

**H.R. 5039, THE SAVING AMERICA'S  
RURAL HOUSING ACT OF 2006**

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**HEARING**  
BEFORE THE  
SUBCOMMITTEE ON  
HOUSING AND COMMUNITY OPPORTUNITY  
OF THE  
COMMITTEE ON FINANCIAL SERVICES  
U.S. HOUSE OF REPRESENTATIVES  
ONE HUNDRED NINTH CONGRESS  
SECOND SESSION

APRIL 25, 2006

Printed for the use of the Committee on Financial Services

**Serial No. 109-86**



U.S. GOVERNMENT PRINTING OFFICE

30-537 PDF

WASHINGTON : 2006

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## **H.R. 5039, THE SAVING AMERICA'S RURAL HOUSING ACT OF 2006**

**Tuesday, April 25, 2006**

U.S. HOUSE OF REPRESENTATIVES,  
SUBCOMMITTEE ON HOUSING AND  
COMMUNITY OPPORTUNITY,  
COMMITTEE ON FINANCIAL SERVICES,  
*Washington, D.C.*

The subcommittee met, pursuant to notice, at 2:04 p.m., in room 2128, Rayburn House Office Building, Hon. Geoff Davis presiding. Present: Representatives Davis of Kentucky, Neugebauer, Cleaver, and Waters.

Mr. DAVIS OF KENTUCKY. [presiding] This hearing of the Subcommittee on Housing and Community Opportunity will come to order. The Subcommittee on Housing and Community Opportunity meets today for the purpose of hearing testimony on H.R. 5039, the Saving America's Rural Housing Act, a bill to improve Section 515, Rural Multi-Family Housing Programs, through sensible and timely reform measures.

The Housing Act of 1949 originally authorized the U.S. Department of Agriculture to make loans to farmers to improve their ability to provide decent living quarters for their employees and others. The program has evolved over the years to provide affordable housing for the rural community as a general population.

Rural Development, an agency in the U.S. Department of Agriculture, released a November 2004 study prepared for USDA by a private consulting firm on the Section 515 portfolio. With an average property age of 28 years, the study revealed that nearly all Section 515 properties included in the study were in need of additional funds to cover essential repairs and maintenance costs.

I'd like to briefly share with the committee one of the most interesting observations of the study, "If new funds are not invested in these properties, two-thirds of the portfolio will only be able to maintain its current status, which keep in mind is not good already for the majority properties. If the roofs never leak, the paint jobs last forever, the building siding is everlasting, no potholes ever develop in the parking lot, no one will ever need to replace a furnace or air conditioner, no doors will ever rust or rot, and all windows will work forever."

If you've ever owned a home, you know that these things would be ridiculous assumptions on which to base your personal budget in an investment in a home or residential property. And they certainly aren't assumptions on which I'd like to base national policy.

The fact of the matter is that Section 515 properties need help, and they need it now, and they need our help. It will only become more expensive to maintain the program as time progresses. I've seen firsthand the dilapidated state of the Section 515 portfolio while traveling Kentucky's diverse Fourth District during my first year as a representative. In the Fourth District alone, there are 40 Section 515 properties. Many of the properties are in dire need of assistance and repair.

Solutions are needed now to revitalize the program and ensure that it's sustainable for the future. These reforms will have a direct and positive impact on over 1,000 families in the Fourth District of Kentucky and many, many more in rural communities across the United States.

H.R. 5039 will create a revitalization program by offering restructuring plans to Section 515 development owners. This will preserve ailing Section 515 properties for the future, saving the United States taxpayers approximately \$2 billion in maintenance and rehabilitation costs by addressing the programs preventively now.

Section 502(c) of the Housing Act restricts the rights of owners of Section 515 properties to prepay their loan, even after they've fulfilled their contractual duty to the USDA. H.R. 5039 will nullify the onerous restrictions in Section 502(c) to allow for prepayment of certain Section 515 loans entered into before 1989, thereby alleviating expensive litigation against the Rural Housing Service, which has cost taxpayers in the United States millions of dollars today.

Additionally, a voucher program will be created to protect tenants who live in the properties subject to prepayment. It's estimated that only 10 percent of the current development owners would consider prepaying their loans.

H.R. 5039 will save money on future litigation by nullifying the burdensome prepayment restriction and protecting tenants, while revitalizing the existing Section 515 portfolio to continue the tradition of providing housing assistance to our rural families.

This is proactive legislation that seeks to deal with the apparent problems now rather than deal with more expensive solutions later. I'd like to thank the Administration, the Financial Services Committee, Ranking Member Frank, Chairman Ney, and other Members on both sides of the aisle for their help in putting together a good piece of legislation that will help to solve the problems of prepayment while combatting the aging portfolio of Section 515 properties.

The bill institutes sensible and timely reforms that will enable the program to continue providing low income rural families with affordable housing.

Thank you, Chairman Ney, and Ranking Member Waters, for holding the hearing today on such an important and relevant topic. I also want to thank the witnesses on both of our panels for participating, for their graciousness in attending the hearing today, and I look forward to hearing your testimony and your thoughts on the Section 515 program.

Without objection, all members' opening statements will be made part of the record. Does the gentleman from Texas have an opening

statement? Then we'll move to introducing the first panel, in which we have one witness. I'd like to introduce Mr. Russ Davis. He's the Administrator for Rural Development Housing and Community Facilities Programs at the Department of Agriculture.

Prior to joining the Department of Agriculture, Mr. Davis served as a Senior Policy Adviser with the Department of the Treasury, and during the Administration of President George Herbert Walker Bush, he served as the Acting Deputy Assistant Secretary for Housing Operations at the Department of Housing and Urban Development.

Without objection, your written statement will be made part of the record, and you will be recognized for a 5-minute summary of your testimony.

**STATEMENT OF RUSSELL T. DAVIS, ADMINISTRATOR, USDA  
RURAL HOUSING AND COMMUNITY PROGRAMS**

Mr. DAVIS. Thank you very much, Mr. Chairman and members of the subcommittee. I thank you for the opportunity to present this Administration's initial comments on H.R. 5039, the Saving America's Rural Housing Act of 2006.

Let me begin by acknowledging and thanking the sponsors and co-sponsors of H.R. 5039 for their leadership on this important issue. Mr. Chairman, we appreciate the fact that you personally have been interested in this bill, as well as Chairman Ney, and Ranking Member Frank. The quality of thought and effort are evident throughout. We also thank everyone involved with this legislation for their work and the experience they have brought to this process.

There is an urgent need to address long-term physical and economic needs in the rural rental housing portfolio. There are over 17,000 properties in this portfolio. Our studies have shown that the two biggest threats to it are prepayment, expected to affect 10 percent of the portfolio, and more importantly, the potential loss of properties due to physical deterioration and economic obsolescence. This bill will address both problems. I'm grateful that we are stepping up to that challenge.

The Administration supports the basic strategy outlined by this legislation and believes it will work. In fact, I'm pleased to report to the committee that the two new housing mechanisms in this bill, rural vouchers and debt restructuring, are already being tested on a demonstration basis with promising results.

First, and thanks to your assistance, Mr. Chairman, USDA issued its first rural housing vouchers last month. A property in southern Georgia had left the program after meeting all of the prepayment requirements. The residents would have faced eviction within 30 days, but Under Secretary Thomas C. Dorr, of the USDA, personally went to Georgia to give the affected families housing vouchers that allowed them to remain in their homes.

On the debt restructuring side, and also thanks to your assistance, Mr. Chairman, USDA has begun a test demonstration of the types of multi-family restructurings envisioned in H.R. 5039. Within the last 30 days, owners of approximately 4,000 properties have applied to undergo debt restructuring. This shows that there is demand for the transactions authorized by H.R. 5039. The 4,000 ap-

plications total almost 25 percent of the entire Section 515 portfolio. But without the authorization provided by H.R. 5039, only a handful of these can undergo a restructuring that will keep them affordable.

The Administration's own revitalization proposal was circulated on the Hill in August of 2005. The President's fiscal year 2007 budget supports this proposal by requesting \$74 million for vouchers and debt restructuring. The Administration's proposal and H.R. 5039 are generally quite similar. We support the bill, with certain clarifications, and look forward to working with the subcommittee to address these issues.

One item of concern is that H.R. 5039 would set a maximum tenant contribution of 30 percent for restructured properties. This has been called the overburden provision, as it aims to protect tenants who pay over 30 percent of their incomes toward rent.

Our concern with this provision in H.R. 5039, as written, is that it may have unintended consequences. If the maximum rent provisions remain in H.R. 5039, at a minimum, we strongly recommend that certain controls be put in place that would still protect the currently overburdened. Such provisions could include:

First, allowing restructurings where additional rental assistance funds are required only for residents in units who are overburdened at the time of restructuring, in other words, taking a snapshot of the property at that time. This would protect the currently overburdened, yet not expose the properties in the program to high, open-ended costs if the overburdened leave the properties.

Second, we would suggest limiting the potential beneficiaries to tenants or applicants who don't already have HUD assistance. About a fifth of our units already have Section 8 tenant assistance. We believe that the Section 515 program will, in the long run, be on a stronger footing by preserving multiple sources of tenant assistance.

The Administration applauds Members of Congress for taking this very important first step. We remain committed to protecting tenants and retaining as many properties as we can in the Section 515 program. USDA Rural Development looks forward to working expeditiously with Congress on this important legislation.

Thank you very much.

[The prepared statement of Mr. Davis can be found on page 73 of the appendix.]

Mr. DAVIS OF KENTUCKY. Thank you, Mr. Davis. This is an issue in the rural counties and transitional counties in my home district. We have great personal interest in creating longer-term, affordable housing opportunities increasing that outreach, but also making sure that we have good stewardship of the process.

So one question I'd like to start with is, do you feel that the program that we presented in this legislation gives you all the restructuring tools that you need?

Mr. DAVIS. Yes, Mr. Chairman. We believe that this is an adequate set. There are approximately 10 different tools enumerated in the legislation, and this gives us what we call a tool box that we can choose the least expensive and most effective financial tool in any given situation.

Mr. DAVIS OF KENTUCKY. One related thing which is of some concern to me, just in general, dealing with many Federal agencies, some of the process tools or systemic tools, software in particular, methods of processing information and maintaining accountability are, let's say, somewhat less efficient than we find in the commercial sector, because of the goal to keep costs under control and more money adding value directly.

Could you comment a little bit on the steps that you're going to take to make sure that taxpayer dollars are not paid away in overhead in this program but that we can direct more to the front lines?

Mr. DAVIS. Yes, Mr. Chairman, that's a very good issue. We have been looking very closely at the logistics of what it will take to process up to 10,000 properties for restructuring, and what it really comes down to is that we have to use automation and standardization to get large numbers through on time.

We have prepared standard documents over the past year, and in fact we've closed a number of properties already under our current authorities, so that we have standard documents and we are not handcrafting property by property. We're going to have to do these wholesale, not retail.

The second thing we are doing is automating the process. We're linking the documents together so that, again, we are not reinventing the wheel on every property. I would point out that we took in 4,000 property applications for the restructuring in 30 days, and we did it all on the Web in an automated fashion, and are scoring them automatically. So automation and standardization are really going to be critical to keeping the cost of these transactions down.

Mr. DAVIS OF KENTUCKY. As the legislation moves forward, I'd personally like to see some of the tools that you're using. Hopefully they can be adopted in some of our other agencies, as well, to speed processing and to reduce cost.

Before deferring to other members for some questions, I do want to have you discuss one practical application, a pilot project you alluded to in your testimony in Hinesville, Georgia. There was a pilot program with the use of vouchers for folks who were caught in the prepayment situation.

And one of the, I guess, some would call it six degrees of separation, but it's apparently a very small world circumstance. Many of the soldiers that you mentioned in that, whether you realize it or not, were from the 2nd Brigade Combat Team, the 3rd Infantry Division, who had just come back from Iraq at the first of the year, and they were commanded by a close friend of mine from college.

So, I'd like you to maybe bring the human side of this and how this—the pilot process steps were implemented by the Secretary down there personally, but also if you might comment as well on maybe some things that you saw in the process that could be improved or changed to make it even more effective when we get to an actual rollout.

Mr. DAVIS. Sure, and I thank you for the opportunity, Mr. Chairman. The voucher program is designed to protect tenants when there is a prepayment of the loan. When the loan is prepaid, the rental assistance terminates, the property leaves the program, and

the tenants are effectively on their own. We do not have a conversion voucher program like HUD does, and that is one of the things that H.R. 5039 is addressing.

On a pilot basis, we were given a small amount of money this year to experiment with a voucher program. In order to implement it quickly, without going through the entire regulation process, we worked with HUD on an interagency agreement to essentially use their regulations. In the second week of February, we received notice that a property in Hinesville, Georgia—which is, I believe, where Fort Stewart is—had given notice that they would be prepaying in about 10 days. And in fact, they did prepay their loan. And the residents had 30 days to leave the property or face a doubling of their rents. The area is growing very quickly, and the housing markets are very, very tight. And we have heard that housing markets were affected up to 100 miles in each direction. So the tenants did not have very many options.

The Under Secretary was able to go down there and was able to hand out vouchers to the tenants. They had gotten notice within 2 weeks of their rent increase notices, so they were allowed—they were permitted to stay in their properties, and the rent increase was effectively picked up by the vouchers. This actually was a cost-effective way for us to protect the tenants, so we are pleased with the low cost of it, but also the flexibility. Normally, we would only use vouchers if there were no other way to protect the tenants, such as finding vacant units in other properties of ours or finding other housing subsidies. This is one of those cases where all of the other possibilities we had were not available, and so the vouchers were available just in time. And we thank the committee for their help on this.

The woman who received voucher number one was a service-woman, and there were quite a few servicepeople in this apartment complex.

Mr. DAVIS OF KENTUCKY. One more question that comes to mind just listening to you describe that story, particularly as we're dealing with prepayment situations, one thing that I would not want to see happen, and that I know many of the panel members would feel the same way, is that there be no means for a precipitous eviction, particularly in a situation like that.

Do you foresee any controls from a regulatory perspective? You know, I'm very troubled hearing that soldiers coming back from serving their country would be faced with what might be greed-motivated eviction on the part of a civilian property owner there. But what can—what would you recommend or see as steps to take to prevent such a thing from happening in the future?

Mr. DAVIS. Well, we believe that the more notice, the better. And there is some discussion, and you will hear from the panel coming later; there is some discussion about the timing of the notice period, and this is something we'd like to work with the committee on.

There are two competing forces. The owners, the financiers, and the government want as much notice as possible, because they need to get other financing lined up or buyers, etc. Whereas the longer the tenant notice you have, the tenants live under a cloud

longer, and they become understandably concerned. There can be a lot of anxiety.

I see what happens when these notices go up in the washroom, and we want to minimize any period of anxiety. That's why we really like having the voucher option so that we can say, don't worry about this. You will be taken care of. And that's the most important thing. So having a voucher is number one.

And number two is having a good marketing effort around a reasonable notice period so that the tenant anxiety is minimized.

Mr. DAVIS OF KENTUCKY. Okay. Thank you. The gentleman from Missouri, Mr. Cleaver.

Mr. CLEAVER. Thank you, Mr. Chairman and Mr. Davis, thank you for being here today. With what we have all seen in the Gulf Coast region, I'm wondering what the demand is in that area. We're talking about properties before 1995. How many properties were damaged or destroyed in Hurricanes Katrina and Rita? Do you have any idea?

Mr. DAVIS. The numbers I have seen from FEMA, the single family homes, about 120,000 or so in Louisiana, and I believe 80,000 in Mississippi. That's my recollection from their documents, and I'll get you the right number.

Mr. CLEAVER. No, I'm talking about the 515 program.

Mr. DAVIS. Oh, in the 515 program. We have 13 properties that had significant to total damage. One property was just absolutely destroyed, and we have provided rehabilitation funds for those, and the people who were living in those were able to take their subsidies to other properties.

So, because they were located in rural areas, we were set back farther from the urban areas on the coast. And so our multi-family properties did not bear the brunt of it.

Mr. CLEAVER. That's good. However, I understand that this program was \$20 million or the money that—there's no money in this proposed budget for 515?

Mr. DAVIS. The 515 budget money is spread over a number of accounts. We have \$74 million for Section 515 properties. It's a new budget item so it doesn't often get noticed, but it's called revitalization. It is to cover this bill, and it's \$74 million for repair, rehabilitation, and vouchers.

We get more leverage off of that \$74 million because of the credit and loan provisions in this bill, which allows that funding to go a lot farther. We are essentially using this function for rehabilitation and reconstruction, rather than new construction at the moment.

Mr. CLEAVER. Okay. Thank you. You're right. It doesn't get noticed. The final question, Mr. Chairman, which do you prefer, the 30- or the 90-day notice? Can you say?

Mr. DAVIS. Personally, I would rather address this in the discussion with the committee and the industry groups and the public.

I'm not saying that there's anything secret here, but I'd prefer a longer notice period for the owners but a shorter one for the tenants. And somewhere, and I don't mean to evade the issue, we believe that 90 days is a sufficient period to find buyers or financing when that's necessary.

Mr. CLEAVER. Why?

Mr. DAVIS. I'm sorry. I don't understand. Your question is—

Mr. DAVIS OF KENTUCKY. Would the gentleman yield for just 1 second?

Mr. CLEAVER. Yes.

Mr. DAVIS OF KENTUCKY. I think that what Congressman Cleaver is asking, probably the same question that I'm asking, if I might clarify it. It seems a little paradoxical—would you explain why we want the longer notice for the property owner and a shorter notice for the tenants. If you could clarify what that means in the practical application.

Mr. DAVIS. Oh, I'm sorry. I did not mean a shorter notice period for tenants. Everybody would get the same notice period, but we want to inform the tenants almost immediately to make clear to the tenants that a lot of what is going on will not affect them. They will have vouchers or we will have some way to protect their rent. It's a matter of keeping the anxiety level down.

Mr. CLEAVER. I understand the answer. I disagree with it, but I understand your answer.

Mr. DAVIS. Okay.

Mr. DAVIS OF KENTUCKY. The gentleman from Texas is recognized for 5 minutes.

Mr. NEUGEBAUER. Thank you, Mr. Chairman. I want to start a little bit different line of questioning. Mr. Davis, talk to me a little bit about the voucher program. Is that a temporary voucher until they can make transition housing, or if that goes to a market-based project they can stay there and continue to get voucher rental assistance for what period of time?

Mr. DAVIS. Sure. The voucher program that the Administration had proposed, and is mirrored here, is a tenant-based portable voucher, meaning that they can use it in the property they are originally in, or they can take it to another property, theoretically anywhere in the country, but the rent is limited to where they started out.

It is a 1-year term currently in our demonstration program, but it has a renewal that would be subject to appropriations. This would be like our rental assistance currently when the term ends; it is subject to appropriations to renew that rental assistance, and we would be renewing these vouchers under this bill the same way.

Mr. NEUGEBAUER. Because Secretary Jackson comes over a number of times a month, and he says over and over and over again, that this voucher program is squeezing the life out of the housing program in this country. What kind of things do we look for—in other words, if you go—let's say that you go to a voucher program, how are you going to handle the competition between the funds for building new housing in rural America and offering the voucher assistance at the same time out of the same budget?

Mr. DAVIS. Well, that's a good question. It is obviously subject to appropriations as is new construction, and there is always tension in a tight budget atmosphere. We have always placed the highest priority on renewing current assistance and protecting tenants who are currently there. That is throughout this bill our number one principle—protecting the current tenants in their markets or in their properties.

The prepayment vouchers in this proposal are to cover a portion of the portfolio that is expected to prepay, which is about 10 per-

cent of the portfolio. It is a small part of a much larger problem, which is keeping as many properties in the program as possible. We are not looking to voucher out the 515 program at all. This is just a small component.

Mr. NEUGEBAUER. And talk to me a little bit about—I think you said you expect about 10 percent prepayment if this legislation is passed. How will that impact the program? I mean—

Mr. DAVIS. The total portfolio is about 17,000 properties, so 10 percent is around 1,700 properties, and that's about 50,000 units. This group is mostly in high cost areas, although they can appear anywhere, but we have a lot of properties that were in rural areas 30 years ago, and the cities grew. They are now in high-cost suburbs. We have properties that are now in resort areas or just very nice areas that people are moving to and have become high-cost areas. These properties are drawing a lot of the resources out of the rest of the portfolio.

We see the voucher program as solving one part of the portfolio's problems.

Mr. NEUGEBAUER. One of the things—I have a very rural district also—and one of the things that mayors and county judges call me all the time about is, you know, what can we do to get more affordable housing? And I want to compliment—some of your folks in Texas have always agreed to go and meet with the community leaders on some of the options that are available to them.

As you move forward, do you see this program threatening any new build opportunities for the future? Because some communities are currently underserved and don't have existing housing stock in their community, and so obviously we need to make sure we have funds for new program opportunities that would be needed.

Mr. DAVIS. I thank you for asking about that. We have two loan programs for new construction, Section 515 and Section 538, which is a guaranteed loan program. I'm very reluctant to pit them against each other because it does neither program any good to have them fighting against each other. I'd prefer to view them separately.

For the 515 portfolio, the best advantage we get for the dollar is repair and rehabilitation right now. We can repair a unit for, on average, \$20,000 a unit, whereas a new unit would cost \$85,000 and up. So, we see the current role for 515 right now as a repair and replacement program. The Section 538 program has advantages of very high leverage and the ability to draw a lot of outside money. We are building 10 times the units in the Section 538 program per budget authority dollar as we are in 515. They serve the same constituencies in different ways. We are interested in looking at the 538 program to see how that might be more useful for particularly very, very low income people. But we want to build two strong programs. We don't want to get the two competing against each other.

Mr. NEUGEBAUER. My time has expired, Mr. Chairman. Thank you.

Mr. DAVIS OF KENTUCKY. The gentleman's time has expired. Before moving on, I'd like to return to the tenant-property owner question here. The economics are, I think, very straightforward on using market-based principles to leverage the value of the property

and maintain a quality living environment. And I appreciate those very much. I think it's going to be good for the American taxpayer, good for the enhancement of our affordable housing program.

But coming back to the timeframes of notification both of prepayment and also tenant notification, what I was wondering if you could take a couple of minutes and do before the ranking member speaks, is walk through that process from the time a decision to prepay under the proposed legislation would work, and those notifications, so that we can understand clearly how the tenants' rights, if you will, are protected; that they have a fair and reasonable time of notification while the owner is preparing for his business transaction.

Mr. DAVIS. If I could ask just one moment while I turn to the right pages here.

Mr. DAVIS OF KENTUCKY. That's without objection.

Mr. DAVIS. There are several different notice periods, and I just want to keep them straight. There is notice to the tenants to inform them that a prepayment is occurring. And we currently have a process whereby the property owners must notify us, but they also notify the tenants, and this is where they post the notices in the buildings.

There is a separate track which is a notice that the owner is giving for a possible sale of the property. This is in the "Prepayment of Section 515, Multi-Family, Housing Loans Notice of Prepayment and Sale" section of the bill.

