equity investment of capital gains will generate the intended benefits only if the broader commercial and multifamily development ecosystem is also actively engaged. This includes HUD and other federal agencies, sources of debt capital, developers, business operators, state and local governments, and state Housing Finance Agencies (HFAs).[6]

Sources of debt capital include MBA member companies that can provide mortgage debt financing for the acquisition and substantial improvement of business properties. To further the purposes of the Opportunity Zones provision, MBA continues to work with our members across multiple capital sources to ensure that they are prepared to play a critical role in financing Opportunity Zone projects.

Housing projects can stimulate and support economic development and job creation in Opportunity Zones, so it is appropriate that HUD Secretary Ben Carson, MD, has a special role with respect to Opportunity Zones. Specifically, an executive order established a new While House Opportunity and Revitalization Council of various agency heads, which is chaired by the HUD Secretary.[2]

[1] 84 Fed. Reg. 16029 (April 17, 2019).

[2] Executive Order 13853 (Dec. 12, 2018).

Appropriate the role HUD-administered housing programs can have on economic development and job creation in Opportunity Zones, HUD has determined that it should review of existing policies, practices, planned actions, regulations and guidance regarding HUD-administered programs to identify ways to encourage beneficial investment in Opportunity Zones consistent with HUD's core housing mission.

To facilitate that review, HUD has issued this RFI, which seeks relevant information and perspectives from a broad range of stakeholders. MBA provides out comments below

II. HUD PROCESSES

Many of the questions in the RFI revolve around process issues, including how HUD could reduce barriers or friction in ways that might identify ways to encourage beneficial investment in Opportunity Zones.[3]

A. HUD Opportunity Zone Incentives

We applaud HUD actions already taken to reduce barriers and friction. In particular, in a May 9, 2019 release, HUD announced that was decreasing barriers to possible Opportunity Zone investment.[4] This includes both reducing application fees and reducing process friction by allocating expert resources and committing to expedited processing.

We understand that HUD may also be considering some additional changes, including:

- Submission of streamlined Plans and Specs (already allowed for affordable deals);
- Early start of the environmental review, including SHPO/THPO correspondence (subject to certain conditions being met, other 3rd parties completed; appl. submission shortly after, etc.; and
- Setting a closing date at the time the Firm Commitment is issued

In addition to the above, we suggest HUD also consider the following changes, which are similar to elements of HUD's actions to foster private-sector investment in Opportunity Zones described above:

- Dedication to meeting stated processing times;
- An early start of 2530/Previous Participation review;
- An early start of HUD management forms and Affirmative Fair Housing Marketing Plan reviews by Asset Management;
- Limit HUD's plan and cost review to compliance with civil rights laws and applicable accessibility requirements; and
- Reduce inspection fee to 0.25 percent rather than 0.50 percent.

[3] See, e.g., RFI item (1)(b), 84 Fed. REg. at 16031.

[4] "FHA OFFERS INCENTIVES FOR PROPERTY OWNERS WHO INVEST IN OPPORTUNITY ZONES, *Lower costs and dedicated underwriters to stimulate housing investment in distressed neighborhoods,"* (May 9, 2019); https://www.hud.gov/press/press_releases_media_advisories/HUD_No_19_058.

Adopt delegated construction monitoring and escrow releases, as allowed under the Expedited track of the (d)(4) Pilot

As an additional benefit, process improvements prompted by the review process underlying the RFI could carry forward to inform potential similar process improvements across other HUD-administered programs.

B. CNA eTool improvements

We also note improvements HUD has made and plans to make to the CNA e-Tool. While those improvements benefit FHA-financed projects without regard to whether they are located in an Opportunity Zone, the improvements help reduce process friction that could otherwise serve as a disincentive to investment in Opportunity Zones.

III. HUD PROGRAMS AND POLICIES

HUD is seeking ideas on actions HUD could take within its existing authority, including "what policies could HUD implement that would make it easier for recipients to receive and manage multiple types of public and private investments, including by aligning certain program requirements?"[5]

A. LIHTC program

While not something HUD could do unilaterally under its existing authorities, we believe that HUD could also stimulate additional Opportunity Zone investments by working with Treasury to better align the requirements of the Low-Income Housing Tax Credit (LIHTC) with the Opportunity Zone incentives specified in the Tax Cuts and Jobs Act. We note that the Secretary of the Treasury is a member of the White House Opportunity and Revitalization Council that the HUD Secretary chairs.

The difficulty in combining the LIHTC program and Opportunity Zone incentives is a recurring theme that we are hearing from our members.

