MORTGAGE BANKERS ASSOCIATION

May 12, 2015

Mr. Benjamin T. Metcalf
Deputy Assistant Secretary for Multifamily Housing
U. S. Department of Housing and Urban Development
Room 6106
451 Seventh Street, SW
Washington, DC 20410-8000

Re: Comments on Chapter and Appendix 5 of the Draft MAP Guide, Requirements for Capital Needs Assessments (CNA), Estimated Reserve for Replacements (R4R) and Energy Audits

Dear Mr. Metcalf:

MBA appreciates the opportunity to review and comment on the MAP Guide prior to its final form, including the requirements for Capital Needs Assessments. HUD's efforts are evident by the quality of the Draft Guide. MBA's comments on other aspects of the Draft MAP Guide will be submitted separately. The CNA comments herein will also be included in a MAP Guide comment form requested by HUD. Overall, Chapter and Appendix 5 provide further improvements since the release of Housing Notice 2012-27/Mortgagee Letter 2012-25.

However, as discussed at the recent MBA FHA Roundtable meeting, FHA MAP lenders believe there are significant challenges with the Chapter and Appendix related to HN 2012-27 (ML 2012-25) and the energy audit requirements that will continue to unnecessarily increase the costs of financing via the HUD Insurance Program. As a result, HUD and its Lender partners are losing opportunities to provide much needed long term financing to workforce and affordable housing properties around the country, and will continue to miss out on future opportunities. We believe that these requirements go too far, inhibiting the financing of needed workforce and affordable rental housing in our communities. More broadly, we are concerned that these requirements could make the Section 223(f) program a program of last resort, which could have detrimental and far reaching impacts.

MBA offers the comments herein on recommended changes to Chapter and Appendix 5 of the Draft MAP Guide, specifically as it relates to CNAs. Comments were developed by the MBA PCNA Working Group, and were discussed at the Lender meeting at the MBA FHA Roundtable.

Positive Aspects of the CNA Provisions in the Draft MAP Guide

In general, we believe the following are positive aspects to the MAP Guide as it relates to CNAs:

- The proposed reduction of the cash-out holdback in certain circumstances
- The proposed reduction of the repair escrow to 110% in certain circumstances

- The proposed increase in the threshold for substantial rehabilitation from $6,500 to $15,000 per unit
- Creating levels of alterations for purposes of properly managing the scope of repairs and the level of due diligence required for each level
- The inclusion of Seismic Resistance and Fire Protection Standards for Existing Buildings
- The breakdown of the various Building Components for purposes of identifying substantial rehabilitation versus refinance
- Further clarification on how to analyze the Estimated and Assessed Remaining Useful Life
- The creation of an R4R schedule for new construction and substantial rehabilitation project
- The implementation of the e-CNA Tool

MBA appreciates the progress made in the CNA provisions. We also firmly believe improvements should be made to the guidance to ensure that HUD and its lender partners can provide financing to rental housing for families of modest incomes. We underscore the following concerns, along with our recommended policy revisions.

Concerns with and Recommendations on the 20 Year Replacement for Reserve (R4R) Schedule

The current minimum replacement reserve balance requirement is increasing the overall reserve contributions on every transaction. In most cases, there is a peak year or two of reserve needs that causes the Initial Deposit to Replacement Reserves (IDRR), as well as the Annual Deposit to Replacement Reserves (ADRR) to over-compensate for those peak years. In almost every proposed R4R schedule, this causes the proposed R4R for the 20 year schedule to be severely overfunded by the end of the term.

Most projects financed prior to the current guidance are retaining sufficient funds in the R4R accounts, when comparing the current balance to the R4R schedule set under guidance prior to HN 2012-27. The previous guidance focused in practice on the first ten years, or “Near Term” requirements for the property, as compared to a 20 year R4R schedule in place today. And when 10 year PCNAs are being ordered, the results show that most of the projects have sufficient reserves in places, even with the more stringent requirements, proving further that the previous guidance was sufficient.

One analysis below shows the impact of funds required under current guidance. The property backed by this specific loan was built in 1978, was workforce housing, and was in good condition overall. For purposes of comparison, we have shown the Fannie Mae numbers, because this loan ended up being financed via Fannie Mae after the HUD PCNA (with 20 year schedule) was presented to the borrower. Under a 12 year schedule, the borrower’s required repairs and initial deposit decrease by over $824,000, while, in our view, still providing sufficient funds to the R4R account.