Let me deal with the sale issue first. The owner is not permitted to simply prepay. We see here a notification period that gives potential buyers of that property who would be buying for affordable housing purposes the time to put in a bid to buy that property and keep it affordable. Obviously, it takes a certain amount of time to find a buyer, and for those buyers to make sure they have their financing lined up and so forth. And so the 90 days that I have been talking about beforehand was this 90 days to provide for a sale.

There is a second notice, on the next page, the small paragraph (i), which is a notification at the same time to the tenants that vouchers will be available. What we have found in our pilot program so far is that the notifications that had been used—I don't want to say they were overly legalistic, but they used language that was correct, but had the tendency to scare people, frankly.

We have prepared a series of brochures and essentially a marketing program whereby every time we get one of these notices, we immediately send our field office staff out to the property. They meet with the tenants and take their questions, provide answers, and talk them through the process.

Our concern is not that there be just a legalistic trading of notices by certified mail, but that human beings meet and sit down in the property and work everybody through the process. That is a separate issue from how long should the period be. Some people feel that once owners have prepaid, they should be able to take their money and go. We think that—I think it's either 75 days or 90 days that's in here, is a reasonable accommodation for affordability, and we have no objection to that time period either.

Mr. DAVIS. Okay. I appreciate the clarification. The thing I was particularly interested in was the human factor on this to make

sure that the tenants are treated in a fair and just way. You know, in a private commercial setting, the owner would have certainly a great freedom contractually to use his property as he saw fit. However, the key in respect of property rights is the relationship of our taxpayer dollars being invested in that, and I want to make sure that they are well cared for and taken care of.

The Ranking Member, Ms. Waters from California, has joined us, and without objection, I would like to recognize her to make her opening statement.

Ms. WATERS. Thank you very much, Mr. Chairman. I appreciate the fact that Chairman Ney and others worked to make sure we are holding this hearing so that we could address the problems of our rural areas. I'd like to thank all who are here today.

As many of you know, Mr. Ney and I participated in a hearing in my district that focused on the impact of the Community Development Block Grant on communities such as the ones that I represent in Los Angeles. The reason I'm talking about that particular hearing is because we mentioned that just as we have problems in urban areas, there are problems in our rural communities that are not being addressed. The people who live in the rural communities are situated different geographically, but they have housing and community development problems that must be confronted just like the rest of the country.

One of the most pressing needs recognized by the sponsors of the bill is a shortage of quality affordable housing in the Nation's rural areas. In many parts of the country, not only is there an inadequate supply of affordable housing, but the housing is aging. The average age of the Section 515 units is, I'm told, 28 years old. In many rural communities, grants are known to have traditionally been used to finance single and multi-family housing. The Section 515 program has assisted approximately 250,000 people, most of whom are poor. What other criteria do we need to support a housing program? I believe that it is enough that there be just one family, one person in need of housing in rural America, there's a real need for housing, one that mirrors the housing needs in non-rural areas. However, without the reform and revitalization measures contained in H.R. 5039, we will not be able to deal with the needs of this community. They need repairs. The properties are old. Many of the owners are paying off their properties. Where will the tenants go? All of these questions are questions and concerns that we all must share.

Today we have an opportunity to send a message of hope to rural America by hearing testimony that will enable us to consider the appropriate measures to address the Nation's rural housing needs. I am sure that no one thought that we would see a proposal that would eliminate Section 515 altogether. If we really want to address the housing needs of our rural citizens, many of whom again, are poor, disabled, and elderly, we can start today by considering how to improve existing program efforts to assist them.

I thank you for the opportunity to share this statement with you. It will be submitted for the record. And I look forward to hearing the rest of the testimony here today.

Thank you.

Mr. DAVIS OF KENTUCKY. The gentleman from Missouri.

Mr. CLEAVER. Thank you, Mr. Chairman. I've been put back in my place since the ranking member has come, so I'm just a regular person. I was a big shot for about 30 minutes, and I appreciate Ranking Member Waters coming in late. That is my first time actually sitting at the big table, and I just thought I'd share.

Let me go a little further, though. I want to revisit the question I asked you earlier is that, you know, your answer—what is the amount of funding in the proposed budget from the President this year?

Mr. DAVIS. The President has proposed \$74 million for the Section 515 revitalization program—

Mr. CLEAVER. Okay.

Mr. DAVIS. In addition to rental assistance and the 538 program.

Mr. CLEAVER. Okay. Last year it was \$100 million.

Mr. DAVIS. Correct.

Mr. CLEAVER. So we've got a 26 percent reduction.

Mr. DAVIS. We have a reduction in budget authority but an increase in loan authority.

Mr. CLEAVER. You said it's a loan fund?

Mr. DAVIS. If I could just expand on budget authority versus loan authority. Budget authority supports a certain amount of leverage to get a higher amount of loans. For example, in the 515 loan program, each budget authority dollar can be leveraged basically two to one to get new construction loans. So, \$50 million of budget authority would produce \$100 million worth of loans. We have a better, much more advantageous leverage rate for repairs and revitalization, so that \$74 million will go much, much farther, into the hundreds of millions of dollars in loan authority.

Mr. CLEAVER. Okay. Thank you. I understand. You said the \$74 million is going to be spread over a number of other line items.

Mr. DAVIS. It will cover both vouchers and restructurings, and those restructurings could take different forms under this bill. If this bill is passed, we will have authority to do more types of recapitalizations of properties.

Mr. CLEAVER. So let me repeat what I—so the President did not zero out the 515 program?

Mr. DAVIS. The President has proposed using the money for 515 revitalization repairs, not direct 515 new construction. For new construction, we have increased, and even doubled, our request for 538 new construction. Section 538 is multi-family guaranteed loans.

Mr. CLEAVER. Okay. You turned a little—you painted in a little tiny spot. The President, is the question.

Mr. DAVIS. Yes.

Mr. CLEAVER. The President did not zero out new construction in the 515 program? It's a question.

Mr. DAVIS. There is no request for 515 new construction loan money. There is a request for the 515 program. The question is often broader than new construction. But, no, there is no new construction for the 515 program. That has been moved into 538 and with repair of the 515 program.

Mr. CLEAVER. Are you all right with that?

Mr. DAVIS. I believe that this is the best use of our tight budget resources right now and that this gives us more leverage and more

outside money. We will produce more housing and protect and preserve more housing under this approach. I really believe that.

Mr. CLEAVER. I can tell.

Mr. DAVIS OF KENTUCKY. The gentlewoman from California.

Ms. WATERS. Yes. I guess there is some confusion about income limit. H.R. 5039 and the Administration's proposal related to income limits for rural housing tenants are inconsistent.

The bill sets the income limit at 30 percent for both the revitalization and the tenant protection voucher programs. The Administration does not spell out what it supports with regard to income limits, but rather suggests that H.R. 5039 is likely to greatly expand the cost of preserving these properties.

What does this mean? How does it tie to the 30 percent income limit in the bill? Are you suggesting that the 30 percent income limit would prevent preservation of the rural housing start? And how did you arrive at this conclusion?

Mr. DAVIS. Yes. And thank you, that is an issue that we want to make sure is handled correctly, because we are afraid that there might be unintended consequences. I'll describe an example.

H.R. 5039 proposes covering what are called the overburdened tenants, those paying more than 30 percent of their income. And we believe that protecting the overburdened tenants is something that is a worthy objective and is something that we had proposed in our voucher and prepayment policy for last year.

In fact, the voucher program that we're doing now is essentially holding harmless the overburdened in the property. So for the first time, they are getting protected against rent increases.

What this bill does is extend that in an open-ended way to restructurings also. Our concern is probably best given by an example. Say you have an overburdened tenant who is making about \$10,000 a year. It's not a lot of money, but they will be held at 30 percent of their income.

If that person were to move out and were replaced with a person making zero income, then the property would be burdened with having to cover not just an overburdened person, but a person with no income. That extra cost would either be put on the rest of the tenants or put onto the property. It would create a burden that wasn't intended when the original plan was done.

We want to be able to work with the committee on language to make sure that planning could be done at the beginning, but also making sure that we aren't creating a new entitlement program, beyond what is just protecting the current overburdened. This is something that we think that we can work with the committee on language to cover.

Ms. WATERS. Your example is one that helps me to understand what you are trying to do. But if someone moves into a unit with no income, you're saying there's a need to spread that cost in some way among the other tenants. Is there another way of dealing with that?

Mr. DAVIS. Well, there are generically I guess three ways of handling it. Either we could put a new rental assistance unit on the property, but that would mean that we would have to commit to future years appropriation, which we can't do. Or we would have to spread it across the rest of the property and raise everybody

else's rents to hold that one unit harmless, or somehow take it out of the property's financials, which may not be available.

Ms. WATERS. Are any of these units marketable?

Mr. DAVIS. These are all Section 515 units, so they are covered by the 515 basic rent levels. But these are units that don't have rental assistance or Section 8 on them. We would essentially be creating a new class of subsidy which would cover overburdened people. But if that status changes, then it changes the financial status of the transaction.

Mr. DAVIS OF KENTUCKY. All right. Let me just say that perhaps one of the co-authors of H.R. 5039 can talk about what their preference is in dealing with this kind of problem. But of course, if there are people with no income, we would certainly want them to be covered, and we certainly don't want existing tenants to be burdened with the cost of covering those who have no income.

Mr. DAVIS. Yes.

Ms. WATERS. So I don't know whether you work out something new, or how you do it. The fact of the matter is that would have to be dealt with.

Mr. DAVIS. We understand this, and we welcome working with the committee on how this can be set up.

Ms. WATERS. Thank you.

Mr. DAVIS OF KENTUCKY. I thank the gentlewoman. I appreciate you coming, Mr. Davis, to share today. I'm sure there will be many other questions that will come up, but in the interest of time and in deference to the people who have come from rural housing authorities and the operators to share.

The Chair notes that some members may have additional questions for the panel which they may submit in writing. Without objection, the hearing record will remain open for 30 days for members to submit written questions to these witnesses and to place their responses in the record.

Without any objection, thank you for your time. You're dismissed, and we'd like to ask the second panel—our second panel this afternoon includes Mr. Gideon Anders, executive director of the National Housing Law Project; Mr. James N. Arbury, senior vice president of government affairs, the National Multi Housing Council, also testifying on behalf of the National Apartment Association; Mr. Thomas Carew, Red River director of Frontier Housing from Kentucky; Mr. Moises Loza, executive director of the Housing Assistance Council; Mr. Robert Rapoza, executive secretary of the National Rural Housing Coalition; Mr. Robert Rice, Jr., president of the Council for Affordable and Rural Housing; and Mr. Charles Wehrwein, senior vice president of Mercy Housing, Inc.

Without objection, your written statements will be made part of the record. And you will each be recognized for a 5-minute summary of your testimony.

Gideon Anders is the executive director of the National Housing Law Project in Oakland, California, and this organization engages in public policy advocacy and researches the impact of housing policy on the poor.

You are recognized for 5 minutes, Mr. Anders.

**STATEMENT OF GIDEON ANDERS, EXECUTIVE DIRECTOR,  
NATIONAL HOUSING LAW PROJECT**

Mr. ANDERS. Thank you, Mr. Davis. I just want to point out that I have worked on rural housing preservation issues for 28 years, and that the primary principle that guides our preservation work is the need to protect federally assisted residents against displacement from their homes.

I would like to quickly and straightforwardly address one of the questions you have had about the displacement of residents.

Our primary concern with H.R. 5039, Mr. Chairman, is the fact that it, in fact, would potentially displace 110,000 people, of which 50 percent are elderly and 10 percent are people with disabilities. We are extremely concerned about that. It puts the residents at the pleasure of the Congressional budget process, and at the pleasure of the Administration not potentially asking for sufficient funds to protect against displacement. We do not believe that should be happening.

In 2003, Chairman Ney introduced a bill that made the existence of the vouchers conditioned upon the availability of funding and essentially conditioned the right to prepay upon the availability of funding for the voucher program. We think that is a critical element.

If that does not happen in this bill, we are going to have a situation where legislation allows owners to prepay their loans, and displace potentially up to 110,000 people because we did not have a voucher program in place, or because the Administration misconstrued or miscalculated the number of units that owners are actually going to be prepaying.

We are also concerned, Mr. Chairman, that the 90-day period that is in the bill, which allows residents to move and, potentially, allows people to structure deals whereby the projects are sold to nonprofit and public institutions, is simply inadequate.

Mr. Chuck Wehrwein will be talking about this later, but I do not know of a single institution that can take a multimillion dollar project and find the financing in 90 days to transfer that project from one entity to another and to retain the affordable nature of that project. It simply isn't possible. We need a longer period of time to make those deals work.

More specifically, Mr. Chairman, I've got issues with respect to the voucher program as it is being proposed. First of all, there is an intent in the program to create a right for the residents to remain in their units. Essentially the voucher is to cover the cost of the unit after it is converted to market rate. Unfortunately, the way the bill is drafted, that is not happening. The bill, as it is currently drafted, essentially precludes owners from discriminating against voucher holders, by virtue of the fact that they are voucher holders. It does not give residents a right to stay in the unit.

So, that means that if a landlord doesn't like the resident with a voucher, he or she can force the resident to move to another place, and they are going to have to move out of the unit in which they are currently residing.

Again, 50 percent of the people who are living in these projects are elderly people. They are people over 62 years of age. Their income is somewhere between \$8,000 and \$10,000 a year. They are

simply not going to have another place to which they can move very readily.

The other problem with a voucher, as it is currently set up, is that it is based upon the market rate of the unit in which the current resident is living. Unfortunately, that may not work if there is no affordable, decent housing in that same community. If the voucher holder is required to move to another community where the rents are higher, they are not going to be able to move and use that voucher to move to other communities. And they are not going to be able to use that voucher to buy a home, as is contemplated in H.R. 5039.

We are very concerned that many of the issues that this committee and Congress has previously dealt with, with respect to the HUD programs, are simply left out of H.R. 5039. Residents are not given the right to remain in the units. The vouchers are not set at the same income level. It does not protect residents against hardships. In the HUD Section 8 voucher program, if a family's income is reduced by more than 15 percent, there is a possibility for the voucher subsidy to be increased. There is no comparable provision in the current bill.

The bill does not address the need for subsidy increases in rent and utility cost increases as they come downline. In the HUD Section 8 program, when owners seek to opt out of the program, they have to give a 1-year notice. We are here offering a 90-day notice.

The program does not have a viable mechanism for transferring any of the units to the nonprofit and public sector. There is a prohibition upon the owner from actually doing a deal within 75 days. There is no requirement that the owner negotiate with anyone in good faith or that, in fact, anybody be given priority.

There is no funding for new construction. As I think has been pointed out by the Congressman from Missouri, the Administration is asking for zero money for section 515 housing. It is unfortunate; that means that there is not going to be any financing, in fact, to transfer these units within the 515 program.

[The prepared statement of Mr. Anders can be found on page 45 of the appendix.]

Mr. DAVIS OF KENTUCKY. I appreciate your comments, Mr. Anders. Your time has expired. And I would like to come back and revisit that specifically when we get the questions and talk in a little bit more detail about this.

Mr. ANDERS. Sure.

Mr. DAVIS OF KENTUCKY. Thank you very much. Were we to have a smaller witness panel, we could continue indefinitely, but we don't want the lateness of the hour to keep everybody.

Next is Mr. Jim Arbury of the National Multi Housing Council. The members of the Washington, D.C.-based council are active in all aspects of the rental housing business and share an interest in legislative and regulatory issues affecting the apartment industry, as well as promoting apartment living.

Mr. Arbury, you are recognized for 5 minutes.

**STATEMENT OF JAMES N. ARBURY, SENIOR VICE PRESIDENT  
OF GOVERNMENT AFFAIRS, NATIONAL MULTI HOUSING  
COUNCIL, AND NATIONAL APARTMENT ASSOCIATION**

Mr. ARBURY. Thank you, Congressman Davis, and Congressman Cleaver.

I'm Jim Arbury and I am the senior vice president of government affairs for the National Multi Housing Council/ National Apartment Association Joint Legislative Committee. Our members own or manage more than 6 million apartments around the country and we have over 50,000 members.

I am pleased to address the views and opinions of our membership on H.R. 5039. We have a variety of members who are involved in this program in one form or another. Apartment owners and managers are committed to providing safe, decent, affordable rental housing in both urban and rural areas.

We advocate a stronger, more responsive rural housing service preservation program. But we must be fair to both residents and owners of this critical housing stock in order to preserve it. It has been mentioned that a lot of the stock is older and in need of repair. The committee is meeting today to see what kind of legislation is needed to preserve the nearly 15,000 properties and 460,000 units in the Rural Housing Service program.

In Missouri, there are 858 of these properties with over 19,000 units. And in Kentucky, there are 456 properties with 12,280 units. If you look at this type of property, it's 30 or 40 units on average. It's not a big apartment property. These types of properties are very difficult to pencil out in terms of economic viability. And that's why I think there is great stress in the program at the moment.

H.R. 5039 can potentially help preserve as much of this housing as decent and affordable, but it is much easier to say the words "decent, affordable housing" than it is to actually put it into practice, as we've seen, because of all the financial stress.

And the other problem is that our national housing policy is far too unbalanced in favor of single family home ownership. The imbalance makes it very difficult to find the resources to build and maintain decent affordable rental housing for lower income Americans.

Raising the home ownership rate through a variety of programs such as zero down and interest-only loans will not solve our Nation's affordable housing problem, and the resulting foreclosures will make it worse. In fact, foreclosures this quarter versus the same quarter a year ago are up 77 percent.

Tightening the screws on the Section 8 program and mismanaging the housing crisis caused by last year's hurricanes will only make matters worse in the future with respect to the supply of affordable rental housing. For long term viability, the debt needs to be restructured in the 515 program and a dependable flow of income established.

Since it appears that between 7,900 and maybe almost 12,000 of the properties need to be restructured, we have some question whether the Rural Housing Administration is equipped to do this. We urge you to carefully examine the large task at hand to make sure that any legislation can be implemented properly.

On the income side, rental assistance continues to be a growing problem because of uncontrollable expenses, such as energy, utility costs, property taxes, other local taxes and fees, and insurance. It's tough for a property owner to assume that there will be any type of viable subsidized voucher system in view of recent events with Section 8, and with the FEMA hurricane voucher system.

So, it's hard for a property owner to figure out what kind of vouchers will still be in place 5- 10 years from now.

We do have concerns about the wording in the bill on the 90-day notification period. When an owner seeks to prepay a 515 loan or sell the property, we would urge that the notification period begin when the owner notifies residents and the RHS of its intent to prepay or sell.

Finally, we are concerned about the sale restrictions and prohibitions on the sale of the property. These clearly need to be debated and resolved as you move forward with this legislation.

We are here today as an advocate for a stronger, more responsive Rural Housing Service preservation assistance program that offers a balanced approach, and which is fair to the residents and owner-managers of rural multifamily rental housing.

I thank you, and I would be happy to answer any questions.

[The prepared statement of Mr. Arbury can be found on page 55 of the appendix.]

Mr. DAVIS OF KENTUCKY. Thank you, Mr. Arbury.

Mr. Tom Carew, director of the Red River, Kentucky Office of Frontier Housing. Frontier Housing focuses on expanding affordable housing opportunities for low-income rural families. And we are grateful to have someone from the great Commonwealth of Kentucky here.

Mr. Carew, you are recognized for 5 minutes.

**STATEMENT OF THOMAS CAREW, RED RIVER DIRECTOR,  
FRONTIER HOUSING, INC.**

Mr. CAREW. Thank you, Mr. Chairman. Frontier Housing is a non-profit corporation providing housing solutions for low income Kentuckians since 1974. We serve an area of nine counties in northeastern, Appalachian Kentucky. Five of these counties, unfortunately, are listed in the top 100 poorest counties in the United States. This area includes two Congressional Districts, the fourth, Mr. Davis', and the fifth. Poverty rates range from a high of 45.4 percent to a low of 19.4 percent in the nine counties.

House Resolution 5039 addresses certain issues affecting the 515 Rural Rental Program of the United States Department of Agriculture's Rural Housing Service, formerly known as the Farmer's Home Administration. The 515 program has financed approximately 12,000 units in Kentucky and approximately 450 projects.

Many of these units are in our service area, and they provide decent housing for the poorest of the poor. H.R. 5039 addresses the issue of an owner's right to prepay the Rural Housing Service on developments financed prior to December 15th of 1989.

Secondly, the bill puts forth a program that would enhance the revitalization of the majority of Section 515 developments on a voluntary basis.

We applaud the provisions of the bill, which create financing mechanisms which will enable the revitalization of many units in the 515 stock.

In my previous position at the Commonwealth of Kentucky's Housing Finance Agency, Kentucky Housing Corporation, we found it very difficult to assist a developer wishing to revitalize a 515 project. The existing RHS regulations essentially prohibited other financial partners from participating in a financial restructuring and an injection of new capital to rehabilitate an older project.

This bill includes provisions for the following financial enhancements: reduction and elimination of interest on the loan; partial or full deferral of payments; forgiveness of loans; subordination of loans; reamortization; and grants.

In return for the government's new investment, the owners would agree to new property use restrictions for a period of not less than 20 years. These financial enhancements will enable other partners, such as housing finance agencies, to participate in the revitalization of a project, thus making better housing available for very low income Kentuckians.

The bill also addresses the prepayment of projects financed prior to December 15, 1989. Recent settlements in the U.S. Court of Claims in favor of project owners have raised the concern of many as to the cost of keeping the pre-1989 units in the Section 515 program.

As many of you know, the RHS, over the past 12 or so years, has drastically reduced the funds available to construct new 515 projects to the point where there is little to no new construction. In fact, there haven't been any new 515's in Kentucky for several years now.

This raises the concern that if we are to lose the thousands of affordable units across America, how will they be replaced? Does it make sense to give up the units we have now for an investment we made years ago, and pay today's prices to replace the units?

The cost to replace these units surely will cost more than to keep them in the program. What funding is on the horizon to replace these units at affordable rents? Generally speaking, the tools we have today, tax credits, HOME, the affordable housing program of the Federal Home Loan banks, State trust funds and other State funds, will not begin to be able to replace the affordable units we might lose in the 515 program. No other national program—not the 538 program—can match the 50-year, 1 percent interest rate, the lowest rate the 515 program could go. We are not replacing this new construction program with anything that matches it. The 538 is a rental guarantee program, so I can go to a bank and get a loan at market rate, but I can't get it at 1 percent on a 50-year term. So, the two really are apples and oranges.

The bill does provide a mechanism for housing vouchers for tenants who would be displaced. There are some technical corrections that should be made in the bill to clarify when a tenant is able to receive a voucher. Tenants should be eligible if they are residents on the date the owner notifies the tenant of their intention to pre-pay.

There are some budgetary questions related to the vouchers. How long will the vouchers last? These questions should be addressed before the bill is finalized.

