



Testimony of The Institute for Responsible Housing Preservation
Presented by Sarah Metherell, Vice President, Steadfast Companies
Financial Services Committee
Subcommittee on Housing and Community Opportunity
U.S. House of Representatives
Hearing on Affordable Housing Preservation
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Madam Chairman. Thank you for inviting me to testify on the important topic of affordable housing preservation. My name is Sarah Metherell. I am Vice President of Acquisitions for Steadfast Residential Properties which is based in Newport Beach, CA. Steadfast Residential is involved in the acquisition, rehabilitation and preservation of federally assisted multifamily affordable housing properties. We own and manage approximately 15,000 apartments in 18 states, concentrated primarily in California and the Western United States. Nearly all of our properties receive some form of federal assistance including low income housing tax credits and project based Section 8.

I am here today in my capacity as Vice President of the Institute for Responsible Housing Preservation (“IRHP”). Since 1989 IRHP has represented owners and managers of federally assisted multifamily properties on preservation issues including advocating for legislative and regulatory changes for preservation policies and providing educational seminars on preserving affordable housing. IRHP members worked with this committee and HUD in structuring and closing the first Section 236 “de-coupling” preservation transactions in 1998. More than 800 Section 236 properties – approximately 80,000 units – have been substantially rehabbed and

preserved as affordable housing over the past 11 years using the de-coupling program. In his testimony before the Financial Services Committee two weeks ago, HUD Secretary Shaun Donovan recognized the de-coupling program as one of HUD's premier and successful preservation initiatives.

Madam Chairman, as you know well, even with the success of the 236 de-coupling transactions, there is more work to be done in preserving the existing HUD multifamily portfolio. No one questions the need for affordable housing. Various private and public studies prove that. Yet, notwithstanding the benefits and proven success of the Section 236 de-coupling preservation program HUD has not taken the lessons learned from this initiative and applied them beyond the Section 236 portfolio. Many other properties financed under other affordable housing programs are also in need of preservation. Many of these properties continue to be "at risk" to conversion to market rate housing or are in crucial need of updating, repairs and energy upgrades. These aging properties are approaching the end of their use restrictions, in most cases within the next few years.

We all know that it is much less expensive to preserve an existing asset than to build a new one. We think HUD should be embracing the success of the Section 236 de-coupling program and utilize the same preservation tools for these other portfolios. In most instances, HUD has the statutory and regulatory authority to implement the required preservation tools for other affordable programs.

The critical tools that made the de-coupling program a success include:

- A budget based rent increase which includes new debt service.

This upfront analysis and setting of rents is critical to get lenders and equity providers comfortable with any preservation transaction. Unfortunately, the Section 8 guidelines do not allow for budget based rent increases to include new debt service to be used in calculating rents, which would be capped at post rehab market levels. Without the ability to know what rents HUD will pay it is extremely difficult to finance a preservation transaction or be competitive with conventional buyers hoping to convert the property to market rate housing to the detriment of the residents and communities most in need. Again, in his recent testimony Secretary Donovan addressed this issue and pointed it out as a critical component to secure financing in a preservation transaction.

- An increased annual distribution for all preservation owners – for profits and nonprofits.

Both the Section 236 de-coupling program and the Section 202 preservation program permit an owner to receive increased distributions –a critical incentive to owners. The Section 8 guidelines in April were revised to allow for an updating of the annual distribution in certain circumstances but not all. Today, in many preservation transactions the new owner must accept the original owner’s annual distribution limitation which was established in most cases more than 30 years ago and based on their original investment, not the new investment. HUD has the regulatory authority to change this for all of its properties. Deferred developer fees which may be needed to make a transaction viable can only be paid from distributable cash. Any limitation potentially interferes with the ability to pay a deferred developer fee. IRHP proposes that a cap on distributions be eliminated entirely. Any limitation only serves as a disincentive to preservation.

- Rollover of certain HUD debt.

Oftentimes when properties are being transferred to new ownership certain HUD debt including flexible subsidy loans and Mark-to-Market soft debt cannot be paid off in full. HUD guidelines allow for flex subsidy debt to be rolled over and deferred if it is necessary to make the preservation transaction economically feasible. Notwithstanding these guidelines, HUD over the past several years has required this debt to be repaid, often times making a good preservation transaction unworkable. The draft legislation allows for the forgiveness or assignment of flexible subsidy loans for a preservation developer. We urge you to include the deferral of this debt and expand it to include mortgage restructuring debt held by HUD.

These are simple, practical and workable preservation tools which have made the Section 236 de-coupling program a huge success. I point out that the average rehab in the preservation transactions we have participated in is \$25,000-\$35,000 per unit. The properties are recapitalized and renovated taking into consideration today's standards – increased security, lighting, energy efficient appliances and windows, new baths and kitchens, landscaping and the creation of community and learning centers. Often, owners will also provide a package of tenant supportive services, including lifestyle training, computer training and coordination with local service providers. We did this in our 2008 purchase of the 370 unit Foxview Apartments in Carpentersville, IL and our 2007 purchase of the 400 unit Villa Nueva Apartments in San Diego, CA. Both properties were preserved with a 20-year HAP contract and significantly renovated at a cost of approximately \$30,000 per unit and \$60,000 per unit respectively. In both cases, social service areas were renovated or built, major interior and exterior renovations were undertaken, security was improved, and at Villa Nueva solar panels were installed to supply nearly all of the electric needs for the property. These two acquisitions will provide renovated, safe, well operated housing for nearly 800 low income families for the next 20 plus years.

Madam Chairman, the draft preservation legislation incorporates the lessons learned from the Section 236 de-coupling program and sends a clear message to HUD that preservation should be a priority. Secretary Donovan has a strong record on affordable housing preservation and we believe he will implement key policies to expand preservation. The draft bill however goes even further. It includes converting RAP and Rent Supp contracts which are nearing their 40 year expiration to project-based Section 8, expands the events for providing enhanced vouchers to residents, keeps existing subsidies in properties that otherwise would be lost, and allows for increased opportunities for an owner to project base Section 8 vouchers. Further, it puts to rest HUD's controversial policy of restricting a nonprofit's sales proceeds.

IRHP applauds your efforts. It is critical, however, that all preservation developers – for profit or nonprofit – have access to the same resources – that there is a “level” preservation playing field. Preservation developers are competing for the same resources – tax exempt bonds, low income housing tax credits, and other available federal, state and local funds. The final preservation bill must maintain this evenhandedness. In this regard any abridgement of an owner's property or contract rights will have a chilling effect on preservation. The bill incorporates a federal right of purchase which has the potential to negatively affect these rights. Secretary Donovan himself noted the legal complications of a local law providing certain groups a priority to purchase affordable housing projects in New York City where he served as housing commissioner. The state courts eventually overturned the law but unfortunately preservation efforts in New York City were interrupted for 2 years. This provision should be eliminated.

Madam Chairman, thank you for providing us the opportunity to testify here this morning on this extremely important issue. IRHP and its members are committed to affordable housing.

We are committed to preservation. We look forward to working with you and Secretary Donovan in expanding the efforts to preserve affordable housing.