B. Historic Tax Credit projects

FHA-financed Historic Tax Credit (HTC) projects may be useful vehicles for private-sector investment in Opportunity Zone projects. However, certain elements of HUD requirements for FHA-finance projects can unnecessarily result in Master Lease terminations and subsequent tax credit recapture events. We describe in an appendix to this letter two possible changes that HUD could make that could make HTC projects in Opportunity Zones more attractive to investors.

* * *

[5] RFI item (1)(d); 84 Fed. Reg. at 16031.

MBA appreciates HUD's commitment to Opportunity Zones, including its efforts to review and improve or revise how it implements HUD-administered programs and laws, in an effort to encourage beneficial investment in Opportunity Zones, and we appreciate the opportunity to participate in that process. We will continue to provide feedback as our members identify additional opportunities for HUD to take actions to foster beneficial Opportunity Zone investment.

For additional information, please contact Associate Vice President, Commercial/Multifamily, at 202-557-2747 or swalker@mba.org.

Sincerely,

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Appendix to MBA Response to HUD RFI on Opportunity Zones
June 17, 2019

POSSIBLE CHANGES TO ADMINISTRATION OF THE HISTORIC TAX CREDIT PROGRAM

MBA suggests two alternative possible changes, below, to how HUD's FHA program interacts with the Historic Tax Credit (HTC) program that could make HTC Opportunity Zone projects more attractive to private-sector investors.

Background

HTC projects utilize a Master Lease structure, which preserves the investor's basis by not reducing basis by the depreciable property and also allows for a greater share of available cash flow to flow to the developer.

In the case of FHA-financed projects, Chapter 16.3.G of the MAP Guide requires that HUD have the ability to terminate the Master Lease. This requirement is almost always reflected in both the "HUD Required Provisions" in the Master Lease and in the Standard Non-Disturbance and Attornment Agreement (SNDA), if HUD permits the lender to enter into an SNDA with the Master Tenant (i.e., the entity entering into the lease with the mortgagor). HUD's termination of the Master Lease would result in a recapture of the tax credits from the HTC investor in the Master Tenant.

In non-FHA financed transactions, HTC investors typically require an SNDA to avoid the risk of Master Lease termination and subsequent recapture event. The standard SNDA would permit the Master Lease to remain in place so long as there was no default under the Master Lease, notwithstanding a default as to the primary financing. Often this provision is coupled with a right of the Master Tenant to cure defaults under the primary financing.

Unfortunately, HUD currently does not sign the SNDA itself or allow the lender to sign it; and in cases where HUD does permit an SNDA, HUD has required an exception provision that states that, in the event the HUD loan is assigned, the Master Lease automatically terminates. Because the termination of the Master Lease triggers a recapture of the tax credits, this practice makes many HTC investors reluctant to invest in projects that include FHA financing.

We suggest two potential solutions to this issue, which we describe below:

Option 1: One way to address this disincentive to investment in FHA-financed HTC projects would be for HUD to allow the SNDA to include a provision to the effect that the lender/HUD agrees not to terminate the lease following a foreclosure. Instead, the lender/HUD would receive a pledge of the developer/Managing Member's (MM) interest in the master tenant.

Such a pledge would give the lender and HUD effective control at both the landlord level and the master tenant level, which would results in a more marketable sale scenario in the event of a default/assignment.

Additional considerations:

- The HTC investor would need to consent to the MM pledge of interest to the lender and the HTC investor would need to agree not to exercise MM removal rights if HUD or lender were to step in as replacement MM. And an HTC investor would need to agree not to unreasonably withhold consent or otherwise hinder HUD's attempts to replace the MM with a capable new manager.
- The HTC investor may want the lender/HUD to allow the HTC investor a right of first refusal to prevent a sale (following foreclosure) to a disqualified transferee (which include tax exempt organizations such as governmental entities, foreign persons, and REITs), because such a sale would trigger a recapture. Preventing sales to disqualified transferees would not impact the value of the collateral because it would exclude such a small segment of potential buyers. HTC investor/affiliates would need to obtain HUD Transfer of Physical Assets (TPA) or other asset management approvals that would be necessary in connection with proposed transfer.
- The lender/HUD would have the right to terminate the Master Lease once the 5-year recapture period had expired.
- Marketability of the project upon foreclosure is dependent upon the amount of cash flow to the HTC investor. One key to the viability of this possible solution is that there should be little to no cash flow going to the HTC investor. Otherwise the marketable value of the developer/MM's interest would be impaired.

Option 2: Alternatively, HUD could permit an SNDA that would allow the Master Tenant to cure any defaults under the mortgage loan documents, so long as there is no default under the mortgage loan. That is, HUD could agree not to terminate the lease so long as the Master Tenant guarantees repayment of the mortgage loan and regulatory compliance.