I want to raise the issue of should the number of units coming offline, as a result of prepayment, be tied to the number of vouchers in the budget? If we lose 1,000 units due to prepayment, should we have 1,000 vouchers available? I think that is a real concern of many of us.

Finally, I want to remind us why the 515 program was created. It was created to provide safe, decent housing for the poorest rural Americans. If we are unable to preserve the units we have, then we should look at a mechanism to replace the units we lose. This bill provides some excellent tools to revitalize those units which remain in the program, and provides a prepayment mechanism for those developers looking to leave the program.

I would respectfully challenge the committee to create a new program or adequately fund the Section 515 program, to finance the construction of replacement units.

Mr. Chairman, members of the committee, I thank you for this opportunity to be here. I applaud your work on behalf of the poorest of the poor, both in Kentucky and in America.

[The prepared statement of Mr. Carew can be found on page 67 of the appendix.]

Mr. DAVIS OF KENTUCKY. Thank you, Mr. Carew.

Moises Loza is the executive director of the Housing Assistance Council. The council is headquartered in Washington, D.C. It assists with the development of both single- and multi-family affordable housing rural communities.

Mr. Loza, you are recognized for 5 minutes for your opening statement.

**STATEMENT OF MOISES LOZA, EXECUTIVE DIRECTOR,  
HOUSING ASSISTANCE COUNCIL**

Mr. LOZA. Thank you, Mr. Davis and Mr. Cleaver.

The Housing Assistance Council is a national nonprofit corporation dedicated to improving housing conditions for rural, low income Americans. I would like to express our appreciation for all of the work that has gone into developing this particular bill.

The Housing Assistance Council views the Saving America's Rural Housing Act of 2006 as a step toward resolving serious issues regarding the availability of decent, affordable rental housing for low income rural Americans.

The nearly 5 million rural households, about a quarter of the total, who rent their homes are some of the worst housing problems in the United States. Housing costs are their most significant problem. Rural renters are twice as likely as owners to live in physically substandard housing. Approximately 12 percent of non-metro renters live in either moderately or severely inadequate housing. For minorities, the rate rises to 18 percent.

The Department of Agriculture's rural development 515 Rural Rental Housing Program, particularly when coupled with the Section 521 Rental Assistance Program, provides decent, affordable homes for rural renters.

The average income for a Section 515 household is \$9,785. For those receiving Section 521, the average is \$7,836. The majority of Section 515 tenants are elderly or disabled, and 94 percent of them have very low incomes. That is, they earn about half of the median income in their area.

Our primary concern is ensuring the availability of decent, affordable rental homes for current and future tenants. If ELIPHA is to be repealed for pre-1989 properties, we believe that tenants will be best protected by permitting payment if vouchers are available or if sufficient, decent available rental housing in the market is affordable to Section 515 tenants.

HAC supports the inclusion of vouchers in this bill. First, vouchers should be available to tenants who live in the property on the date the owners give notice to the tenants, not only to those who live there on the date of prepayment, as is proposed in the bill. This change would enable tenants to explore alternative housing, and to take advantage of available opportunities before prepayment occurs.

The bill seems to require prepaying property owners to accept vouchers as they are under HUD's market program. HAC supports this intent. Provisions that vouchers may be used, may be provided imply an option rather than a requirement. To indicate clearly that USDA tenants have the same rights as HUD tenants, this bill could use the same language as HUD's Section 8.

Because USDA vouchers could become costly if tenants move from relatively inexpensive small towns to pricey cities, unrestricted portability may not be the best choice for the USDA voucher program.

We would like to suggest, however, that the bill make an exception to the value limit for elderly and disabled tenants, who move to expensive areas to be close to family members, essential services, or other support systems.

The bill tries to create two rights of first refusal, an idea that we support. The language should be clarified and funding be provided to assist entities exercising these rights.

The bill provides that for the first 75 days after notifying USDA that it wants to prepay, an owner could sell only to a purchaser who would accept 20-year use restrictions. The owner, however, is not required to bargain. We recommend revising the bill's language to establish a clear right of first refusal for a purchaser that would accept a 20-year use restriction.

The bill also attempts to provide a right of first refusal for tenants in the revitalization context. It would give an owner the option to offer the property to the tenants for purchase as a cooperative or condominium in conjunction with revitalization. Again, we recommend establishing a clear right of first refusal.

Finally, Housing Assistance Council observes that rural America needs not only preservation of existing decent, affordable rental housing units, but also production of new units.

USDA's budget proposal for 2007 proposes to finance construction of new rural rental units through the Section 538 rental guaranteed loan program. Section 538, however, serves a higher income population than Section 515.

Rent subsidies also cannot end rural America's rental housing problems. Often rural areas do not have enough decent, affordable rental units available. HAC encourages the subcommittee to support increased annual appropriations for the Section 515 program and/or the creation of a new rural rental production program.

Thank you.

[The prepared statement of Mr. Loza can be found on page 81 of the appendix.]

Mr. DAVIS OF KENTUCKY. Thank you, Mr. Loza.

Bob Rapoza is president of Rapoza Associates, located in Washington, D.C. His firm specializes in providing legislative analysis related to the development of low income housing needs for rural areas, as well as other issues facing rural communities.

Mr. Rapoza is testifying today on behalf of the National Rural Housing Coalition, and is recognized for 5 minutes for a summary of his opening statement.

**STATEMENT OF ROBERT A. RAPOZA, EXECUTIVE SECRETARY,  
NATIONAL RURAL HOUSING COALITION**

Mr. RAPOZA. Thank you, Mr. Chairman. I am Bob Rapoza, and I am representing the National Rural Housing Coalition, a national membership organization that advocates for improved Federal housing and community development policies.

We would like to thank you and the committee today for sponsoring H.R. 5039, and for focusing attention on the importance of preserving Section 515 housing.

We thank the Section 515 effort is a great success. Over 500,000 families across the country with low incomes, most of whom are senior citizens or disabled, have decent, affordable housing because of Section 515. In most rural areas, the 515 development is the only affordable housing in town.

As the chart included in our statement shows, there has been a substantial fall-off in Section 515 funding. This has had two regrettable results. The first result is that there's very little new construction under 515. The second result is that the financing incentives for long term use for Section 515 has fallen from about \$25,000,000 to less than \$5,000,000 in fiscal year 2006.

To be clear, as summarized here, the present budget does not request funding for Section 515. Not a penny. Yet 515, at the moment, is the only Federal authorized funding source to revitalize and to restructure 515 developments.

Because of this funding shortfall, Section 515 developments have been under funded, and the project owners have had limited access to incentives for long term use and for subsequent financing to revitalize and restore their projects. These incentives were first authorized by the Congress in 1987, after a rash of prepayments and displacements of the families who were living in 515 developments who did not have access to help to gain affordable housing nor did they have access to subsidies for that housing.

In 2004, the Agriculture Department released an important study of the 515 portfolio. They found that 10 percent of the portfolio was in so-called "hot markets" where the developments could be converted to some other use, including market-rate housing, but that the balance of the portfolios was located in communities where

prepayment didn't seem to be a very good option for the project, and the best use of the project was for low income housing.

In these cases, there was a need for additional funding to ensure the adequate operation of the projects. The average age of a 515 development is 26 years, and the report projected the cost to renovate and/or restore the 515 portfolio at \$2.6 billion over a 20-year period.

H.R. 5039 addresses these findings by permitting the prepayment of certain 515 developments by establishing a voucher program for those displaced and a restructuring fund to revitalize the developments.

This legislation is a significant improvement over some of the drafts we have seen over the last 6 months. The legislation does limit the number of developments eligible for prepayment. It establishes a minimum use restriction for structured developments, such that a favorable rent structure for those developments with a stay in place voucher.

In addition, we appreciate the provisions on the right of first refusal and tenant notification, and would like to work with the committee to improve these provisions. In addition to that, we also recommend that when the bill is marked up, that the committee include a dollar authorization for vouchers and restructuring aid.

Our basic concern is with the overall framework of the legislation. If this bill becomes law, it is possible that low income families will be displaced without other affordable housing options and without vouchers.

It is true that vouchers and affordable housing could be available in which a prepaid 515 is located, but it is also true that it could not be.

In the 2006 appropriations bill, Congress provided \$16 million for vouchers and \$9 million for restructuring demonstration program. The Agriculture Department has already put some of those vouchers to use, and the NOFA on restructuring aid was issued last months.

We urge the Congress to take a careful look at the experience in the field with these funds. We know a good deal about the Section 515 portfolio, but what we don't know is how the owners, the tenants, and the rural housing markets will react to these resources. It could be, as some have contended, that restructuring funding will reduce the incentive to prepay loans, and we can preserve more of the 515 portfolio. We think it would be useful to see how the demonstration works before final action on this legislation.

[The prepared statement of Mr. Rapoza can be found on page 89 of the appendix.]

Mr. DAVIS OF KENTUCKY. Thank you, Mr. Rapoza. Your time has expired, and we will continue with this discussion in a moment.

Next is Mr. Bob Rice, president of Crest Management Real Estate Company, based in Frankenmuth, Michigan, specializing in management of affordable multifamily housing.

Mr. Rice is testifying today as the president of the Council for Affordable and Rural Housing, and is recognized for 5 minutes for a summary of his statement.

**STATEMENT OF ROBERT L. RICE, JR., PRESIDENT, COUNCIL  
FOR AFFORDABLE AND RURAL HOUSING**

Mr. RICE. Thank you. I am Robert Rice, president of Crest Realty, located in Frankenmuth, Michigan. I have been involved with the management of affordable rural housing for 30 years. I currently am a hands-on manager of 27 Section 515 properties, which amount to about 450 units.

I am appearing here in my capacity as president of the Council for Affordable and Rural Housing. We call it "CARH."

CARH is a national organization based in Alexandria, Virginia. It's comprised of for-profit and nonprofit developers, managers, owners, syndicators, public agencies, and others interested and involved in providing affordable housing to low income families in rural areas.

On behalf of our members, I thank you, Mr. Chairman, for asking CARH to testify today on H.R. 5039, "Saving America's Rural Housing Act of 2006."

The major Federal program to subsidize rental housing over the last 40 years has been the Section 515 program. Over the years, the Rental Housing Service has tried to balance the need for adequate rents to support a project with the reality that the 515 subsidy is too shallow to serve the lowest income ranges.

Although rental assistance, where it is available, is very helpful, RHS has attempted to stretch limited budget resources for that program by keeping rents lower than prudent for the long term viability of the projects. Rents and rental assistance system-wide have been held down too far for too long, creating a crisis in resources.

I have an example of two projects that I manage which are 30 miles apart from each other. Project A is a 515 loan with Section 8 subsidy. Project B has a 515 loan with Rural Housing Service rental assistance. The rents for the two projects—Project A's rent is \$100 a month more because when I go in for my budgets, I am not held down on the HUD ones, because they are not spending their own subsidy.

We think that has caused a problem and it makes it so there is not enough money to do a lot of the things that we would like to do with the project, maintenance-wise.

Coupled with the fact that owners, by and large, have not been allowed out of the program to recapitalize, a situation has been created that we refer to as a "toll road with no exit."

Two years ago, RHS conducted a comprehensive review of the condition of the 515 housing stock, and found that to correct the imbalance between income and expenses for many projects, there is a need to reduce debt service and to facilitate the injection of new capital equity into the projects. Such a revitalization of the portfolio will involve budget authority for the reduction, elimination or deferral of debt service on a 515 loan and for grants in some cases. To process efficiently a large volume of projects, I strongly believe that RHS should use the services of private entities and State and local agencies to develop project financial plans, particularly those entities that gained experience by participating in HUD's mark-to-market restructuring program, and we are pleased that H.R. 5039 authorizes the use of outside contractors.

As within the legislation, there are provisions in the bill which raise some concerns within the industries. The bill proposes a maximum rent for all tenants in revitalized projects of 30 percent of adjusted income. We don't believe that this would work unless there is a subsidy involved as well, for the reasons that have pretty much already been raised here.

We are pleased that the committee is receptive to ending prepayment restrictions for owners; however, the new statutory prepayment framework in H.R. 5039 raises some concerns, which we discussed in our written testimony.

We would appreciate the opportunity to work with the committee to resolve any of the issues we have placed in our written testimony so that new uncertainties and legal disputes are not created, and that the bill carries out the stated purpose of H.R. 5039, which is "to avoid further costly litigation."

With respect to tenant protection, we would only note that the legislation should be clearer as to whether the amount of assistance remains fixed at the year one level or rises as comparable market and project rents rise. We support the latter as providing a better measure of protection.

Overall, we feel H.R. 5039 is promising legislation, and we thank the Administration, the bill sponsors and this subcommittee for moving forward the important rural housing issue. Thank you again for this opportunity to testify and I will be happy to answer any questions.

[The prepared statement of Mr. Rice can be found on page 98 of the appendix.]

Mr. DAVIS OF KENTUCKY. Thank you, Mr. Rice.

Chuck Wehrwein is senior vice president of strategic development of relationships for Mercy Housing. This organization is headquartered in Denver, Colorado. It uses public/private partnerships to develop housing in communities for low income and underserved families.

You are recognized for 5 minutes for a summary of your opening statement.

**STATEMENT OF CHARLES WEHRWEIN, SENIOR VICE  
PRESIDENT, MERCY HOUSING, INC.**

Mr. WEHRWEIN. Thank you, Mr. Chairman. As you indicated, I am a senior vice president of Mercy Housing and also have held posts overseeing multifamily housing at USDA Rural Development and at HUD.

Mercy Housing has direct and significant experience with owning, acquiring, and restructuring federally assisted properties, working within and using the Mark-to-Market program at HUD, using State and market rate tools, and we led one of the largest rural portfolio acquisitions by a non-profit.

I appreciate the opportunity to offer comments today on H.R. 5039. Mercy Housing is a non-profit affordable housing developer, owner, and manager headquartered in Denver, with real estate interests in many other regions throughout the Nation. In our 25 year history, we have developed or preserved over 18,500 units of affordable housing serving more than 55,000 low income Americans on any given day.

We would like to extend our appreciation to the bill's sponsors on recognizing the need to respond to the desperate preservation needs of the rural portfolio. We would like to offer some suggestions based on our experiences in rural and urban preservation, about how the existing bill can be improved to respond to the existing situation.

Mercy Housing has recently completed the purchase, and is finalizing the rehabilitation of a 30-property, 926 unit rural portfolio located throughout Washington State, known as Cobble Knoll. The total development cost for the 30 properties will be about \$42 million, including about \$8,000 per unit in initial rehab, and \$31,000 per unit in acquisition costs.

Our experiences, in summary, are: a high capacity, not-for-profit can bring significant benefits to a large scale transaction; that restructuring tools made available to the Department, such as subordination, new debt, debt restructuring and, in limited cases, debt forgiveness, are key to creating extended affordable use, as is the ability to reallocate rental assistance resources to raise some partially assisted properties to fully assisted.

We have learned that projects with 100 percent rental assistance, under either Section 8 or Section 521, are much more likely to be successfully preserved and to be economically viable going forward.

We have learned that project based rental assistance is critical to achieve effective underwriting from market sector lenders, with longer terms providing more comfort and therefore more private sector resources to help preserve these valuable assets.

We have learned that partial or no rental assistance, especially those in remote or low cost areas, are extremely difficult to restructure using housing finance tools available today and will likely need debt forgiveness, new or transferred rental assistance and/or grants to be viable.

We have learned that the Rural Development field staff is made up of well trained generalists with a strong commitment to this housing and to rural communities in general. However, they have little experience with modern housing finance tools and strategies being used outside of the USDA today. Furthermore, the Department lacks expert restructuring agents. And USDA's structure and culture is very decentralized, resulting in poor sharing of best practices, little capability or willingness of the national office to direct strategies based on best practices to the entire field, and a maddeningly variable application of rules from State to State, and even county to county.

As I noted earlier, Mercy Housing has preserved many other affordable homes in addition to the rural acquisition I noted earlier. This experience is entirely relevant to the discussion today. and I would offer a few comments based on our experience.

One, creating and empowering a central unit to direct the implementation of preservation policy at HUD has been a model of efficiency and good government that should be copied. These tools and their implementation have preserved scores of affordable homes and saved the taxpayers money—\$1.9 billion at least count.

A final point I would make about the lessons learned from other preservation experiences is that not all owners share the same goals of meeting property needs, assuring renewed and extended

affordability and engaging in long term ownership. MAHRA specifically recognized the unique role of high capacity non-profit owners. Mercy Housing and others like us are in this for the long haul and our missions are congruent with the government's.

With the foregoing experience in mind, we offer the following suggestions for improving this bill, so that this rare opportunity to change rural housing policy is maximized.

We suggest that we create or contract with a unit of expert housing restructuring staff such as exists in HUD's Office of Multi-family Housing.

We suggest that we empower this expert unit to promulgate policy, tools and best practices that will be used consistently across the country. Furthermore, we ask that for any owner or purchaser seeking it, we would require the Secretary to provide a formal commitment as part of the long term viability plan. Failure to do so would make the current or future owner uncertain of the Department's ability and commitment to carry through on these commitments and will chill their interest in engaging with the Department.

We suggest that we provide for the ability to accelerate the replacement of systems that are due to be exhausted or obsolete within the coming years.

We suggest that the legislation provide the Secretary with the authority to split current USDA loans into multiple loans, some with fully amortizing terms, others with cash flow only terms, so that this debt might be preserved and used for low income housing tax credits basis.

We propose eliminating the 75 percent rule, clarifying the 30 percent rent rule, and providing that the notice of prepayment and sale is certainly way too short at 90 days, and should be extended at least to 6 months, both to help the tenants in finding replacement housing if needed, and to provide more time for interested preservation buyers to become aware of and enter into negotiations with the seller.

We would like to encourage transfers of high capacity not-for-profits.

Mr. Chairman, this concludes my testimony. We have more detailed information in the written testimony. We stand ready to assist the committee and the Administration in any way possible.

[The prepared statement of Mr. Wehrwein can be found on page 106 of the appendix.]

Mr. DAVIS OF KENTUCKY. Very efficient cue that you picked up on there. Thank you very much.

Just—as we move forward here, without objection, the following written statements are going to be admitted for the record: statement of the National Association of Home Builders, and the letter from the National Association of Realtors.

I appreciate your comments on best practices. I think there is much that we can learn by copying the efficiencies, the successes from one another relevant to the different parts of the country and our communities uniquely.

As I listen to your opening statements, and read your opening comments for the record, one thing that I noted is that there is a wide variety of issues. Very well intended, important focus.

We have the potential on this bill to get very global, very quickly, as with all legislation. And one of the things that I am reminded of, the old proverb that says, the main thing is to keep the main thing the main thing.

And the one thing I want to clarify, our heart of the committee is to work with you closely, in a very focused bill. The purpose of the bill is about restructuring and prepayment, and not about new construction. I am very sensitive to the concerns over this, and our need for expanding housing. Our intent is to preserve and expand quality affordable housing in the context of this legislation.

So, with that, I would like to direct my first question to Mr. Carew. And you have a unique perspective. In Kentucky, in the communities where you are dealing in both my district and Congressman Rogers' district, you have seen from your perspective the State as well, dealing with urban housing issues.

And one thing I would like to comment on briefly, for the record, is how you see affordable housing needs in rural areas, different from the urban areas, and why do the rural residents who are now ready for home ownership find it more difficult to find safe and decent apartment housing in their communities?

Mr. CAREW. Thank you, Congressman. That's a global question.

Mr. DAVIS OF KENTUCKY. I'm not meaning to engage in political hypocrisy, although I am sure that has happened in this chamber before. Just from a practical perspective.

Mr. CAREW. From a practical perspective, the main differences between rural and urban—and one of them is, to this day, in rural Kentucky, we have no enforcement of the building code. So, the housing stock that we have was never built to a code. So that it's very difficult to find quality housing at an affordable in rate.

I think the other thing we should keep in mind is that in eastern Kentucky, Appalachian Kentucky, we have some of the poorest counties in America. And we are always limited by Federal statutes to serve those below 60 percent of median in a rental project.

So, when I go to Owsley County, the second or third poorest county in America, to Booneville, the county seat which is in the Fifth District, and I try and make a project work for families who are below 60 percent of median in that county, the window of opportunity to make that project financially successful is very, very small.

So, it's almost unheard of, although we have one tax credit project in Housley County. But tax credits alone don't do the trick. And that's where 515 projects, when you go around all Kentucky, every small, rural community has a 515 project.

And so I think it's difficult to do deals in rural America, in rural Kentucky, without bring in subsidies to the table. If you looked at a line east of I-75 in Kentucky, and counted up the tax credit projects, it would be a very small number of projects. But if you counted up the 515 projects, basically every community has got one.

I am not sure I am addressing your question. Those are some general answers.

Mr. DAVIS OF KENTUCKY. I appreciate the perspective. I was actually out in Owingsville last night, and talking to a fairly large group of folks out there. I mentioned this issue, and the interesting

thing from the grassroots, getting into all the technicalities of the bill. There seemed to be a very positive response from folks, this idea of being able to preserve and improve the quality of the process. Prepayment is much less an issue down there, but preservation is a very critical issue from the standpoint of leveraging resources long term.

Mr. Anders, in your opening statement, and I apologize again for us having to move down the line, but to get back to your concerns. We take those very seriously.

You mentioned your opinion that there should be changes to the way H.R. 5039 allows tenants to be free from discrimination simply because they hold a voucher. Could you please explain what recommendations that you would make, or you would have for this specific provision?

Mr. ANDERS. I think the simplest way is to state, as it does in the HUD Section 8 program, that the residents have a right to remain in their present home. That right should only be subject to good cause eviction.

Currently, you simply have a provision that states that the landlord may not discriminate against voucher holders. If the landlord does not like them for any other reason, he or she can decide not to rent to a particular household. There is nothing that prevents them from otherwise refusing to rent to voucher holders, as long as they do not discriminate under the Fair Housing Act, and as long as they don't say that I'm not going to have any voucher holders in this building. Those are two prohibited provisions. The right to remain is in the HUD Section 8 program. It's in the enhanced voucher program. It gives the residents the right to remain in their homes.

Mr. DAVIS OF KENTUCKY. Mr. Rice, would you like to share your perspective, maybe, on Mr. Anders' comments?

Mr. RICE. Sure. The 515 program, as well as HUD programs, require us to develop tenant selection criteria that the agencies look at, that meets their requirements.

And we have to stick to those very strictly. I don't see where some—certainly, we are not going to have something in our policy that says we are not going to rent to somebody because they have a voucher. So, I don't believe it would be a problem because they wouldn't approve a policy that would allow us not to rent to someone for that kind of reason. We have to have very good reasons not to rent to tenants, the same way we have to have very good reasons to evict a tenant.

Mr. DAVIS OF KENTUCKY. I appreciate your perspective. My concern is maintaining balance between the right to remain and the property rights of the owners, from the perspective of this legislation.