R4R and Repair Comparison - 1978 Vintage Property					
		223f Pre-Risk Mitigation, (10-year focus)	223f post RM + PCNA Guidance (20 YR R4R)	223f (Proposed 12- Year R4R)	Fannie Mae Loan (12-Year R4R)
Number of Units	**169**				
Year Built	**1978**				
Appraised Value	**$24,100,000**				
Repairs		$61,306	$375,846	$61,306	$ 35,000
IDRR/unit		$234,065	$743,600	$520,520	$ -
Annual RFR/unit		$500	$500	$500	$ 302
Max LTV		85.0%	83.3%	85.0%	80.0%
LTV Loan amount		$20,485,000	$20,082,530	$20,485,000	$ 19,280,000
HUD Repairs and IDRR		$295,371	$1,119,446	$581,826	$ 35,000
Cost to Refinance		$17,934,625	$18,758,700	$17,934,625	$17,674,254
Cost Differential		($824,075)		($824,075)	($1,084,446)
Actual Loan Amount		$17,934,625	$18,758,700	$17,934,625	$17,674,254
Effective LTV		74.42%	77.84%	74.42%	73.34%
Increase in Loan amount due to 20 year R4R				**3.42%**	**4.50%**

Based on this information and other information shared by MAP lenders, we have concluded that a reduction in the minimum balance and number of years in the schedule will not have an adverse effect on the portfolio. We recommend a reduction in the 20-year term of the Reserve tables to no more than 12 years and reduce the 105% balance requirement to 100%. HUD already has a backstop in place to mitigate this risk by requiring a new PCNA at *year ten*. This will reduce the potential for the unnecessary overfunding over the term of the reserve schedule.

The portfolio of multifamily loans is performing well and is composed primarily of loans delivered prior to the effective date of the 2012-25 Mortgagee Letter. We urge HUD to reduce the 20 year replacement reserve schedule to no more than 12 years.

<u>Requirement for Bids on Non-Critical Repairs</u>

The Section 223(f) program requires borrowers to obtain bids for any non-critical repairs over $25,000. We understand that HUD does not want projects to have a significant overfunding/underfunding of the repairs. HUD requires an additional 20% escrow to account for an underfunding of the repair escrow. The MAP Guide includes specific guidance to mitigate the risk of overfunding of the repair escrow.

HUD requires the CNA provider to be a trained professional and use proven methods to establish the estimated cost of each item to be repaired. It is also in the best interest of the borrower to verify any repair recommendations that seem inadequate. Borrowers prefer to use mortgage proceeds, and also do not want to pay any more than necessary. They are not interested in dipping into the 120% cash escrow to complete the work. In instances where the borrower feels the repair estimates are too high, they will obtain bids to justify lowering the repair escrow. The typical borrower/lender interaction mitigates this risk in the lion's share of deals.

We recommend the additional proposed guidance: **"**If the lender and/or borrower determine the estimates provided are insufficient, the lender will require the borrower to obtain bids to ensure the escrowing of adequate funds."

We also recommend that in cases where a General Contractor is involved and provides a Form 2328, separate bids should not be required to be provided to HUD, as the General Contractor is already obtaining bids for their work.

Section 223(f) Benchmarking and Energy Audit Requirements

The proposed changes to the Section 223(f) program include energy benchmark assessments for all properties, as well as an ASHRAE Level II Energy Audit for properties exceeding 10 years of age. We understand HUD's dedication to benchmarking energy consumption within multifamily housing; however, aspects of the new energy requirements are overly burdensome for some properties. We recommend a review of the triggers within the draft Guide that precipitate an ASHRAE Level II Energy Audit.

The age of a property does not often determine energy intensity or use. The age of a building may define the minimum energy code at the time of construction; however, system performance is a much better metric than age. The requirement for ASHRAE Level II Energy Audits on all properties exceeding 10 years of age is overly burdensome in instances of well-performing properties or recently renovated properties (e.g. LIHTC). A well-performing building with a high Statement of Energy Performance (SEP) score will typically be indicative of well-capitalized buildings with newer systems. An approach of making the ASHRAE Level II Energy Audit contingent upon site specific energy scores is more appropriate, than basing the need for the audit upon age alone.

A more pragmatic approach would be the following deductive reasoning:

- All 223(f) properties are to obtain a Statement of Energy Performance (SEP).

- If a property is proposed to have presumed utility reductions underwritten, then the property must obtain an ASHRAE Level II Energy Audit.

- If a property receives a SEP Score of less than 50, then the property must obtain an ASHRAE Level II Energy Audit.

By following this logic, well-performing but older properties would not procure unnecessary and potentially costly energy audits.

MBA looks forward to meeting with HUD to discuss these items, as well as other aspects of the Draft MAP Guide. In the meantime, if you have questions, please do not hesitate to contact MBA's Eileen Grey at egrey@mba.org or me at bob.warren@wellsfargo.com.

Sincerely,

Robert M. Warren, CCIM
Chair, MBA PCNA Working Group

Cc: Ted Toon
Dan Sullivan
Steve Ervin
Sarah Garland