Going back to Mr. Anders, a follow-up. In your testimony, you also expressed concern over the fact that tenants will be provided a voucher that will assume that a tenant will take that voucher to a unit renting roughly the same price as the unit that had been prepaid. In essence, the voucher program will ensure that tenants are not made worse off by prepayment.

You suggested that tenants should not necessarily be bound by the same formula. Could you comment on the voucher formula,

keeping in mind that the goal of the voucher program is to protect tenants from being disadvantaged by prepayment.

I would appreciate your insights.

Mr. ANDERS. There are three problems. The first problem is that the top end of the formula in the voucher program that is in H.R. 5039 essentially restricts the rent to fair market values of the unit on the date of prepayment.

If, as is the case that Tom just pointed out in Kentucky, you have a tenant who has to move to another community because there is no decent, safe, and sanitary housing in the community in which the 515 project is located, there is quite a strong likelihood that the neighboring community, which does have the decent and affordable housing, will have higher rents.

The voucher program, as it is currently set up, does not allow the agency to pay for the higher rent. That means that the rent which the tenant is going to be paying is more than the tenant can afford and he or she will be overburdened.

The second problem is at the low end of the voucher formula. Here we have a two-fold problem. One arises when you have a resident who is already overburdened. If you force that resident to another locality you are likely to increase that burden if rents are higher in that community. Second, if their income goes down, they are going to be evicted, because there is no mechanism in the voucher program, as it is presently structured, to reduce their rent.

So, there is a limitation there.

The third problem is simply affordability. When somebody is going to move, particularly an elderly person, the likelihood is that they are going to move to a locality where their family is already located. That may mean that they are going to move across the Nation. They are not simply going to move into the next town.

Elderly people, when they are forced to move, and they see it as the last move, want to move to where their family is located. And the restrictions on the voucher subsidy in H.R. 5039 may simply not work in the new community. It's as simple as that.

Mr. DAVIS OF KENTUCKY. Thank you very much. Would any of the other panelists like to comment on the statement? Mr. Loza?

Mr. LOZA. We had noted the problem of the portability of the vouchers and we understand the need to keep costs down. However, we would agree with Mr. Anders that particularly for our elderly or disabled persons, who happen to be displaced from 515 projects, we would—we don't know what would happen, but we would expect that they would want to go to a place where there are support systems, nursing homes, close to family.

So, at a minimum, we were suggesting that maybe we can make an exception for those particular populations.

Mr. DAVIS OF KENTUCKY. That is a very good point, especially dealing with long term care issues for the elderly.

Mr. Arbury?

Mr. ARBURY. As I listen, I think we are talking about two separate issues. We are talking about elderly people who might move out of—as Gideon was talking about, Kentucky, but as I understand it, the areas that Mr. Carew was talking about in Kentucky are very depressed, and so I can't see where a number of those

properties are going to be prepaid and somehow, some higher market rent is going to occur in those areas.

Whereas if an elderly person moves across country, that is a whole different problem, in terms of where they are going to locate, and I thought the whole issue was to preserve, as much as possible, the 515 housing that we have today.

Mr. DAVIS OF KENTUCKY. I appreciate the insight. And you are right. They are two different issues. Mr. Carew and I see firsthand the overwhelming number of counties in our district are really preservation issues. I have probably three, maybe four, counties that are exurbs or maybe becoming exurb areas, since a large metropolitan area—northern Kentucky metropolitan area, where that growth is taking place, and prepayment could potentially become an issue.

It's a small part of the unit population, but still it's an important question to ask, on balancing that out but maintaining the focus on presentation.

And I appreciate what everybody shared. I would like to recognize the gentleman from Missouri.

Mr. CLEAVER. Thank you, Chairman Davis. I intend to support this bill during the write-up and when it goes to the Floor. I think some of you have made some interesting suggestions about improvements.

My concern is still that, the answer of which may have gone out of the door a few moments ago, and I'm not sophisticated enough to leave it alone. No matter how I look at this, the 515 program has been zeroed out, and at first I thought, you know, it's got to be me, because I asked the question three different ways, and I never could get the answer.

You are involved in these programs every day. I'm just curious, before I go any further. Do any of you see that the 515 program has been zeroed out?

Mr. RAPOZA. Yes.

Mr. DAVIS OF KENTUCKY. The Chair recognizes a show of hands. That would be—

[Laughter]

Mr. RAPOZA. Congressman, the budget, if you turn to the budget and you turn to the Section 515 line, there's zero there.

Mr. CLEAVER. Yes. Yes. And zero means naught?

Mr. RAPOZA. That's right. That's right.

Mr. CLEAVER. Okay. I think we can communicate. I think this is going to be good from now on.

[Laughter]

Mr. CLEAVER. The 515 program is zeroed out, and if we are now going to place emphasis on the 538 program, are we making a move away from the poorest of the poor?

Mr. RAPOZA. Yes.

Mr. CLEAVER. And accommodating those whose means are much greater?

Mr. RAPOZA. Very simply, yes, sir. That's exactly right. Yes. The 538, a guarantee is just that. It doesn't provide any subsidy at all. To make 538 work for the most part, the projects have to be geared toward larger cities, and they have to serve families who are

wealthier. 515 for the most part serves poor communities and poor families. 538 doesn't work for poor communities and poor families.

Mr. LOZA. Mr. Cleaver, the markets will vary, depending on different parts of the country. And we've asked the Department of Agriculture to provide us with the data that allow us to see from area to area who is being served. The data is not as good as we'd like it. However, from what we have seen, there are clearly two different markets. 531 serves a higher income market, and 515 serves a lower income market. There's no doubt about the data that is available.

Mr. CLEAVER. Mr. Carew?

Mr. CAREW. Mr. Cleaver, we are in the process of developing a 538 in Moorehead, Kentucky. But essentially what it means is that we have to bring other subsidies to the table, such as HOME money, such as State trust fund money, such as the affordable housing program of the Federal Home Loan Bank, such as tax credits, so that we've got to make up the difference between a 1 percent 50-year loan and a 30-year market rate loan. That's the simple analysis.

Mr. CLEAVER. Okay. But here's my concern. First of all, I think without any new construction, the program is essentially dead on the vine, and I'm not sure if there is a suggestion here, a subtle suggestion that is not even subtle, that there's no need for new construction, which would attract primarily the poor. And so we're going to deal with rehabbing, you know, existing units, and we're not going to do anything in terms of expanding housing opportunities for the poor and rural areas.

And to go back to Mr. Rapoza, your question—I mean, your statement, if you are supporting prepayment, and you are—

Mr. RAPOZA. We don't, actually.

Mr. CLEAVER. So nobody up here is supporting—

Mr. RAPOZA. Well, I think some people do. We don't support prepayment without having housing options and subsidies for families tied to that prepayment.

Mr. CLEAVER. Okay. Who is supporting prepayment?

Mr. ARBURY. We're not against prepayment as long as you have certain restrictions that are put in this bill in terms of notification and/or long-term viability plans and other things to try to preserve the housing, but we're not against prepayment per se.

Mr. CLEAVER. So your support is contingent on the notification period?

Mr. ARBURY. Notification, restrictions on the sale, you know, if other parties are willing to come forward and finance this housing and keep it under a long-term viability plan, I think it's 20 years in here, to make sure that it stays as rural 515 housing, we're not opposed to that. But we're saying if an owner wants to get out and fresh money needs to come into the property, why not?

Mr. CLEAVER. Yes, sir.

Mr. WEHRWEIN. Congressman, we recognize that there—litigation that's taken place over many years has not played out well in terms of maintaining the inability—or the limitations on prepayment. We would, like many of the other panelists here, recommend that many of the issues in H.R. 59 be addressed in terms of protection of residents, and that resources and timeframes and structures

be made such that these assets have a good chance of being preserved as affordable, as opposed to just simply being lost to the affordable housing inventory.

There are many, many buyers who might be interested in maintaining these as affordable homes, maybe even within the 515 program. We would encourage the committee to make changes that would encourage owners to sell to those folks and folks to buy those units and keep them in the inventory.

Mr. ANDERS. Congressman?

Mr. CLEAVER. Yes, sir?

Mr. ANDERS. I know that in Kentucky the prepayment issues may not be as significant as it is in California. My colleagues in California estimate that practically every 515 project in that State—and that State is not fully urbanized yet—will be lost through prepayment because property values in the State have increased. We're effectively going to lose the 515 program in the State.

Let me raise another issue. And I think some of the numbers that were bandied around today are interesting. The Administration's proposal to revitalize the 515 stock cost of about \$20,000 a unit. They're saying that it's going to cost \$80,000 a unit to build a new unit under the section 515 program.

If I'm not mistaken, the numbers that Chuck was putting out say that it cost them about \$40,000 a unit to preserve about 1,000 units in Washington State, which is not an inexpensive State. It seems to me that that's a reasonable and rational way of approaching this prepayment problem rather than simply taking, you know, approximately 50,000 to 70,000 units of 515 housing and simply converting them into other uses.

Mr. CLEAVER. Let me share with you my take on this. You do it every day. That if we leave 515 essentially and go to 538, we are abandoning the rural poor. That's how I see it. And on top of that, my concern is that if we allow for repayment—prepayment, I'm sorry—you're going to end up selling the property and making a—you don't want to sell it to lose money. I mean, anybody who wants to lose money, raise your hand.

And so you're going to sell it to make money. Do you believe that you owe something because you were able to get this at 1 percent, which—1 percent is free? I mean, you did 1 percent, and then you're going to sell it and make a profit. We eliminate housing for the poor. People who are in 538 will get a guaranteed loan, but you're not going to get a guaranteed loan for property if you are poor, whether you live in a rural area or if live in the middle of New York City.

Yes, sir?

Mr. RICE. If I could address that, the 1 percent interest rate is a benefit to the resident, not to the owner. The 1 percent interest rate—my rents are based on my costs and my loan repayment at 1 percent, and all of my costs and a very small return to the owner, which hardly any owners get any more. And to say that the 1 percent benefits the owner is not true.

The 1 percent benefits the tenant, because it lowers their rent. The market rent rate for a project is based on the note rate. The basic rent is based on the payment at 1 percent. And so the dif-

ference between those two, the interest credit, lowers the rent to the tenant. It does not benefit the owner.

Mr. CLEAVER. Yes, but the program was designed to help the renter.

Mr. RICE. Correct.

Mr. CLEAVER. It wasn't designed for the owner.

Mr. RICE. Okay.

Mr. CLEAVER. The prepayment you are saying is now the time for the owner to get his or her due.

Mr. RICE. It's time for the owner to do what he was contractually told he could do—

Mr. CLEAVER. Which was?

Mr. RICE. The loan agreement states that at any time that the owner could obtain sufficient financing outside of the government that they were required to prepay, not only that they could, but it was a requirement. When we built these apartments in the beginning, the first thing they had to do is go to a bank and get a letter of denial saying that they would not loan us the money to build a project here at these rental rates.

Mr. CLEAVER. I can get a letter of denial. That's not—

Mr. RICE. I didn't say it was hard, okay. So, but it was an apartment project that nobody else wanted to build because it was an area that couldn't meet market rents. So we went to the Rural Development, and we said, we want to use this—take your money at 1 percent. And they said, okay, but as soon as you could get a bank loan, if your equity was down or your rents were high enough you could get a bank loan, you're supposed to come in and pay us off.

None of our owners thought they would be in these projects over 7 years. Now, my newest project was built in 1991, and none of my owners have gotten out, other than the ones who passed away. Now I think they have a right to, if they sell to a nonprofit, whatever, they have a right to get out of these projects and move on. And I don't think—I don't think it's a gift they're getting, this 1 percent and that they owe something, no I don't.

Mr. CLEAVER. We disagree. And we probably—there's nothing that's going to stop me from disagreeing with you. But if you get a 1 percent loan you didn't benefit, I mean, I—you know, I just—I cannot accept that. But that's okay.

Are you familiar with Washington, D.C., property at all?

Mr. RICE. A little. You mean like rental rates and stuff?

Mr. CLEAVER. Yeah. I mean, you know, if you go not far from the Capitol, you'll find properties that were almost falling apart—that a few years ago you could have purchased for \$25,000—are now being sold at \$400,000. It's happening all around Washington. Are you familiar with the term “gentrification?” Can that happen in a rural area?

Mr. RICE. Sure.

Mr. CLEAVER. Okay.

Mr. RICE. I mean, I'm in a number of towns that were rural a long time ago that aren't anymore. But I'm in a lot of towns that are rural and are going to be rural forever, if they stay alive at all.

Mr. CLEAVER. And if—and that will remain rural if people can still afford to live there. But if all of these properties are sold and

we end up with new rural condos, we have gentrified even rural areas.

I guess I'm not comfortable—

Mr. DAVIS OF KENTUCKY. If the gentleman would yield for one second.

Mr. CLEAVER. Yes, Mr. Chairman.

Mr. DAVIS OF KENTUCKY. We're just talking about 10 percent of the properties are in question on being sold right now, just for my—I do share your concern on this, but just to bring the number down to a more practical level. I yield back.

Mr. CLEAVER. Mr. Chairman, thank you for bringing that—I think I made my point. I'm very concerned about what's going to happen to people who are poor, who cannot get guarantees. And I don't know how we address it. It is a concern.

Mr. DAVIS OF KENTUCKY. My commitment—I empathize very much with those concerns and would like to work with you on ways to fund Section 515. It's probably going to need to be in a different piece of legislation. Perhaps what Chairman Ney has proposed with the affordable housing fund and the GSE reform bill, you know, may be one path to address this separate from our preservation efforts here, prepayment efforts.

One thing that I would like to direct a question to Mr. Wehrwein from his perspective and the other members of the panel join in. And one thing I would like to clarify as well, is when we speak of prepayment in our estimation, for example, the majority of my district overwhelmingly, the question is preservation and not prepayment. And what we want to do is improve the quality and hopefully expand that base of affordable housing that's out there, and that nobody can prepay unless they have fulfilled their 20-year use restriction commitments. So there's got to be contractual fulfillment before prepayment even becomes an option under any circumstance.

But to Mr. Wehrwein first, how many—approximately how many Section 515 developments has your organization or members of your organization helped to finance or develop? And out of those, if we can just put the follow-on there together, how many are at risk of becoming unsuitable for housing and for revitalization programs such as the one that we're attempting to craft if H.R. 5039 is not enacted?

Mr. WEHRWEIN. Mr. Chairman, thank you. We have acquired or built about 45 Section 515 deals in our history. I would say that most of those are in pretty good shape, mostly because we've—30 of them we've recently acquired through this transaction that I spoke of in my testimony, and we've brought some new resources to bear almost on an exceptional basis to try to make those units modern and to sustain their quality.

And as I indicated, you know, that took about eight to ten thousand bucks a unit to accomplish. In some of our other projects, we've built new and we've been able to maintain some reserves. I would suggest, however, that we have looked at and passed on probably another three to four thousand units of affordable housing because these tools that are described in H.R. 5039 are not in place, and it's not a smooth track to go through Rural Development to try to close on these. Again, we did this in a rather exceptional

way and found that it was quite challenging. And there are also specific resources available in the State of Washington that happen to make this work. We actually—we've looked at Section 538 as a vehicle to help acquire and use other soft resources, and it just tends not to work and not to be efficient.

So, if anything, Mr. Chairman, I might suggest that we have passed on a number of units because we couldn't make it work.

Mr. DAVIS OF KENTUCKY. Okay. Thank you. Would anyone else like to make a comment on that from your experience? Yes?

Mr. ANDERS. I just want to point out that not all owners of 515 projects which are in markets that have not appreciated are going to stay in and preserve their units.

I think what we're going to see, and what we have seen in the HUD program, is that certain owners who are sitting with projects that clearly need revitalization are going to opt for revitalization. You're going to see owners of projects who sit in markets that have appreciated which are going to prepay, and current estimate in 2004 was that 10 percent of stock will prepay.

You're going to find that probably somewhere between 5 to 15 percent of the other owners are going to sit. They're going to sit and look at what happens to market conditions in their area in the next 5, 10, or maybe even 15 years, and then decide which way they're going to go.

So, potentially, even though the estimate in 2004 was that only 10 percent of the units would prepay, I think the number eventually will be substantially higher because certain owners are simply going to sit, as they have done in the HUD mark-to-market program, because they don't know what's going to happen in their market. If and when the market improves, they will opt out.

And the translation is that—and the RHS just recently released a study that shows that approximately 1.6 persons live in a Section 515 household, if we take the conservative estimate that 50,000 units are going to be prepaid, which is 10 percent of the stock, we're talking about 80,000 people subject to displacement. And that's not an insignificant number.

Mr. DAVIS OF KENTUCKY. Anybody else have something they'd like to share?

[No response]

Mr. DAVIS OF KENTUCKY. Just as we wrap up, I'd share a personal perspective in my interest in working on this bill that indirectly brought me into contact with the 515 program. We have a rapidly—in fact, one of the fastest growing counties in the entire Commonwealth where I live in Boone County, Kentucky, but in Covington, Kentucky, Newport, Kentucky or urban areas with rapid economic growth, we're seeing a similar thing that has happened with Section 8 housing programs and with the low income, working class families being driven out of the area potentially and having to move down into areas where in fact other rapid economic growth is taking place in the next few years has a potential to displace them again.

And what we want to strive for ultimately is a fair and compassionate means of providing that affordable housing, but at the same time allow the market to work in such a way that there's a

balance so the property owners have their rights protected, that all parties maintain their contractual and personal obligations to this.

I appreciate very much your coming here today. Your written testimony is of great value to us. We'd like to continue to work closely with you as this bill moves to markup in May. If there are places where we can make appropriate adjustments dealing with both the prepayment question and dealing with the preservation issue, the voucher issue, we consider your expertise in the field to be most valuable to us and look forward to working with you.

It's been a pleasure, and I personally want to thank you very much. The Chair notes that some of the members of the committee may have additional questions for the panel, which they may wish to submit in writing. Without objection, the hearing record will remain open for 30 days for members to submit written questions to these witnesses and to place their responses in the record.

With that, this hearing is adjourned.

[Whereupon, at 4:07 p.m., the subcommittee was adjourned.]



# **A P P E N D I X**

April 25, 2006

**Opening Statement**

**Chairman Michael G. Oxley  
Committee on Financial Services**

Hearing

H.R. 5039, the Saving America's Rural Housing Act of 2006

**Tuesday, April 25, 2006**

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Good Morning. Preserving affordable rural housing programs is important to the thousands of small towns and communities that face shortages of clean, decent housing for families. In many communities, section 515 apartment housing, developed using loans from the Department of Agriculture, serves as the only source of this type of housing. In my district in Ohio, for example, there are approximately 53 section 515 multifamily properties housing over 2,000 individuals and families. While homeownership should be a realistic goal for every American, some families are not ready to own their own home and multifamily apartment living often provides a safe and affordable alternative.

However, while the need for affordable housing is increasing, especially in rural areas, the construction of section 515 properties has slowed. The average 515 property was built 28 years ago, which means that the wear and tear of nearly three decades of use has resulted in the need for repairs to ensure that 515 housing remains safe and clean. Without needed repairs, we risk losing part of the portfolio because some of these properties will no longer be safe or useful as affordable housing.

I thank Congressman Geoff Davis for his leadership in introducing H.R. 5039, the Saving America's Rural Housing Act of 2006, which will create a revitalization program, to be administered by the Department of Agriculture. This program will allow section 515 owners to enter into loan restructuring agreements with the Department in order to increase cash flow for properties and provide the much-needed repairs that will preserve these units for the future, ultimately reducing the need for new construction.

I am encouraged that there is agreement among many groups that the revitalization program that H.R. 5039 creates is necessary to the long-term health of the section 515 program.

I also applaud the cosponsors of H.R. 5039 for recognizing that we must repeal the onerous prepayment restrictions that currently block section 515 owners from prepaying their loans in a timely manner after they have fulfilled their obligations to the Department of Agriculture. For the past several years, the Department of Agriculture has been involved in expensive litigation, defending a

statute that prevents prepayment. This repeal would save valuable taxpayer dollars which could be put to much better uses than litigation.

Additionally, the Saving America's Rural Housing Act of 2006 offers a variety of tenant protections modeled on the HUD section 8 program, both for tenants living in revitalized properties and tenants living in units subject to prepayment. While allowing owners of section 515 properties to prepay their loans once they have fulfilled their commitment to the Department of Agriculture is a worthy goal, there must be sufficient protections in place for tenants who currently make these properties their home. I commend the sponsors of H.R. 5039 for acknowledging the importance of tenant protections.

I want to thank Subcommittee Chairman Ney for holding this important hearing today.

**Opening Statement  
Congressman Geoff Davis**

**Housing and Community Opportunity Subcommittee Hearing  
Tuesday, April 25, 2006, 2:00 P.M.**

This hearing of the Subcommittee on Housing and Community Opportunity will come to order.

The Subcommittee on Housing and Community Opportunity meets today for the purpose of hearing testimony on H.R. 5039, the Saving America's Rural Housing Act, a bill to improve the Section 515 rural multifamily housing program through sensible and timely reform measures.

The Housing Act of 1949 originally authorized the U.S. Department of Agriculture to make loans to farmers to improve their ability to provide decent living quarters for their employees and others. The program has evolved to provide affordable housing for the rural community as a general population.

Rural Development, an agency within the U.S. Department of Agriculture, released a November 2004 study prepared for USDA by a private consulting firm on the Section 515 portfolio. With an average property age of 28 years, the study revealed that nearly all Section 515 properties included in the study were in need of additional funds to cover essential repairs and maintenance costs.

I'd like to briefly share with the Committee one of the most interesting observations of the study: "If new funds are not invested in these properties, two-thirds (2/3rds) of the portfolio will only be able to maintain its current status – [which, keep in mind, is not good already for the majority of the properties] – if: The roofs *never* leak, the paint job lasts *forever*, the building siding is *everlasting*, no potholes *ever* develop in the parking lot, no one will *ever* need to replace a furnace or air conditioner, no doors will *ever* rust or rot, and all windows will work *forever*."

If you've ever owned a home, you know that these would be ridiculous assumptions on which to base your own personal budget, and they certainly aren't assumptions on which I'd like to base national policy. The fact of the matter is that Section 515 properties need help, and they need it now. It will only become more expensive to maintain the program as time progresses.

I've seen firsthand the dilapidated state of the Section 515 portfolio while traveling Kentucky's diverse Fourth District during my first year as a Representative. In the Fourth District alone, there are 40 Section 515 properties. Many of the properties are in dire need of assistance and repair.

Solutions are needed now to revitalize the program and ensure that it is sustainable for the future. These reforms will have a direct and positive impact on over 1,000 families in the Fourth District of Kentucky, and many more in rural communities across the country.

H.R. 5039 will create a revitalization program by offering restructuring plans to Section 515 development owners. This will preserve ailing Section 515 properties for the future, saving U.S. taxpayers an estimated \$2 billion in maintenance and rehabilitation costs by addressing problems now.

Section 502(c) of the Housing Act restricts the rights of owners of Section 515 properties to prepay their loan, even after they have fulfilled their contractual duty with USDA. H.R. 5039 will nullify the onerous restrictions in Section 502(c) to allow for prepayment of certain Section 515 loans entered into before 1989, thereby alleviating expensive litigation against Rural Housing Service, which has cost U.S. taxpayers millions of dollars to date.

Additionally, a voucher program will be created to protect tenants who live in properties subject to prepayment. It is estimated that only 10 percent of the current development owners would prepay their loans.

H.R. 5039 will save money on future litigation by nullifying the burdensome prepayment restrictions and protecting tenants, while revitalizing the existing Section 515 portfolio to continue the tradition of providing housing assistance to rural families.

This is proactive legislation that seeks to deal with the apparent problems now, rather than deal with more expensive solutions later. I'd like to thank the Administration, the Committee, the Ranking Member, Chairman Ney and other Members on both sides of the aisle for their help in putting together a good piece of legislation that will help to solve the problem of prepayment, while combating the aging portfolio of section 515 properties. The bill institutes sensible and timely reforms that will enable the program to continue providing low-income rural families with affordable housing.

Thank you Chairman Ney and Ranking Member Waters for holding the hearing today on such an important and relevant topic. Also, I want to thank the witnesses on both panels for their graciousness in attending the hearing today. I look forward to hearing your testimony and thoughts on H.R. 5039.

And with that, I would yield to Ranking Member Waters for her opening statement.

Opening Statement for Congresswoman Maxine Waters  
April 25, 2006

Hearing on HR 5039, the Saving America's Rural Housing Act of 2006

Good afternoon ladies and gentlemen. Let me congratulate Mr. Ney, the Chairman of the Subcommittee on Housing and Community Affairs for holding today's hearing on H.R. 5039, the Saving America's Rural Housing Act of 2006".

As many of you know, Mr. Ney and I recently participated in a Field hearing in my District that focused on the impact of the Community Development Block Grant Program (CDBG) on communities such as the City of Los Angeles, Inglewood, Hawthorne, Lawndale, Gardena, and Los Angeles County. I bring the hearing to your attention for one simple reason, because rural communities are really no different from other communities. The people who live in rural communities are situated different geographically, but they have housing and community development problems that must be confronted like the rest of the country?

One of the most pressing needs recognized by the sponsors of this bill is the shortage of quality affordable housing in the nation's rural areas. In many parts of the country, not only is there an inadequate supply of affordable housing, but the housing is aging; the average age of the Section 515 units is 28 years old. In many rural communities, grants and loans have traditionally been used to finance single and multi family housing.

The Section 515 Program has assisted approximately 1/2 million people, most of whom are poor. What other criterion do we need to support a housing program? I believe that it is enough that there be just one family, one person in need of housing. In rural America there is a real need for housing, one that mirrors the housing need in non-rural areas. However, without the reform and revitalization measures contained in H.R. 5039, the Congress might as well get out of housing business all together. We all know that housing and community development programs have been under attack for the past six years, and without a commitment to the pressing rural and non-rural housing needs in this country the quality of life for Americans living in these communities will suffer.

Today, Mr. Chairman, we have an opportunity to send a message of hope to Rural America by hearing testimony that will enable us to consider the appropriate measures to address the nation's rural housing needs. I am sure that no one thought that the President would propose to eliminate the Section 515 Program, but that is exactly what was proposed. If we really want to address the housing needs of our rural citizens, many of whom are disabled and elderly, we can start today by considering how to improve existing program efforts to assist them. Thank you



STATEMENT OF  
 GIDEON ANDERS, EXECUTIVE DIRECTOR  
 NATIONAL HOUSING LAW PROJECT  
 BEFORE THE COMMITTEE ON FINANCIAL SERVICES  
 SUBCOMMITTEE ON HOUSING AND COMMUNITY OPPORTUNITY  
 U.S. HOUSE OF REPRESENTATIVES  
 April 25, 2006

I am Gideon Anders, Executive Director of the National Housing Law Project (NHLP), a 38-year old nonprofit corporation that seeks to advance housing justice for low income persons by, among other things, preserving and increasing the supply of decent affordable housing throughout the United States. NHLP has worked on the preservation of Department of Housing and Urban Development (HUD) assisted and Rural Housing Service (RHS) financed housing for more than 28 years. Personally, I have worked on RHS housing issues for more than 35 years, and on rural housing preservation issues for 28 of those years.

While NHLP is deeply concerned with the adequacy of the supply of decent, safe, sanitary and affordable housing in rural and urban areas, the primary principle that guides our preservation work is the need to protect federally assisted residents against displacement from their homes. The statutory requirement that requires owners of Section 515 housing to maintain their developments as affordable housing for 20 years was enacted in 1979 at NHLP's suggestion when we discovered that the program imposed no use restrictions on owners and that some were converting their developments to other uses by displacing elderly and other households at will. Our staff also assisted in drafting the rural provisions of the Emergency Low Income Housing Preservation Act of 1987 (ELIHPA), which was enacted after an increasing number of owners of developments that were financed before 1979 were prepaying their loans and displacing elderly and other households from homes they had expected to occupy for the rest of their lives.

In 1991, NHLP assisted Mid-Minnesota Legal Services in litigating *Lifgrin v. Yeutter*, the first post-ELIHPA prepayment case that challenged an owner's failure to maintain affordable rents after prepaying a Section 515 loan. The residents prevailed in that case and the development was returned to the Section 515 program. NHLP has participated and assisted other legal services programs litigate cases that successfully challenged illegal prepayments of Section 515 loans. We currently represent several Missouri residents in *Charleston Housing Authority v. U.S.D.A.*, in which the United States Court of Appeals for the Eighth Circuit recently upheld the district court decision that the ELIHPA prepayment restrictions preclude the housing authority from prepaying its Section 515 loan. The Court also upheld the district court's decision that the housing authority's decision to prepay its loan and to demolish the 50 unit development that served predominantly African-American households violated the Fair Housing Act.

We are also assisting plaintiffs' attorneys in *Goldammer v. U.S.D.A.*, a case currently before the Ninth Circuit, which, for the first time, squarely raises the issue of whether an owner of a Section

515 development can force the prepayment of an RHS loan using state quiet title law that is in clear contravention of federal law.

At the request of the subcommittee, we are testifying here today on HR 5039, which proposes to lift the ELIHPA prepayment restrictions, protect residents through the creation of a new voucher program and provide RHS with authority to extend incentives to Section 515 owners that would enable the owners to revitalize their developments and maintain them as affordable housing for at least an additional 20 years.

We thank you, Congressman Ney, for inviting us to testify. We also thank Congressmen Geoff Davis and Frank for working with you in an effort to resolve a series of difficult issues involving the Section 515 Rural Rental Housing Program. I also want to thank your staff with whom I have met several times to discuss this bill and other matters.

NHLP generally supports the provisions of HR 5039 that enable RHS to revitalize and preserve the Section 515 housing stock. We, however, have serious reservations about the provisions that would lift the prepayment restrictions on projects financed prior to 1989 and about the voucher program that is proposed to protect residents against displacement. In both cases, we have recommendations that we believe will improve the bill.

Our views and these comments are shaped by the fact that the Section 515 housing stock serves the neediest rural households. According to figures recently released by RHS, nearly 94 percent of the 460,000 families currently residing in Section 515 housing are very low-income households. The average household income in all Section 515 developments is slightly more than \$10,000, while the average household income of those receiving Rental Assistance (61 percent of the households) is just under \$8,000. Households headed by females represent nearly three quarters of all households residing in Section 515 housing and households headed by elderly persons represent nearly one-half. Persons with a disability are the head of an additional 10 percent of the Section 515 households. Minority households comprise 29 percent of the households occupying Section 515 housing. Approximately 16 percent of all Section 515 households are rent overburdened, in that they pay more than 30 percent of their income for rent.

To place our comments in perspective, we reaffirm our fundamental belief that there is an absolute and continuing need for decent, safe, and affordable rental housing in rural areas throughout the United States and that the existing Section 515 housing stock is a major and critical element in meeting that need. Rural communities continue to have a greater need for affordable, decent, safe, and sanitary housing than their urban counterparts because housing conditions in rural areas have historically been, and continue to be, worse than in urban areas. The approximately 500,000 units of Section 515 housing that have been constructed in rural areas continue to serve a critical need in those communities. Frequently, those developments are the only available affordable rental housing that is decent, safe, and sanitary.

Our primary concerns with HR 5039 are that it does not become a vehicle for the displacement of nearly 110,000 persons currently residing in Section 515 housing and that it does not deprive rural communities as well as racial and ethnic minorities of critically needed decent, safe, and affordable housing. Our secondary concern is that any voucher program that is adopted should operate in a manner that provides residents of Section 515 housing with a right and an opportunity to remain in their homes or to easily relocate to other decent safe and sanitary

housing. Lastly, we believe that any legislation that seeks to preserve and improve the condition of the Section 515 stock must have a viable mechanism for transferring part of that stock to the nonprofit and public sector, a mechanism for preserving properties that are troubled, and a cost effective system for revitalizing properties that will be continue to be operated as affordable housing for the next twenty or more years.

#### **Rural Rental Housing Residents Should Not be Displaced by Prepayments**

*HR 5039 should be amended to condition prepayments on the availability of vouchers.* The introduction to HR 5039 states that “any revitalization or disposition of [the Section 515] portfolio, which houses nearly 500,000 low-income families and seniors, **should be handled with great care.**” (Emphasis added). Unfortunately, we do not see that care being exercised in the bill as it is currently drafted. Unless amendments are made to HR 5039, over 110,000 residents of Section 515 housing will be displaced from their homes. This is because HR 5039 does not condition the lifting of prepayment restrictions on the availability of vouchers and does not guarantee the right of residents to remain in their homes.

Our estimate of persons threatened with displacement is based primarily on the Comprehensive Property Assessment Portfolio Analysis (CPA) released by the Rural Housing Service in 2004. It concluded that if the ELIHPA prepayment restrictions were lifted on pre-1989 developments, ten percent of the total Section 515 stock, approximately 46,000 units, would be prepaid. Based on RHS recently released data, this translates to more than 73,000 persons that would be displaced by prepayments.

We believe that the number of projects and units that will be prepaid over time will be substantially larger. This is because the CPA estimate was based on a then current real estate market analysis. It concluded, based on market studies conducted in 2003 and 2004, that owners of 46,000 units had sufficient market incentives in 2004 to prepay their loans and convert the housing to market rate housing. The CPA made no effort to estimate whether owners had other incentives to prepay their loans or whether owners who did not have financial incentives in 2004 to prepay their loans would gain those incentives in succeeding years. We believe that both factors will increase the actual number of prepayments.

Our review and analysis of prepayments over the past several years reveals that not all prepayment are driven by market conditions. Many section 515 owners are prepaying their loans because they no longer want to be subject to the RHS reporting and regulatory requirements. Some are prepaying their loans as part of their estate planning process, while others are prepaying in order to free sizeable reserve funds accumulated in RHS restricted accounts.

More significantly, we believe that a large number of owners whose developments are located in markets that may not currently provide sufficient economic conversion incentives, will prepay their loans over the next several years as real estate market conditions in those markets improve. These owners will not prepay their loans immediately, nor will they enter into revitalization agreements that commit them to remain in the program for an additional 20-years. Instead, they will operate the housing under the current 515 program until such time as local real estate markets improve to the point that they are financially induced to convert the housing to market rate housing. Unfortunately, the CPA made no estimate as to the number of Section 515

developments that are located in such markets. We anticipate that as many as 20,000 additional units could be affected, resulting in the displacement of an additional 36,000 persons. This would bring the total number of persons threatened with displacement to nearly 110,000 if HR 3059 is adopted in its current form.

Unfortunately, the current bill does not protect any residents against displacement. Unlike the bill introduced by you, Chairman Ney, in 2003, HR 5039 does not condition the lifting of the prepayment restrictions on the availability of vouchers. This is extremely significant because it places residents at risk if this bill is enacted before an appropriations bill is adopted or if the appropriations are insufficient to protect all residents from displacement. It effectively puts the interest of 1600 owners before the interest of 110,000 low-income residents.

For the past several years appropriations bills have been passed late in the year while authorizing legislation has been passed earlier. Thus, a distinct possibility exists that HR 5039 will be enacted into law before any appropriations are made available for vouchers and owners will be allowed to prepay their loans and raise their rents before residents can be protected by vouchers.

For very low income elderly residents and for residents with disabilities, particularly those residing in market areas where prepayments are likely to occur, the consequences will be catastrophic. Households with incomes of \$10,000 or less will not be able to remain in their homes, will not be able to find other affordable, decent, safe, and sanitary housing and will not qualify for the Housing Choice Voucher program because, in most jurisdictions, that program is oversubscribed, as evidenced by long or frequently closed waiting lists.

Our concern about resident displacement is not allayed even if an appropriations bill is enacted within a reasonable period of time after HR 5039 becomes law. This is because the current HUD and RHS voucher programs do not permit assistance to be provided retroactively. In other words, if voucher funding is not available as of the day that an owner prepays a Section 515 loan, residents, even if they are allowed to remain in their homes, will be forced to pay market rent for their units until RHS can issue a voucher that will pay their rent prospectively. Most RHS residents simply do not have the resources to do so.

While RHS is undoubtedly and deservedly proud of the fact that it has recently issued 34 vouchers under its new voucher demonstration program to residents of a Georgia development, the agency is unable to retroactively assist hundreds, if not thousands, of other residents whose rents were increased by owners who prepaid their loans between October 1, 2005 and April of 2006. The Notice recently published in the Federal Register by HUD and USDA, advising the public that the agencies have implemented the demonstration voucher program, precludes housing authorities from providing voucher assistance to any tenant before the tenant's unit is inspected for compliance with HUD's Housing Quality Standards (HQS).

Even if voucher funding becomes available on a timely basis, we are very doubtful that the Administration's Fiscal Year 2007 (FY 2007) \$74 million funding request will be sufficient to meet the potential demand for vouchers. Last year, when it first proposed lifting the prepayment restrictions, the Administration estimated that it would need \$214 million for each of three years in order to meet the voucher demand created by prepayments. This year, it has only requested \$74 million and has expanded the purposes for which these funds can be used to include revitalization activities. Unfortunately the Administration has made no public effort to assess the

number of developments and units that are likely to be prepaid and the number of vouchers that will be needed to protect residents against displacement when the prepayment restrictions are lifted.

NHLP does not subscribe to the assumption underlying the Administration's budget request that, at most, one third of the owners who will become eligible to prepay their loans after the prepayment restrictions are lifted will actually prepay their loans during the first year that the restrictions have been lifted. If, as the CPA report concluded, 1600 owners have a current economic incentive to convert their developments to other uses, we cannot believe that at least a majority of those owners will not want to convert their housing as quickly as they can. There is no reason why they will not jump at the opportunity to terminate their participation in the Section 515 program, thus enabling them to make more money by operating the housing as market rate housing.

Even if one assumes that the Administration's assumptions are correct and that the FY 2007 appropriations request is justified by a reduction in the length of the voucher term--from three years to one year--the appropriations request is insufficient to protect even one third of the residents who are threatened with displacement. This is because the Administration has expanded the purposes for which funds can be used to include revitalization. If the administration plans to undertake a meaningful revitalization program in FY 2007, it will not also be able to protect residents from displacement through the issuance of vouchers.

As we do not believe that low-income residents should face the risk of displacement if voucher funding does not become available in a timely or sufficient manner, we strongly urge that the Committee modify HR 5039 to condition prepayments on the availability of vouchers. At the very least, we urge that the bill be amended to allow RHS to make voucher assistance available retroactively to the date of prepayment regardless of when the unit is inspected for HQS compliance.

We will discuss our concern that HR 5039 does not guarantee the rights of residents to remain in their homes below, when we discuss the adequacy and sufficiency of the proposed voucher program. Before doing so, however, we want to express our concern about the impact and consequences of lifting the ELIHPA prepayment restrictions.

*Developments in high cost areas and those that serve minority households must be preserved.*  
The removal of the prepayment restrictions will decimate the affordable rental housing stock in communities that have the greatest need for affordable housing. Rural communities in which real estate prices and rents have escalated simply do not have other decent, safe and affordable housing. The construction of federally assisted housing that serves low and very low-income households was effectively stopped in the 1980's. The removal of the RHS housing stock, which will occur when the prepayment restrictions are lifted, will eliminate a critical supply of affordable housing from the most needy communities and will deprive low- and very low-income persons of their capacity to continue to live in those communities. My home state, California, is a good example. We expect that practically all the Section 515 housing in the state will be prepaid if HR 5039 is enacted into law. This is because developments that currently charge \$300 or \$400 a month in rent will be able to charge \$1500 or \$1800 in rent after the prepayment restrictions are lifted.

Effectively, HR 5039 advances the proposition that we abandon the most highly needed portion of the Section 515 stock and that we deny low-income households the capacity to live in localities in which real estate prices have increased so that we can preserve and revitalize housing in communities where property values have not increased and where the demand for affordable housing is not as great. Such a policy simply does not make sense.

The fact that HR 5039 directs RHS to give funding priority for new Section 515 funding to communities where prepayments have occurred, regrettably will not resolve this problem because the Administration has proposed to stop funding for the Section 515 program. Moreover, even if funding were available, it would be significantly cheaper to preserve the existing Section 515 stock than to construct new units in the same localities.

We are also concerned that HR 5039 repeals a major civil rights provision that seeks to preserve affordable housing that serves minority households by requiring that before a prepayment is authorized the housing be offered for sale to nonprofit or public entities that would retain the affordable nature of the housing. As nearly 30 percent of the households occupying Section 515 housing are people of color, we are concerned that the lifting of the prepayment restrictions will not only remove low-income households from high priced communities but will also deprive persons of color from living in these communities.

We, therefore, urge that the Committee seriously consider amending HR 5039 to continue to require that owners of projects that serve people of color be required to offer to sell those developments to nonprofit or public entities at their fair market value before they are allowed to prepay their loans.

At the very least, we request that the Committee conform the RHS vouchers to the HUD Enhanced Voucher Program. Under that program, vouchers that are issued to persons threatened with displacement remain in the community in which the owner opted-out of the project-based Section 8 program. The continued availability of vouchers effectively replaces the project-based housing that has been removed from the community's housing stock. We see no reason why the rural vouchers authorized by HR 5039 should not be treated in the same manner.

Lastly, we urge the committee to extend the prepayment notice provisions contained in the bill to require landlords to inform public and nonprofit institutions located in their market area of their intent to prepay their loans. Such institutions can assist residents that are likely to be displaced in locating alternative housing.

#### **Adequacy of the Proposed Voucher Program**

The voucher program proposed in HR 5039 has several significant issues that undermine its effectiveness. First, it does not guarantee residents the right to remain in their homes. Second, it unnecessarily requires residents to live in the Section 515 development on the date of prepayment in order to qualify for a voucher. Third, it sets the voucher subsidy at a level that may disable residents from moving to neighboring communities and otherwise discourages portability and use of the voucher for homeownership. Fourth, it does not address the need for increases in voucher subsidies as rent and utility costs increase or household incomes decrease.

Residents of prepaid project must have a clear right to remain in their homes. As drafted, the proposed voucher program does not guarantee residents of Section 515 housing the right to remain in their homes. The bill simply restricts owners from discriminating against voucher holders by virtue of the fact that they are voucher holders. It does not preclude them from denying current resident the right to remain in their units for any other reason. If a landlord does not like the resident, believes that he or she is too demanding, or if the resident has created any other difficulties, the landlord is free to deny the resident the opportunity to remain in his or her home.

The HUD Enhanced voucher program guarantees residents the right to remain in their apartment when the landlord terminates his or her participation in the Section 8 program. The RHS voucher program should guarantee Section 515 residents the same right. Given that 60 percent of the program participants are elderly or persons with a disability—for whom the process of relocating is a severe hardship—this is critical requirement.

HR 5039 should be amended to make the right to receive a voucher absolute and not subject to the eligibility criteria of a local housing authority. Under the RHS demonstration voucher program, Section 515 residents can only qualify for vouchers if they meet the administering housing authority's voucher eligibility criteria. We see no reason for this requirement and believe that it should be eliminated. The purpose of the voucher is to protect the resident against displacement. Housing authorities are simply administrative intermediaries that should not be allowed to impose their own eligibility criteria to determine if the resident is eligible for assistance, particularly when the resident remains in the same unit and the landlord has previously approved the resident's eligibility to reside in the unit.

Section 515 residents should become eligible for vouchers as of the date that their landlord notifies them of the intent to prepay the loan. The provision that conditions voucher eligibility on the household actually residing in the prepaid development on the prepayment date is too restrictive. It disqualifies residents from receiving a voucher if they move from the development after receiving a notice of the owner's intent to prepay but before the owner actually prepays. Since owners will now have an absolute right to prepay, there is no reason why residents who chose to move from the development should be required to stay in their units until the prepayment date. Such a requirement hampers residents' capacity to move to other decent, safe, and sanitary housing that may become available in the community prior to the prepayment date. It also unnecessarily increases competition for vacant apartments in the community since all residents of a prepaid development may have to move at the same time. It is particularly restrictive if the owner of the prepaid development decides not to continue to rent the units to the Section 515 residents, forcing them to move in a very short time frame.

This shortcoming can be addressed simply by modifying HR 5039 to state that residents become eligible for vouchers as of the date that the owner sends out the notice of intent to prepay.

The formula for determining the voucher subsidy must be modified. The level of subsidy that is provided under the voucher program is also too restrictive. On the upper end of the formula, the subsidy cannot exceed the rent charged for the prepaid unit, or a comparable unit in the same market, as of the prepayment date. While this should work when the resident remains in the same unit, it may not work if the resident chooses, or is forced, to move to another community or decides to use the voucher to purchase a home. This is because rents or costs in neighboring

communities may be higher and the voucher subsidy may not be sufficient to cover such costs. As with the HUD enhanced voucher program, we suggest that HR 5039 be amended to provide that if the resident moves from the prepaid development, the upper limit of the voucher subsidy be the same as that for HUD Housing Choice Voucher Program in the community to which the voucher holder moves.

On the lower end of the subsidy formula, the bill requires the household to pay at least 30 percent of household income for shelter or the amount that the household paid for rent under the Section 515 program, whichever is higher. While this provision is acceptable as long as the household does not experience a significant change in income or expenses, it needs to be amended to accommodate hardships. Under the HUD Enhanced Voucher program, the amount of subsidy extended to a household can be increased if the household income decreases by 15 or more percent. Because no one benefits from an eviction of a household due to its failure to pay rent due to a decrease in income, HR 5039 should be amended to conform to the HUD Enhanced Voucher program.

Lastly, HR 5039 should clarify that RHS is obligated to adjust the voucher subsidy annually to accommodate rent and utility cost increases imposed by landlords and utility companies.

#### **The Right of First Refusal Must Be Made More Effective**

Unfortunately, the provisions of HR 3059 that are intended to provide nonprofit and public agencies, as well as resident organizations, an opportunity to purchase developments prior to their prepayment is ineffective. They only preclude owners of the housing from transferring the housing to anyone except a nonprofit or public agency for 75 days after the owner of the development has notified RHS of his or her intent to prepay the loan. It does not preclude the owner from negotiating a sale with anyone else prior to notifying RHS of the intent to prepay or from negotiating the sale during the 75 days but not completing the sale until after the 75 days have expired. It does not require the owner to negotiate with a nonprofit or public agency in good faith and does not give the nonprofit or public agency a right to purchase the development. Significantly, it does not authorize any funding or subsidies for the purchasing entity to maintain the housing as affordable housing.

HR 5039 should be amended to give nonprofit and public agencies as well as resident organizations an absolute right of first refusal to purchase any development that an owner is seeking to prepay, to provide funding for such purchases, and to provide subsidies to ensure that the development continues to serve low income households.

On a related matter, we also urge that provisions be included in HR 5039 that make all nonprofit and public agencies that are negotiating for the transfer of a Section 515 development eligible for RHS predevelopment grants. Currently, these grants are only available to nonprofit and public agencies that offer to purchase a development when the owner offers to sell the development under the prepayment process. Since prepayments will no longer be prohibited, the authority to make predevelopment grants must be modified.

### **The Bill Also Needs to Protect Resident of Troubled Projects**

*Residents of troubled projects should also be eligible for vouchers.* HR 5039 should also be amended to address issues related to troubled Section 515 developments. Currently, if RHS is unable to secure an owner's cooperation in bringing a development up to standards, it will foreclose on the development and, if necessary, reduce its foreclosure sale bid to ensure that the property is sold to a third party and not brought into the RHS inventory. When the foreclosure is complete, RHS's subsidy is terminated and residents are either displaced by increased rents, by the new owners revitalization plans, or forced to remain in the troubled and often substandard development.

We believe that residents in troubled projects should be protected in the same manner that residents of prepaid project are protected. Accordingly, we urge that the Committee amend HR 5039 to authorize RHS to issue vouchers to residents of developments that are being foreclosed upon, thus giving them the opportunity to move to other decent housing in the community.

We also urge that HR 5039 be amended to prevent RHS from simply foreclosing on troubled properties and allowing them to be sold to the highest bidder without placing habitability and use restrictions on the properties. Whenever possible, RHS should be required to force the transfer of troubled properties to nonprofit or public agencies and to provide those agencies with incentives and financial assistance to rehabilitate the properties and to rent them to low- and moderate-income households. The agency should only be allowed to dispose of troubled properties to the highest bidder when there is no clear need for affordable housing in the community in which the housing is located. In such cases, the agency should place habitability restrictions on the property to ensure that troubled projects are not used for habitation without bringing them up to decent safe and sanitary standards.

### **Revitalization**

As noted earlier, we generally support the revitalization provisions contained in HR 5039. We think that revitalization of the Section 515 stock is critical if it is expected to serve the needs of low-income households and communities for an additional 20 years.

We do, however, urge the committee to reconsider a provision in the bill that gives owners the right to obtain a commercial rate return on the investment made by limited partners under the Low Income Housing Tax Credit program. The investors already receive a lucrative return on their investment through the tax credit program. We see no reason why owners should be allowed to collect additional returns on that same investment. It will simply provide owners with additional profits and unnecessarily increase the cost of operating developments, which either translates into greater subsidies or higher rents.

We also urge the committee to modify HR 5039 to protect residents in developments undergoing revitalization from displacement, to provide them with relocation benefits and a right to return to their units if relocation is necessary.

In addition, we strongly urge that residents be given an opportunity to review and comment upon proposed revitalization plans. Residents are intimately familiar with the management and condition of the development in which they live. They should be allowed to review the

revitalization plan to ensure that all necessary systems are revitalized and the actions affecting them, such as individual unit revitalization activities, are carried out in a manner that considers the residents' needs.

Lastly, we urge that the provision regarding the termination of the long term use agreement be amended to allow an owner to terminate the use agreement only if the incentives that were offered but not provided are significant and material to the revitalization agreement.

#### **Minimum and Maximum Rents**

We endorse the provision in HR 5039 that limits residents rents to 30 percent of income. We also question the need and justification for a minimum rent. Minimum rents are not justified by the fear that extremely low-income households under report their income. We believe that RHS and landlords have ample tools to verify resident income and that rent determinations should be based on that verification. All the studies and reports about income and rent determination that we have seen suggest that both favorable and adverse mistakes are made in the income and rent determination process by landlords as well as residents. Such mistakes affect households of all incomes. Accordingly, we do not believe that extremely low-income households, which are the only household subject to minimum rents, should be penalized by their imposition.

Thank you Mr. Chairman and subcommittee members for the opportunity to present our views on HR 5039. The National Housing Law Project is prepared to assist you and your staff in addressing the various issues that the bill seeks to address.



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**TESTIMONY OF JAMES N. ARBURY**  
**SENIOR VICE PRESIDENT OF GOVERNMENT AFFAIRS**  
**ON BEHALF OF THE**  
**NATIONAL MULTI HOUSING COUNCIL**  
**NATIONAL APARTMENT ASSOCIATION**  
**BEFORE THE**  
**HOUSE COMMITTEE ON FINANCIAL SERVICES**  
**SUBCOMMITTEE ON HOUSING AND COMMUNITY OPPORTUNITY**  
**H.R. 5039, "THE SAVING AMERICA'S RURAL HOUSING ACT OF 2006"**  
**TUESDAY, APRIL 25, 2006**

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*The American apartment industry...working together for quality, accessible, affordable housing.*

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TUESDAY, APRIL 25, 2006**

Chairman Ney, Ranking Member Waters and distinguished members of this Subcommittee, my name is Jim Arbury I am the Senior Vice President of the National Multi Housing Council, in Washington, D.C. I am responsible for implementing strategy for all legislative and regulatory issues of interest to the National Multi Housing Council (NMHC) and National Apartment Association (NAA). NMHC and NAA represent the nation's leading firms participating in the apartment industry. Their combined memberships include apartment owners, developers, managers, builders and lenders.

The National Multi Housing Council represents the apartment industry's largest and most prominent firms. NMHC members are the principal officers of these organizations. NAA is the largest national federation of state and local apartment associations, with 190 affiliates representing more than 50,000 professionals who own and manage more than six million apartments. NMHC and NAA jointly operate a federal legislative program and provide a unified voice for the private apartment industry.

I am pleased to address the views and opinions of our membership on H.R. 5039, the "Saving America's Rural Housing Act of 2006". While the number of NMHC and NAA owners and developers serving rural areas is a small component of our overall membership, supporting their efforts to provide safe, decent, affordable rental

housing is no less important than those that are engaged in such efforts in urban and metropolitan areas. We are here today as an advocate for a stronger, more responsive Rural Housing Service (RHS) preservation program that offers a balanced approach and which is fair to the owners and managers of rural multifamily housing, as well as those served by this critical housing stock. We see H.R. 5039 as a major step towards this goal. Legislation that addresses the research and recommended actions sought by the United States Department of Agriculture (USDA) and addresses most of the issues that housing providers face in the market will go a long way toward ensuring that decent affordable housing continues to be available.

I would like to focus my comments on key elements of the legislation in an effort to help the Subcommittee take the appropriate action to move this important legislative initiative forward.

Before I discuss the housing issues related to Rural Housing, I would like to offer some background on the apartment industry in general and alert you to our ongoing concerns with regard to hurricane recovery issues.

#### **INDUSTRY OVERVIEW**

Apartments account for about 14 percent of the entire housing stock, and approximately 16 million American households live in apartments. These households represent the full spectrum of America's population; they are young and old, single and married, wealthy and poor. Rental housing is an important economic driver in the American economy. Apartment revenues total almost \$120 billion annually, and apartment management is responsible for approximately 550,000 jobs. More than 200,000 new apartment homes have been built each year for the past three years at an average value of \$26 billion annually, and this construction activity supports jobs for more than 220,000 workers. Apartments are owned by a wide range of investors, including individuals, partnerships, real estate investment trusts, publicly-traded corporations and nonprofit organizations. They are financed by an array of lenders including commercial banks, thrift institutions, life insurance companies and government-sponsored enterprises. A growing share of the financing comes from publicly traded mortgage-backed securities.

**BALANCED HOUSING POLICY**

Housing and community development have become top priorities for many communities in recent years, fueled by a worsening affordable housing shortage and growing citizen calls for more livable communities and a better quality of life.

Unfortunately, there is a growing disconnect between the country's housing needs and federal housing policy. As it has for the past 50 years, national housing policy continues to emphasize homeownership almost exclusively. While homeownership is a worthy goal for many families, it cannot solve many of the country's most pressing housing challenges.

Raising the homeownership rate will not solve the affordable housing shortage. It will not create homes for many nurses, teachers, fire fighters and police officers who cannot find shelter reasonably close to their jobs. It cannot hope to house the estimated 13 million immigrants who will come to this country in the next 10 years or the nation's nearly 74 million Baby Boomers as they age and find single-family housing too difficult to manage. For many of America's most pressing challenges, from suburban sprawl to affordable housing, apartments are a much better solution.

By 2030, there will be 94 million more people in the United States than there were in 2000. And all of these people need somewhere to live, somewhere to work and somewhere to shop. If the country hopes to accommodate this population growth without giving up all green space and adding to the nation's pollution and traffic congestion, Americans need a more balanced housing policy that explicitly recognizes and values apartments and rental housing.

Apartments help create stronger and healthier communities: by offering enough housing for the workers that businesses need; by reducing the cost of providing public services, such as water, sewer and roads; and by creating vibrant live/work/play neighborhoods.

Not only are apartments needed, but a growing number of Americans want them. For generations, married couples with children dominated housing markets. But today those families are less than 25 percent of American households. In their place are young professionals, childless couples, empty nesters and single parents who want the conveniences, amenities, shorter commutes and financial freedom that apartment life gives them.

The National Apartment Association (NAA) and the National Multi Housing Council (NMHC) seek a more balanced housing policy for our nation, one that respects the rights of individuals to choose housing that best meets their financial and lifestyle needs. NAA/NMHC urge decision-makers at all levels of government to work with the apartment industry to craft a smarter national housing policy that:

- Ensures that everyone has access to decent and affordable housing, regardless of his or her housing choice;
- Respects the rights of individuals to choose the housing that best meets their financial and lifestyle needs without disadvantaging, financially or otherwise, those who choose apartment living;
- Promotes healthy and livable communities by encouraging responsible land use and promoting the production of all types of housing;
- Recognizes that all decent housing, including apartments, and all citizens, including renters, make positive economic, political and social contributions to their communities; and
- Balances the expected benefits of regulations with their costs to minimize the impact on housing affordability.

#### **HOUSING HURRICANE EVACUEES**

Hurricane Katrina will go down in the record books as the nation's largest and most costly natural disaster ever. According to Red Cross estimates, at least 416,894 housing units across the Gulf region were destroyed, nearly ten times more physical damage than any previous U.S. natural disaster. In addition, 85,000 housing units suffered major damage and 130,000 suffered minor damage. Forty-seven percent of

the units destroyed throughout the region were rental units; in New Orleans 55 percent were rental units.

The record-breaking 2005 hurricane season caused the largest mass migration of Americans in the past 150 years, leaving more than one million people homeless.

As our nation struggled to recover from this unprecedented disaster, one of the most pressing needs was to find safe and decent housing for hurricane victims. Moving displaced families from temporary shelters into more suitable housing is the first step in helping them rebuild their lives. These are extraordinary times that call for the private sector and the federal, state, and local governments to respond accordingly.

In the immediate aftermath of hurricanes Katrina and Rita, the apartment industry stepped up to the plate and took a leadership role in the relief efforts to house the displaced people of Louisiana, Mississippi and Alabama. The response was immediate, creative and generous.

In the early days following Katrina, federal officials reached out to the apartment industry, and the industry responded enthusiastically by submitting thousands of available units into a national database. They also answered FEMA's call for blocks of apartments that the agency could rent directly.

When it became clear that the federal government was not going to quickly offer official guidance or assistance to house the newly homeless evacuees, the apartment industry initiated several programs of its own. In Texas, where the largest number of evacuees were sent, many NMHC and NAA member firms forged relationships with local charities and created programs to award free rental units and other support services to needy families. In all, more than 400 free apartments were donated to the United Way and the Urban League.

Around the country, apartment owners submitted their available units into a national housing registry, [www.hurricanehousing.net](http://www.hurricanehousing.net), complete with offers of waived security deposits, reduced rents, flexible leases and other concessions.

The first few months of the recovery effort were marked by a series of different FEMA assistance programs, nearly constant changes in rules and deadlines and a level of confusion and chaos. Three different government assistance programs were created to help move the evacuees out of shelters and hotels. Some people are eligible for housing assistance through a special Katrina voucher program created by the U.S. Department of Housing and Urban Development (HUD), others can receive housing assistance directly through FEMA's Individuals and Households Program, and still others are being helped by FEMA-funded city voucher programs through the FEMA public assistance programs.

The information provided to both the evacuee and the apartment owners remains inadequate and continues to lead to significant confusion. In many cities, rents promised through the voucher programs remain unpaid. Many evacuees, unaware that their assistance checks could only be used for rent, used the money instead for pressing needs like food, clothing and medicine. Even now, nearly eight months after the hurricane, the evacuees face new issues which range from having to become experts with regard to FEMA housing programs and in some cases evacuees in Texas are just learning that they do not qualify for assistance. As you can imagine this is an option that neither the evacuee or the housing provider likes to have to address.

At present we are supportive of language in H.R. 4939, the "Emergency Supplemental Appropriations Act for Defense, the Global War on Terror, and Hurricane Recovery" passed by the House on March 16, 2006 and the Senate Appropriations Committee on April 5, 2006. The legislation will be brought to the Senate floor, today, April 25, 2006. This legislation provides for much-needed housing assistance funds for the victims of Hurricanes Katrina and Rita.

We are particularly interested in Section 2501 of the bill, which grants the Federal Emergency Management Agency (FEMA) the authority to provide funds to a state or local entity to pay for utility costs associated with the thousands of leases currently in place. This is important because limitations of the Stafford Act prevent FEMA from allowing the payment of these costs through the Individuals and Households Program (IHP), which is a primary source for housing assistance. Under prior program funding, evacuees entered into apartment leases that covered the cost of rent and utilities, but they are at risk of losing utility coverage as they transition to the Individuals and Households Program. Without this provision, evacuees will incur additional financial obligations they did not anticipate and may not be able to pay. In addition, prevention of such payments interferes with the contracts in place between the evacuees and housing providers.

The apartment industry continues to do its part to house evacuees. However, it is essential that we operate with clear and consistent rules. Commitments were made, leases were signed and evacuees are being housed. To deny payment of utilities is unnecessary and certainly harmful to the evacuees as well as to the apartment owners who have generously opened their doors to evacuees.

We look forward to working with the Administration, Congress, FEMA and HUD to resolve current problems and develop solutions for the future.

We commend you, Chairman Ney, for your leadership, and we thank the Members of the Subcommittee for your valuable work addressing the important issue of housing. We appreciate the dedication of the Subcommittee on this issue.

#### **REVITALIZING AND RESTRUCTURING EXISTING 515 RENTAL HOUSING**

In the area of revitalization of the current Section 515 rental housing stock, we support the approach in H.R. 5039 to look at the long-term needs and provide sound tactical actions such as restructuring debt, providing grants and deferring principal and/or interest payments. Much of the problem today has to do with properties that are in need of maintenance and repairs, but do not have adequate cash flow to

support the needed improvements. Addressing the underlying debt is a critical component to creating the needed cash infusion and to create a long-term cash reserve program to ensure a long-term solution to the existing portfolio. This action in tandem with the creation of a long-term viability plan incorporates the physical needs assessment with the debt restructuring to ensure that proper reserves are funded to ensure the long-term housing need the properties are intended to serve.

However, we are concerned with the capacity and expertise of the Rural Housing Service (RHS) to administer such a program. Based on the 2003 data from the 2004 ICF Consulting study commissioned by the USDA Rural Development, there are over 15,800 properties in the program accounting for over 430,000 units. The assumptions of the report by ICF notes that the Rural Housing Administration will need to restructure and address between 7,900-11,850 properties in this portfolio. This task would be daunting for a large institutional commercial real estate firm let alone the RHS. Our concern is that the need to address policy, create regulations and to oversee the administration of such an effort may be beyond the current capacity of the RHS. Based on feedback from members, current program operations are inconsistent throughout the RHS state and district office network due to a range of resources and skills among RHS field personnel. Some owners have not received responses from RHS offices to prepayment requests for over 15 months. We would encourage you to carefully examine the large task presented by this legislation to make sure that the legislation can be implemented properly. This will be critical given the large number of properties and the unique nature of real estate at the property level. Using the model that was established for the Section 8 Housing Program restructuring, through the creation of the Office of Multifamily Housing Assistance Restructuring (OMAR) seems to be a reasonable approach. We believe it could assemble the resources necessary to address the problems that were unique to each property and focus on the housing needs at the property level. It could more effectively leverage the existing resources in the field and take a more comprehensive and consistent approach to the problem.

**RENTAL ASSISTANCE AND VOUCHERS**

Key to providing adequate low-income housing is the need to provide subsidy to the resident's rental obligation. However, we are concerned with the needed budget authority that rental assistance will place on the RHS to ensure adequate long-term rental assistance. We support the need for a maximum tenant rent of no more than 30 percent of income, however, it must be recognized that the need for continued subsidy will be required to support the properties financially, including the funding of reserves for replacement to ensure the long-term viability of the properties.

Keeping owners vested in the property continues to grow more challenging as these properties are subject to increased fixed and largely uncontrollable expenses that constantly increase such as energy and utility costs, property taxes, other local taxes and fees, and insurance. With income fixed based on the need to meet the needs of low-income families, a sound resident subsidy funding program is key to keep owner's focused on maintaining the real estate and to provide them with the needed long-term investment needs that create the critical partnership between government and the private sector.

We remain greatly concerned regarding budget authority and the assumption that the RHS will not have the funds to serve the housing needs through adequate rental assistance - - that there will be problems with payments that will stem from the annual budgetary process as has occurred in other government rental assistance programs.

**PREPAYMENT OF OLDER PRE-1990 SECTION 515 LOANS**

H.R. 5039 addresses a critical issue and provides a sound approach to addressing the loan prepayment rights of long-term owners that secured loans before December 15, 1989 and whose loan documents do not prohibit prepayment. While some may see this as a loss of needed housing, it is but one small part of the existing stock and will allow the RHS to focus attention on the inventory that will remain in the inventory and requires minor to significant rehabilitation.

Our concerns with H.R. 5039 as it pertains to prepayment of 515 loans that were funded before December 15, 1989 relate to the process to notify tenants, the RHS and others regarding prepayment of sale of the property. We support the need for adequate resident notification. Fewer residents will be adversely affected by augmenting the current resident support with a voucher system will allow impacted residents to secure alternative housing. The 90 day notification period is not problematic, but H.R. 5039 is not clear what specific trigger is to be used for an owner to implement the 90 day notice period. We would recommend that the owner notify the residents and the RHS of its intent to prepay the loan at the time the owner has made that final decision.

We are also concerned with the "sale restrictions" provisions in H.R. 5039 prohibitions on the sale of the property to any purchaser other than one who will extend the use restrictions for 20 years. Such requirements do not appear in other government loan programs and how this restriction will be applied is not specified other than the owner may not engage in a sale for a 75 day period. It is unclear when the period begins and ends, other than it seems to coincide with the 90 day notification period. Seeking a new owner that will agree to extend the long-term affordability may seem reasonable, but it should take place as a right of refusal process, not as a process forced upon the owner. We would recommend a period not to exceed 60 days, following the receipt and acceptance by an owner of a contract purchase offer, for any party to submit a valid offer without further contingency from any party, including non-profit or government organizations, that is not less than the initial contract offer accepted by the owner.

We would welcome the opportunity to work with the Committee to resolve any of these issues.

#### **RELATED AFFORDABLE HOUSING LEGISLATION**

Mr. Chairman, I commend a related bill to the attention of the Subcommittee. H.R. 3715, the "Affordable Housing Preservation Tax Relief Act of 2005," that was introduced last September by Representatives Ramstad and Cardin. The bill would

implement an important recommendation made to Congress in 2002 by the Millennial Housing Commission designed to preserve federally assisted affordable housing. In a nutshell, the bill would provide “exit tax” relief to apartment owners, including owners of Section 515 properties, who sell their properties to new owners who commit to preserving their affordability. The legislation is intended to address the problem of owners who are hesitant to sell federally assisted housing to preservation purchasers because of the capital gains tax burden they would face upon the sale. The bill has attracted support from across the housing spectrum, ranging from our organization to the National Low Income Housing Coalition, the American Association of Homes and Services for the Aging, the Council for Affordable and Rural Housing, the National Council of State Housing Agencies, the National Housing Trust, the National Leased Housing Association, the Enterprise Foundation, and the Local Initiatives Support Corporation, among others.

#### **CONCLUSION**

We are here today as an advocate for a stronger more responsive RHS preservation program that offers a balanced approach and which is fair to the owners and managers of rural multifamily housing, as well as those served by this critical housing stock. We see debate on H.R. 5039 as a vital step towards this goal. Legislation that addresses the research and recommended actions sought by the USDA and addresses most of the issues that housing providers face in the market will go a long way toward ensuring that decent affordable housing continues to be available.

Thank you very much and I will be happy to respond to any questions you may have.

April 20, 2006

Statement Thomas Carew, Frontier Housing, Morehead, Kentucky, regarding  
H.R. 5039, The Saving America's Rural Housing Act of 2006

Mr. Chairman and Members of the Committee (Financial Services)

Frontier Housing is a non-profit corporation providing housing solutions for low income Eastern Kentuckians since 1974. We serve an area of nine (9) counties in North Eastern, Appalachian, Kentucky. Five of these counties are, unfortunately listed in top 100 poorest counties of the United States. This area includes two Congressional Districts, the Fourth and the Fifth. I have attached as part of my testimony two maps from the Appalachian Regional Commission indicating Poverty Rates in Appalachia as of 2000 and County Economic Status as of Fiscal year 2006. As can be seen in the map indicating Economic Status six of the counties in our service area are Distressed (red) the remaining three are At Risk (tan). The Poverty rate map indicates that three of the counties, have poverty rates ranging from 27.6% to 45.4% while the remaining 6 counties have rates from 19.4% to 27.5%.

H.R. 5039 introduced by Congressman Geoff Davis, (R-KY 4<sup>th</sup>) addresses certain issues affecting the Section 515 Rural Rental Program of the United States Department of Agriculture's Rural Housing Service, formerly known as the Farmers Home Administration. The 515 Program has financed approximately 12,000 units in approximately 454 projects across the Commonwealth of Kentucky. Many of these units are in our service area, and provide decent housing for the poorest of the poor.

H.R. 5039 addresses the issue of an owner's right to pre-pay the Rural Housing Service (henceforth RHS) on developments financed prior to December 15,

1989, and secondly the bill puts forth a program that would enhance the revitalization of the majority of Section 515 Developments on a voluntary basis.

We applaud the provisions of the bill, which create financing mechanisms which will enable the revitalization of many units in the 515 stock. In my previous position at the Commonwealth of Kentucky's Housing Finance Agency, Kentucky Housing Corporation, we found it very difficult to assist a developer wishing to revitalize a 515 project. The existing RHS regulations essentially prohibited other financial partners from participating in a financial restructuring, and an injection of new capital to rehabilitate an older project. The Bill includes provisions for the following financial enhancements: reduction or elimination of interest on the loan, partial or full deferral of payments, forgiveness of loans, subordination of loans, reamortization, and grants. In return for the Government's new investment the owners would have to agree to new property use restrictions for a period of not less than 20 years. These financial enhancements will enable other partners, such as Housing Finance Agencies, to participate in the revitalization of a project, thus making better housing available for very low income families.

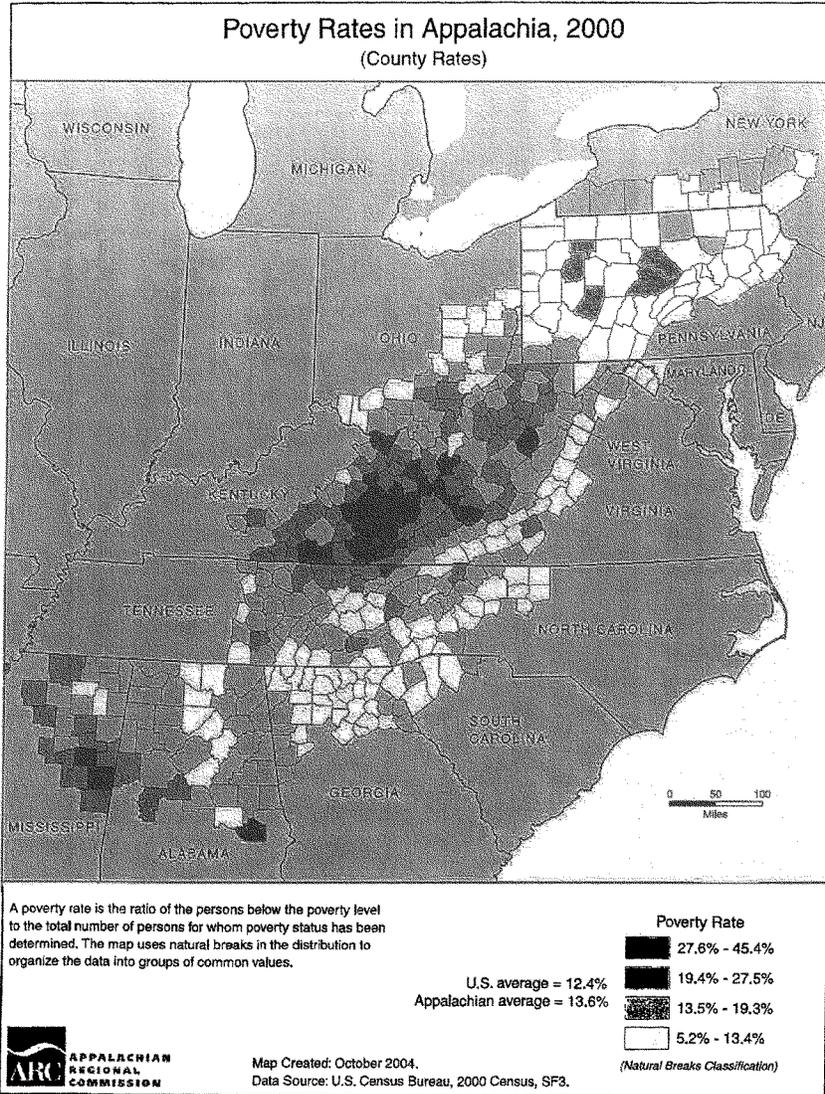
The Bill also addresses the pre-payment of projects financed prior to December 15, 1989. Recent settlements in the U.S. Court of Claims in favor of project owners have raised the concern of many as to the cost of keeping pre- 12/15/89 units in the Section 515 program. As many of you know the RHS over the past 12 or so years has drastically reduced the funds available to construct new 515 projects to the point where there is little to no new construction. This raises the concern that if we are to lose thousands of affordable units across America, how will they be replaced? Does it make sense to give up the units we have now for an investment we made years ago and pay today's prices to replace the units? The cost to replace these units surely will cost more than to keep them in the program? What funding is on the horizon to replace these units at affordable rents? Generally speaking the tools we have today, Tax Credits, HOME, the Affordable Housing Program of the Federal Home Loan Bank, State Trust funds,

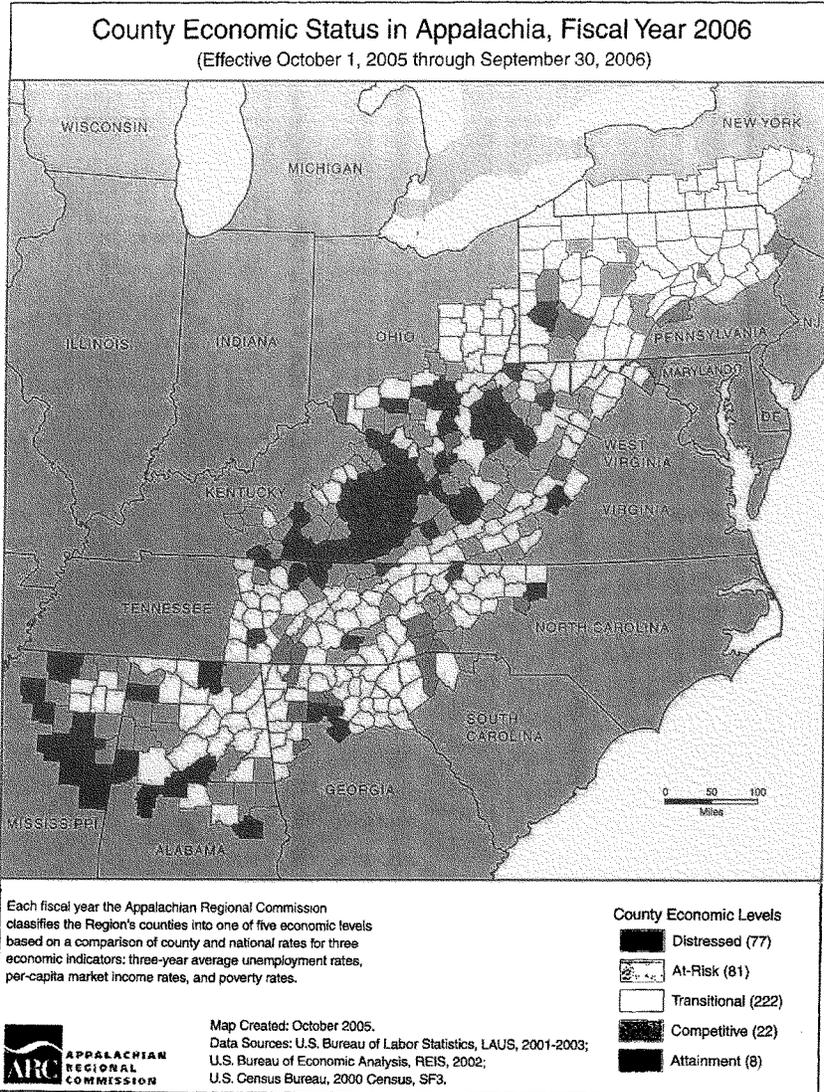
and other State-provided financing will not begin to be able to replace the affordable units we might lose in the 515 program. No other national Program can match the 50 year 1% (the interest rate could go as low as 1%) financing made available through the 515 program.

The Bill does provide a mechanism for housing vouchers for tenants who would be displaced as a result of pre-payment. There are some technical corrections that should be made in the bill to clarify when a tenant is eligible to receive a voucher. Tenants should be eligible if they are a resident on the date the owner notifies the tenants of their intention to pre-pay. Tenants should have the option of using the voucher to remain in the existing project. We recommend that the bill use the HUD Section 8(t) language: "the assisted family may elect to remain in the same project in which the family was residing...". There are some budgetary questions related to the vouchers: will there be sufficient funds to provide the needed vouchers? How long will the vouchers last? These questions should be addressed. Should the number of units coming off line be limited or tied to the number of vouchers budgeted in a specific fiscal year? In other words if we lose 1000 units in a given fiscal year to pre-payment; should there be 1000 new vouchers available for the displaced tenants?

I think we need to recall why the Section 515 program was created: to provide, safe, decent, housing for the poorest rural Americans. If we are unable to preserve the units we have, then we should look at a mechanism to replace the units we lose. This Bill provides some excellent tools to revitalize those units which remain in the program, and provides a pre-payment mechanism for those developers looking to leave the program. I would respectfully challenge the Committee to create a new program or adequately fund the existing Section 515 program to finance the construction of new replacement units at affordable rents.

Mr. Chairman, and members of the Committee thank you for this opportunity to comment on H.R. 5039. I applaud your work on behalf of the housing needs of Rural Kentuckians, Rural Americans.





**Statement of Russell T. Davis, Administrator of USDA Rural Housing and  
Community Programs, before the Subcommittee on Housing and Community  
Opportunity.**

Mr. Chairman and members of the Subcommittee, thank you for the opportunity to present the Bush Administration's initial comments on H.R. 5039, the "Saving America's Rural Housing Act of 2006."

Let me begin by acknowledging and thanking the sponsors and cosponsors of H.R. 5039 for their leadership on this important issue. Mr. Chairman, we appreciate the fact that you have been personally interested in this bill, as well as Congressman Geoff Davis and Congressman Barney Frank. The quality of thought and effort are evident throughout. We also thank everyone involved with this legislation for their work and the experience they have brought to the process.

There is an urgent need to address long-standing and severe issues of deferred maintenance and economic imbalances in the rural multi-family housing portfolio. This initiative will ensure continued viability of thousands of multi-family housing properties

and hundreds of thousands of units for years to come. I am grateful that we have stepped up to that challenge.

We believe the basic strategy outlined by this legislation will work. The two new housing mechanisms in this bill – rural vouchers and debt restructuring – are in fact already being implemented on a demonstration basis with a promising response.

First, let me mention our voucher demonstration program. On April 7, 2006, USDA Under Secretary for Rural Development, Thomas Dorr, issued the first Rural Development vouchers to tenants of Wedgewood Apartments in Hinesville, Georgia, in a property where the borrower had just prepaid its multi-family housing loans. These vouchers provided roughly \$240 per tenant per month and allowed those tenants to remain in their apartments, despite a post prepayment rent increase of about 45 percent. USDA is issuing vouchers both through its field offices and through HUD under an interagency agreement.

Second, the early results of our Restructuring demonstration are also extremely encouraging. As of the close of the application window on April 17, 2006, approximately 4,000 Section 515 property owners have applied to undergo debt restructuring. This represents 25 percent of the total portfolio. These results indicate a tremendous interest among the ownership community in seeking a resolution to the revitalization challenge. I look forward to working with Congress to develop and pass legislation that protects these assets for the low-income rural housing tenant population.

H.R. 5039 is the product of extensive and ongoing discussions among members of Congress, the Administration, and USDA Rural Development. It is heartening that these discussions have been bipartisan and that H.R. 5039 is broadly compatible in approach with the Administration's proposed legislation. The Administration therefore supports this bill, with certain clarifications which I will describe shortly.

#### **Administration's Proposal**

The Administration's revitalization proposal was circulated on the Hill in August of 2005. That draft legislation addressed three critical needs faced by USDA's Rural Housing Programs' Section 515 multi-family housing program: (1) enhancing tenant protections through vouchers when a property owner leaves the program by pre-paying a loan; (2) creating an equitable new agreement with property owners electing to stay with the Section 515 program; and (3) using debt relief as the primary tool to stabilize properties at risk of physical deterioration.

To revitalize properties in the program, the Administration's legislation proposed to restructure the owners' current loan. The restructurings are targeted to the properties that need rehabilitation in the near future, and would be limited to properties placed in service before 1992.

The restructurings would be accomplished through a negotiated process in which USDA would employ a "toolbox" of financial incentives and disincentives to secure another twenty years of decent, safe, and affordable housing for low-income rural tenants, at the

lowest cost to the Federal government. By utilizing a variety of restructuring tools we can ensure that post-restructuring rents are as close to pre-restructuring rents as possible. A fundamental principle of our revitalization study was that restructuring tools are more cost effective in the long run rather than extensive, open-ended tenant subsidies.

One way to look at this restructuring process is to view it as a “fix-up vs. build” decision: it costs \$85,000 on average to build a new affordable housing unit, but only \$20,000 per unit to rehabilitate what we currently have. The vision, then, is to secure the valuable national asset of a large affordable rural rental housing portfolio, for the longest period, at the lowest cost to the government, at the greatest benefit to tenants, owners, and communities.

To provide for the property’s physical rehabilitation, the Administration’s proposed legislation provided the owners with greater flexibility in operating their properties and managing their capital contributions. Deterioration is causing unnecessary increases in costs, and a new capital structure is needed to attract private sector investment.

Loans older than 15 years could go through a financial restructuring. The properties’ budgets reserve requirements, and possibly Section 515 debt levels, would be adjusted to provide more cash flow for rehabilitation. In addition, the securing of outside capital from owners, third parties, housing tax credits, etc. would be encouraged. In return, owners would enter into a “Long-term Use Agreement” with USDA to maintain affordable rents and housing for up to 20 additional years.

Ultimately, the Administration's proposed legislation would help shore up the multi-family housing portfolio so that we continue to provide decent, safe, affordable tenant based housing to the current residents within the portfolio.

The 2007 Budget supports these changes by requesting \$74 million for vouchers and debt restructuring.

**H.R. 5039**

We are pleased that H.R. 5039 reflects the Administration's vision for addressing multi-family housing program concerns. Like the Administration's proposed legislation, H.R. 5039 would protect rural residents from rent overburden when borrowers prepay their loan. The bill would also allow property owners to restructure their loans to provide cash for rehabilitation; in return rural America keeps a valuable multi-family housing property affordable for rural residents.

The differences between the Administration's proposal and H.R. 5039 are, in the main, minor, and we look forward to working with the Subcommittee to address these issues. One such item is that H.R. 5039 would set a maximum tenant contribution of 30 percent for restructured properties. We recognize that this is an understandable policy goal as an attempt to address the 'overburdened' tenant. This approach recognizes that the Section 515 program as currently structured protects some tenants more than others: some low-income tenants receive rental assistance while others do not; and some pay higher percentages of their incomes than do others. As a matter of what social scientists call

'horizontal equity,' many supporters of the Section 515 program desire to broaden the income subsidy nature of the program.

There are, however, significant countervailing considerations. Because the Administration places its highest policy priority on protecting tenants, we have given serious attention to both sides of the equation. We cannot, however, support the bill's 30 percent maximum rent provision.

First, by imposing a lower, and across-the-board, maximum rent cap, H.R. 5039 is likely to greatly expand the cost of preserving these properties. The initial cost of this provision understates its financial impact, because the legislation does not limit the number of beneficiaries of the rent cap to just those residents overburdened at the time of restructuring, but would require that Rural Development provide Rental Assistance to an unknown number of future overburdened residents as well.

Second, the Administration places a high premium on a market-based restructuring in which owners have an economic incentive to respond to market forces. This is also consistent with the policy goal of maintaining a mixed-income tenant population. These yield important social benefits and allow for a more inclusive representation of the rural communities in which these properties are located. A completely tenant subsidy-based property undermines these objectives.

Third, by preserving some degree of market constraints on property owners, the Administration's approach creates a long-term incentive for holding down costs and maintaining property quality. It also eliminates the incentive for owners or managers to seek windfall returns by under funding maintenance and repairs while recruiting tenants willing to accept substandard conditions.

Finally, the Administration's approach recognizes that current overburdened tenants did, in fact, enter willingly into their current rental arrangements with their landlords and are paying their rent. Additionally, existing law already provides the authority to extend rental assistance to the overburdened, and that the matter of doing so should be left to the appropriation process. Particularly in an austere budget environment, there is no reason to extend an unsolicited subsidy to people who are successfully meeting their obligations.

If the maximum rent provision remains in H.R. 5039, at a minimum, we strongly recommend that certain controls be put in place, such as:

- (a) Limiting additional Rental Assistance (RA) funds to only residents in units that are overburdened at the time of restructuring. As written, H.R. 5039 contains no such limits. For example, under the bill, should an overburdened resident making \$10,000 per year move out of a property and be replaced by a tenant with \$1,000 income, the cost of RA (to be incurred by Rural Development) would rise dramatically. Under this scenario, it would be impossible to provide accurate predictions of the future amounts of RA that would be needed. Alternatively, if

the RA were limited to the amount present at the time of restructuring, everyone would be able anticipate annual costs, both present and future.

(b) Limiting potential beneficiaries to tenants or applicants without current HUD assistance, either tenant or project-based. We believe that the Section 515 program will in the long run be on a stronger footing by preserving multiple sources of tenant assistance.

#### **Conclusion**

The Administration applauds members of Congress for taking this very important first step. We remain committed to protecting tenants, while also focusing the remaining resources on the essential long-term purpose of the legislation, the revitalization initiative. The modest changes to H.R. 5039 – very reasonable controls – would achieve this goal. We believe that these modifications would significantly enhance the efficiency and effectiveness of the revitalization initiative. USDA Rural Development looks forward to working expeditiously with Congress on this important legislation.



**Housing Assistance Council**  
1025 Vermont Ave., N.W., Suite 606, Washington, DC 20005, Tel.: 202-842-8600, Fax: 202-347-3441, E-Mail: hac@ruralhome.org  
www.ruralhome.org

**Statement of  
Moises Loza, Executive Director,  
Housing Assistance Council  
before the Committee on Financial Services,  
Subcommittee on Housing and Community Opportunity,  
U.S. House of Representatives  
April 25, 2006**

Thank you for the opportunity to submit testimony to the Subcommittee on H.R. 5039, the Saving America's Rural Housing Act of 2006, and thank you, Chairman Ney, for holding this important hearing. My name is Moises Loza and I am the Executive Director of the Housing Assistance Council, a national nonprofit organization dedicated to improving housing conditions for low-income rural Americans. Let me say first that HAC appreciates the effort that has gone into this legislation by you, Rep. Davis, Rep. Frank, and all of your hardworking and committed staff.

The Housing Assistance Council (HAC) was established in 1971 and is celebrating its 35<sup>th</sup> anniversary this year. HAC provides financing, information, and other services to nonprofit, for-profit, public, and other providers of rural housing.

Throughout its existence, HAC has been active in efforts to preserve decent, affordable rental housing for the low-income and very low-income rural tenants who often have no other housing options. HAC convened blue ribbon task forces in 1991-92 and, with the National Housing Law Project and with support from the John D. and Catherine T. MacArthur Foundation, in 2004-2005, to make major rural housing preservation policy recommendations. In 2005 the U.S. Department of Agriculture awarded HAC \$2,000,000 under its new Preservation Revolving Loan Fund program to assist owners and purchasers with preservation efforts, to which HAC has added \$500,000 from its existing loan funds. HAC sponsored a national rural housing preservation conference in 2005 and will hold a preservation training conference in May 2006. In addition, the organization has published research reports, guides for nonprofit organizations and public agencies, numerous articles, and a special issue of its quarterly magazine on the topic.

The Housing Assistance Council views the Saving America's Rural Housing Act of 2006 as a step towards resolving serious issues regarding the availability of decent, affordable rental housing for low-income rural Americans. At the same time, HAC suggests some changes to the bill to strengthen its protections for the existing housing supply and for low- and very low-income rural tenants.

My testimony includes a brief overview of rural rental housing conditions and needs, then focuses on HAC's suggestions for H.R. 5039 and other steps to meet these needs.

**Building  
Rural  
Communities**

***Celebrating  
35 Years  
1971-2006***

**Southeast Office**  
600 W. Peachtree St., N.W.  
Suite 1500  
Atlanta, GA 30308  
Tel.: 404-892-4824  
Fax: 404-892-1204  
southeast@ruralhome.org

**Western Office**  
131 Camino Alto  
Suite D  
Mill Valley, CA 94941  
Tel.: 415-381-1706  
Fax: 415-381-0801  
western@ruralhome.org

**Southwest Office**  
3839 San Pedro, N.E.  
Suite C-7  
Albuquerque, NM 87110  
Tel.: 505-883-1003  
Fax: 505-883-1005  
southwest@ruralhome.org

**Midwest Office**  
10920 Ambassador Drive  
Suite 220  
Kansas City, MO 64153  
Tel.: 816-880-0400  
Fax: 816-880-0500  
midwest@ruralhome.org

HAC is an equal opportunity lender.

### **RURAL RENTAL HOUSING**

The nearly 5 million rural households (about one-quarter of the total) who rent their homes suffer some of the worst housing problems in the United States. Housing costs are their most significant problem. More than one-third of them are cost burdened (i.e., they pay over 30 percent of their income for housing).

Rural renters are twice as likely as owners to live in physically substandard housing. Approximately 12 percent of nonmetro renters live in either moderately or severely inadequate housing; for minorities, the rate rises to 18 percent.

Worst case needs, as defined by the Department of Housing and Urban Development, afflict one in every four very low-income renter households in nonmetropolitan areas. That is, they are extremely cost burdened and/or inadequately housed, and they do not receive federal housing assistance. The vast majority of these households are severely cost burdened, paying more than half of their income for their housing costs.

Elderly people often face some of the worst housing conditions. In many rural areas, if a low-income senior cannot find an affordable apartment, her choices are likely to be a nursing home or relocation to an unfamiliar urban area.

USDA Rural Development's Section 515 rural rental housing program, particularly when coupled with the Section 521 rental assistance program, provides decent, affordable homes for rural renters. Data just released by USDA RD show that as of January 2006 the average income for a Section 515 household is \$9,785. For those receiving Section 521 rental assistance, the average is \$7,836. There is not enough rental aid for those who need it: 17 percent of Section 515 tenant households are cost-burdened (that is, they pay more than the federal standard of 30 percent of their income for housing costs). The majority of Section 515 tenants (59 percent) are elderly or disabled and 94 percent have very low incomes (that is, they earn less than half the median income in their areas).

Section 515 has proven extremely successful at providing decent, affordable housing for the lowest income rural Americans. The majority of Section 515 apartments were built before 1995, however, and many of these older buildings need significant physical repairs or updates. At the same time, a substantial number of Section 515 loans may be paid off, potentially enabling their owners to convert the units to market rents and displace current tenants. Yet preserving these units has become expensive for the government.

### **THE SAVING RURAL AMERICA'S AFFORDABLE HOUSING ACT**

H.R. 5039 would establish two new ways to deal with Section 515 properties. First, owners of most developments financed before December 15, 1989 would be permitted to prepay their mortgages and a new voucher program would be created to protect tenants. Second, almost all Section 515 properties would be eligible for a revitalization/refinancing program.

### ***Prepayment***

HAC's primary concern is ensuring the availability of decent, affordable rental homes for current and future tenants. To that end, HAC has long supported the protections for rural rental housing units established by the Emergency Low-Income Housing Preservation Act (ELIHPA).

HAC recognizes that enforcement of ELIHPA has become expensive for the government with respect to properties financed before December 15, 1989. HAC appreciates that this bill, unlike the draft legislation released by USDA in summer 2005, would retain prepayment restrictions on properties financed after December 15, 1989, pre-1989 properties subject to use restrictions, and Section 514 farm labor housing developments. If ELIHPA is to be repealed for other pre-1989 properties, HAC believes tenants will be best protected by permitting prepayment only if vouchers are available or if sufficient decent, available rental housing in the market area is affordable to Section 515 tenants without subsidies.

The bill also authorizes USDA to give priority for new construction of Section 515-financed units to areas that need the housing because of prepayments. While HAC supports replacing prepaid units where they are needed, federal funds could be better used to avoid prepayment, for example by encouraging transfers of property ownership, than to replace prepaid units.

### ***Vouchers and Tenant Protection***

HAC supports the inclusion of vouchers in this bill, since vouchers can help low-income tenants afford to rent on the open market when landlords are willing or required to accept vouchers and affordable units are available. To best protect tenants, HAC suggests several changes in the bill's voucher provisions.

First, vouchers should be available to tenants who live in the property on the date of the owner's notice to the tenants, not only to those who live there on the date of prepayment. This change would enable tenants to explore alternative housing, and to take advantage of available opportunities, before prepayment actually occurs.

Second, the bill seems intended to require prepaying property owners to accept vouchers, as they are under HUD's Mark to Market program. HAC supports that intent. The bill's wording may need some clarification, however. Its provisions that vouchers "may be used" and "may be provided" imply an option rather than a requirement. Also, it refers to "communities with insufficient affordable housing alternatives," implying that tenants in communities with alternative housing may not be eligible for vouchers. To indicate clearly that USDA tenants have the same rights as HUD tenants, this bill could use the language of HUD's Section 8(t): "the assisted family may elect to remain in the same project in which the family was residing . . .".

HUD tenants' rights could also inform this bill's provisions that, while allowing USDA vouchers to be used anywhere in the country, would link their value to the market rent in the area of the prepaid property. When HUD tenants move, their Section 8(t) vouchers convert to standard Housing Choice Vouchers with the accompanying portability features. Because USDA vouchers could become costly if tenants move from relatively inexpensive small towns to pricey cities, unrestricted portability may not be the best choice for USDA's voucher program. For some tenants, however, such a move may be the best option. HAC suggests, therefore, that the bill make an exception to the value limit for elderly or disabled tenants who move to expensive areas to be close to family members or essential services.

Finally, the bill should protect tenants when a property owner allows its loan to become delinquent so that USDA will accelerate payments, enabling the owner to pay the loan in full without requesting approval for prepayment. It is not clear whether or how often owners use this tactic but, if and when they do, their tenants should be eligible for vouchers on the same terms as those in prepaying properties.

### ***Revitalization***

H.R. 5039 would provide numerous useful options for restructuring project financing to enable owners to revitalize their properties. Revitalization, particularly when it involves a transfer of ownership, would be further aided by allowing consolidation of loans, consolidation of owner entities, and coverage of management fees for nonprofit owner/managers.

Relatively small, but useful additional assistance for revitalization transfers could be provided by enhancing USDA's existing authority to make grants to cover due diligence expenses for nonprofits and public agencies purchasing properties. First, at present these grants are available to nonprofits and public agencies purchasing during the prepayment process, but are not available for transfers of ownership outside the prepayment process. Instead, they should be available to any purchaser accepting 20-year use restrictions, not solely to nonprofits, and for any transfer of ownership, whether or not connected to a loan prepayment. Second, until this year, these grants were capped at \$20,000 each, an amount insufficient to cover purchasers' upfront costs, which can be as high as \$100,000. USDA's appropriations legislation increases the limit to \$50,000 for fiscal year 2006, a provision that should be made permanent.

HAC also suggests minimizing the cost of revitalization by excluding Low Income Housing Tax Credit investors' capital from the calculation of return on investment. The tax credits alone are effective incentives for investors to participate, so it is not necessary to provide an additional return on their investment. The added return would simply add to the revitalization cost – a cost that must be borne by the government (that is, by U.S. taxpayers) or by the tenants despite their low and very low incomes.

At the same time, the bill would create a disincentive for prepayment-eligible owners to choose revitalization. At the end of the loan term the owner would repay to USDA the lesser of all writedowns, write-offs, subsidies, and grants, or 75 percent of appraised value. If prepayment were clearly unprofitable, a pre-1989 owner might choose revitalization, but an owner who could profit by prepaying a loan – in other words, an owner in a strong real estate market where affordable housing is likely to be needed – would be unlikely to refinance and revitalize with use restrictions if that option would be unprofitable in the long run. The profit-sharing provision should be revised to give owners an incentive to select revitalization rather than prepayment.

### ***Rights of First Refusal***

The bill tries to create two rights of first refusal, an idea HAC strongly supports. To ensure these provisions are effective, their language should be clarified and funding should be provided to assist entities exercising these rights.

In the prepayment context, the bill provides that for the first 75 days after notifying USDA that it wants to prepay, an owner could sell only to a purchaser that would accept 20-year use restrictions. The owner would not, however, be required to bargain in good faith if it received

such an offer, to sell to a preservation purchaser if the offered terms were reasonable, to provide an opportunity for the preservation purchaser to match other offers, or even to give preference to that purchaser. HAC recommends revising the bill's language to establish a clear right of first refusal for a purchaser that would accept 20-year use restrictions. The bill should also, like ELIHPA, require active advertising to such purchasers. In addition, a time period longer than 75 days could be useful for purchasers that must investigate financing and conduct due diligence before making an offer.

The bill also attempts to provide a right of first refusal for tenants in the revitalization context. It would give an owner the option to offer a property to the tenants for purchase as a cooperative or condominium in conjunction with revitalization. The owner is not required to extend such an offer, however, nor to give preference to the tenants, to negotiate in good faith, or to sell if reasonable terms are offered. Again, HAC recommends establishing a clear right of first refusal.

#### ***Rent Levels***

HAC appreciates the provisions of H.R. 5039 that limit rents to 30 percent of income for tenants in revitalized projects and tenants with vouchers. HAC does not understand, however, why the bill accepts USDA's request for establishment of a minimum rent for tenants in revitalized properties. USDA officials have stated that a minimum rent will help combat fraud based on underreporting of income, but USDA already has the authority to verify tenants' incomes. Creating a new administrative process to determine which tenants should be exempted from the minimum income requirement seems unlikely to add to the agency's ability to obtain accurate verifications.

In addition, the standards for annual rent increases in revitalized projects seem unnecessarily complex. The bill would require USDA to establish standards for affordable rents, rather than tying rent increases to project operating costs, as the agency does now. USDA's administrative costs could be reduced by adopting the Department of Housing and Urban Development's Fair Market Rents (FMRs) instead of creating its own standard, and its rent subsidy costs by allowing rents to increase to the higher of (1) area FMRs or (2) levels based on project operating costs.

#### ***Other Provisions***

HAC suggests a few other revisions to the process that would be created by H.R. 5039. First, the bill would require USDA to create a database of potential purchasers, but does not specify how the database should be used. The bill should state clearly that owners must use the database to provide notice to the public of requests to prepay. In addition, rather than limiting the database to entities that have expressed an interest in purchasing properties, the bill should allow any interested entity to be included.

USDA would be required to implement "a plan to administer requests to prepay" within 90 days after the bill is enacted into law. It is not clear whether a plan means something different than regulations. HAC suggests requiring regulations rather than a plan, since regulations provide an opportunity for public comment, an important factor in developing a new program. A new program also deserves sufficient time for thoughtful preparation of regulations and careful consideration of public comments, and those activities are likely to require more than 90 days.

The bill currently does not authorize specific dollar amounts for revitalization costs or vouchers. These should be added.

***Producing New Units***

Finally, HAC observes that rural America needs not only preservation of existing decent, affordable rural rental housing units, but also production of new units.

USDA's budget proposal for 2007, like others in the last few years, proposes to finance construction of new rural rental units through the Section 538 rental guaranteed loan program. Section 538, however, serves a higher-income population than Section 515, up to 115 percent of area median. The governing law makes USDA Section 521 rental assistance unavailable for Section 538 developments.

Rent subsidies also cannot end rural America's rental housing problems. Too often rural areas simply do not have enough decent, affordable rental units available. Furthermore, funding for HUD's Section 8 vouchers, which help tenants pay rent for market-rate housing, is being frozen or reduced despite increases in rent costs. In some rural places, HUD vouchers are not available because administering agencies do not exist everywhere.

Section 515 properties, especially those with Section 521 rental assistance, are able to serve extremely low-income tenants. HAC encourages the Subcommittee to support increased annual appropriations for the Section 515 program and/or creation of a new rural rental production program.

**CONCLUSION**

The Housing Assistance Council appreciates the efforts of Congress and the Administration to address the serious issues connected with the aging rural rental housing stock. It will not be easy to meet the national housing goal, stated in the Housing Act of 1949, of providing "a decent home and a suitable living environment for every American family." Preserving the current homes of tens of thousands of low-income rural tenants, and continuing to produce new homes for others, will be important steps in that direction.

Thank you very much.

## MOISES LOZA

**Housing Assistance Council**  
 1025 Vermont Avenue, NW, Suite 606  
 Washington, DC 20005  
 (202) 842-8600  
 Fax (202) 347-3441  
 moises@ruralhome.org

## EXPERIENCE

March 1989 to Present. *Executive Director*, Housing Assistance Council (HAC), Washington, DC  
 Chief Executive Officer of national nonprofit corporation that works to increase the availability of decent housing for rural low-income people. Governed by a national board of 30, the organization has four regional offices and provides technical assistance, training, research and has a revolving loan fund of over \$50 million to help develop housing for low-income families and underserved populations in rural areas. Created in 1971, HAC has loaned over \$125 million which have helped build approximately 40,000 housing units in 49 states. The organization also conducts legislative, policy and program analyses.

1981 -1989. *Deputy Executive Director*, Housing Assistance Council, Washington, DC

1978 -1981. *Area Director* (Senior Executive Service) Farmers Home Administration, U.S. Department of Agriculture, Washington, DC

Supervised ten State Directors, annual allocations of \$2 billion, over 30 community development programs, personnel, and other activities in 11 Western States, American Samoa, Guam, and Western Pacific Trust Territory. Administered policy, regulations and operating procedures. Responsible for program implementation, targeting of funds, equal opportunity and public affairs.

1973 - 1978. *Deputy Assistant Director*, Housing Assistance Council, Washington, DC

Assisted in managing program of legislative, policy and program analysis and provided technical assistance in low income housing to States, local governments, public bodies and nonprofit organizations.

1973. *Senior Researcher*, Equal Employment Opportunity Commission, Chicago, IL

Reviewed and analyzed discrimination cases investigated by EEOC to determine if civil suits were advisable to U.S. Government; collected data and evidence for lawsuits; assisted staff attorneys with preparation of briefs and motions for federal courts; assigned and supervised research work of six (6) paralegals.

1972 -1973. *Housing Development Consultant*, Interstate Research Associates, San Antonio, TX

Worked in all aspects of housing development for low and moderate income families; gave technical assistance to community groups; packaged farm labor housing built in South Texas; set up a housing development corporation in South Texas; worked closely with various groups in the Southwest.

1971. *Housing Specialist*, Center for Community Change, New York City, NY

Administered contract between Appalachian Regional Commission, HUD and the Center for Community Change to work with the Pennsylvania Department of Community Affairs to assist and prepare nonprofit groups for sponsorship of low-income housing; worked with 15 groups.

1970 - 1971. *Executive Associate*, Educational Systems Corporation, San Antonio, TX  
 Provided technical assistance to migrant and seasonal farmworker organizations in Texas and Oklahoma in areas of management, special education, child care, English as a second language; prepared curricula and training instruments; wrote articles to publicize problems and opportunities for farmworkers; developed a management instrument for use by organizations to improve management and administration of programs.

1969 - 1970. *Urban Intern*, U.S. Department of Housing and Urban Development, Regional Office, Fort Worth, TX

Reviewed employment practices of urban renewal, model cities, public housing, HUD area offices and HUD contracts; assisted and advised users of HUD programs of their equal employment responsibilities per Civil Rights Act, Executive Orders, OFCC, etc. Investigated alleged discrimination by HUD program users; assisted contractors with Affirmative Action Plans and reviewed them in behalf of U.S. Government. Received certificate of commendation for work in disaster area in New Orleans area.

#### **EDUCATION**

B.A. in InterAmerican Studies  
 Pan American University, 1969; Edinburg, TX

Certificate of Completion on graduate work in housing development,  
 Housing Specialist Institute, 1971; Washington, DC

Certificate of Completion in Executive Leadership and Management,  
 Federal Executive Institute, 1979; Charlottesville, VA

Accounting, U.S.D.A. Graduate School, 1985-86; Washington, DC

#### **PROFESSIONAL AFFILIATIONS**

Cooperative Housing Foundation, Board Member  
 Fannie Mae Foundation Knowledge Network, Advisory Committee  
 Freddie Mac, Affordable Housing Advisory Committee  
 Low Income Investment Fund, Board Member  
 National Community Reinvestment Coalition, Board Member  
 National Hispanic Housing Council, Chairman  
 National Low Income Housing Coalition, Treasurer  
 National Housing Conference, Board Member  
 National Rural Housing Coalition, Vice President  
 Rural Development Leadership Network, Chairman  
 United States Delegate to United Nations Conference on Human Settlements,  
 Habitat II, Istanbul, Turkey, 1996

#### **OTHER**

Read, write and speak Spanish fluently

# **NATIONAL RURAL HOUSING COALITION**

1250 Eye Street, N.W., Suite 902, Washington, D.C. 20005 • (202) 393-5229 • fax (202) 393-3034

**STATEMENT**

**OF**

**ROBERT A. RAPOZA**

**NATIONAL RURAL HOUSING COALITION**

**BEFORE**

**SUBCOMMITTEE ON HOUSING**

**&**

**COMMUNITY OPPORTUNITY**

**COMMITTEE ON FINANCIAL SERVICES**

**U.S. HOUSE OF REPRESENTATIVES**

**APRIL 25, 2006**

# NATIONAL RURAL HOUSING COALITION

1250 Eye Street, N.W., Suite 902, Washington, D.C. 20005 • (202) 393-5229 • fax (202) 393-3034

My name is Robert Rapoza and I am Executive Secretary of the National Rural Housing Coalition. The Coalition is a national membership organization that advocates for federal policies which improve housing and community facilities in rural America. We have previously appeared before this subcommittee, and we greatly appreciate the opportunity to testify today on behalf of H.R. 5039, The Saving America's Rural Housing Act, which would strengthen the U.S. Department of Agriculture's Section 515 loan program for the future.

Before I discuss the merits of the legislation, I would like to provide a brief overview of the Section 515 program, its appropriations history, as well as describe some of the challenges it currently faces.

## **Background and Section 515 Appropriations**

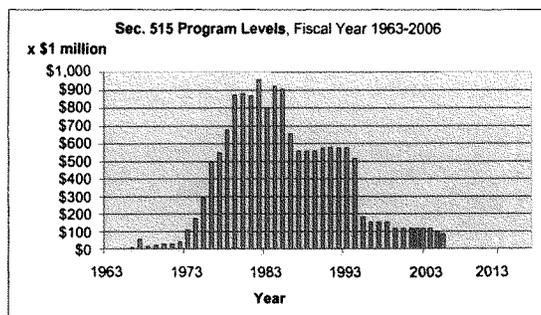
The Coalition has long supported the Section 515 program as the best and most affordable way to provide affordable housing to low income families and senior citizens in rural areas. In these communities, the only affordable rental housing is through the Section 515 program. It is therefore a very important resource for rural America.

Congress established the Section 515 program in 1962 by amending Title V of the Housing Act of 1949. Its purpose was to provide loans for the construction, rehabilitation, acquisition, and operation of rental or cooperative housing for low and moderate income rural elderly people. The U.S. Department of Agriculture was to serve as the lender of last resort – that is, borrowers had to prove that they could not access comparable private financing. The Agriculture Department set their 515 loan terms between 33 and 50 years, and they were expected to “graduate” from the program by repaying their loans as soon as they had the financial means.<sup>1</sup>

The program began making loans in 1963 and has since financed more than 526,000 units. As a result, it has helped alleviate acute shortages of safe and affordable rental housing in rural areas across the United States. Today, the Section 515 loan portfolio serves approximately 475,000 households.

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<sup>1</sup> The preceding discussion and Exhibit 2: Evolution of the Section 515 Program are based on histories provided in: National Task Force on Rural Housing Preservation, *Preserving Rural Housing* (Washington, D.C.: Housing Assistance Council, 1992), 6-8; and U.S. Department of Agriculture, Farmers Home Administration, *A Brief History of Farmers Home Administration* (Washington, D.C.: U.S. Department of Agriculture, 1990), 6-8.



As the chart above indicates, funding for the Section 515 program peaked between 1979 and 1985. During this period, annual budgets exceeded \$864,000,000 and the Agriculture Department's Rural Housing Service made a total of 9,622 loans. The program then underwent steep cuts in the mid-1990s when Congress, seeking opportunities to balance the budget, found that some property owners had defrauded the program. Although RHS eliminated these abuses and made the regulatory changes that Congress suggested, Congress never fully restored the program's funding. In Fiscal Year 2006, Congress provided only \$99,000,000 for Section 515 loans.

In the current budget climate then, the Coalition believes that it is vital to preserve the current portfolio of Section 515 developments. The Administration's Fiscal Year 2007 budget, however, proposes to eliminate this program and replace it with a \$74,000,000 voucher initiative. The budget promises to submit legislation authorizing the use of these funds for restructuring assistance as well.

### **Preserving Rural Rental Housing**

The current funding situation demonstrates the need for the Rural Housing Service to preserve the assets it has already developed. There are now approximately 15,000 Section 515 properties throughout the United States. The developments constitute a priceless asset for rural America where more than 900,000 renters live in moderately or severely inadequate housing, and 1,900,000 people are rent-overburdened.<sup>2</sup>

In 2003, the average annual tenant income in these properties was \$9,168. Seventy-five percent of tenants received a rental assistance subsidy, either through project-based rental assistance, the Section 8 program, or through vouchers. Although rents were extremely low, averaging \$314 per unit per month, 20% of tenants were nevertheless rent-overburdened and 7% paid more than half their income toward rent.

<sup>2</sup> These tenants pay more than 30 percent of their incomes toward rent.

In many rural communities then, Section 515 housing is the only affordable option. It is an essential resource for elderly people, single-parent families, the disabled, and other less mobile residents. It provides them with an alternative to living alone in housing they cannot maintain; residing in overcrowded or other substandard conditions; living in their cars; or moving to a nursing home.

Section 515 housing also is generally well managed. Property managers often invest much of their own free time and creativity in providing tenants with a safe and cohesive community. They organize social get-togethers and, at some elderly properties, they arrange for services such as health screenings and grocery and pharmaceutical delivery.<sup>3</sup> The Section 515 portfolio is also financially sound, with a loan delinquency rate of just 1.6% and only eight properties in inventory.<sup>4</sup>

Nevertheless, the Section 515 program faces some major challenges. For example, numerous owners wish to prepay their loans but statutory restrictions impede their ability to do so, despite the fact that they are also eligible for Rural Housing Service-funded monetary incentives to remain in the Section 515 program. In addition, 89% of Section 515 properties are ten years old or older and in need of significant rehabilitation. The Rural Housing Service lacks sufficient funding to meet the need for the incentives as well as for rehabilitation. Its preservation efforts rehabilitate only 3% all units in the portfolio each year, and it now faces lawsuits from owners who want compensation and/or the right to prepay. It is vital then that these concerns are addressed so that the Section 515 program can continue to provide these vital services to rural America.

### **Overview of Prepayment Issues**

It is also important to trace the evolution of the Section 515 program and the prepayment process in order to show how the Rural Housing Service's lack of funding for incentives and rent subsidy vouchers has hurt both owners and tenants.

The Rural Housing Service faces approximately many lawsuits for prepayment-related lawsuits and cannot meet the demand for preservation incentives. At the same time, it is losing more units to prepayment than it is building.

Starting in 1968, six years after the Section 515 program was established, non-profit organizations and consumer cooperatives could qualify for "interest credit," which reduced the interest rate on their loans to as low as 1%. The interest credit resulted in rents lower than at properties developed by for-profit entities, which received market-rate loans and offered market-rate rents. In the first decade of the Section 515 program, most

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<sup>3</sup> U.S. Department of Agriculture, Rural Development, Rural Housing Service, *Rural Housing Service 1997 Progress Report* (Washington, D.C.: U.S. Department of Agriculture, 1998), 12, 24.

<sup>4</sup> Rural Housing Service, Office of Rural Housing Preservation, untitled PowerPoint presentation, January 2004.

borrowers were locally-based non-profit organizations and small “mom and pop” for-profit investors.

In the late 1970s, however, the Rural Housing Service found itself balancing competing pressures. Rising property values in rural areas enabled a growing number of owners to prepay their loans. Given the agency’s history of enforcing the requirement that they “graduate” from the program by repaying their loans as soon as they had the financial means, the owners expected they could do so. As a result, there was a sharp increase in prepayment activity, with 55% of all prepayments since the program’s occurring between 1977 and 1979.<sup>5</sup>

At the same time, tenant advocates began mobilizing to halt this trend, since prepayments often led to dramatically increased rents and the eviction of very low income tenants. Advocates argued that owners had reaped tax and other benefits at the taxpayers’ expense, and that they should not be allowed to profit even more by converting their properties to market use.

Congress responded by passing the Housing and Community Development Amendments of 1979 (P.L. 96-153). This law requires that properties with Section 515 loans made on or after December 21, 1979 serve low income residents for 15 or 20 years, depending on the level of the Section 515 interest rate subsidy. Congress also placed prepayment restrictions on existing, pre-1979 loans but repealed these restrictions in 1980.

As the federal tax benefits to those participating in the Section 515 program began to expire during the 1980s, more owners prepaid. The resulting displacement of large numbers of tenants, many of which were elderly, generated much publicity and controversy. In response, Congress mandated a moratorium on prepayments in October 1986, which remained in effect until the Emergency Low-Income Housing Preservation Act (ELIHPA, P.L. 100-242) became law in 1988. While creating financial incentives for borrowers with pre-1979 loans not to prepay, ELIHPA also restricted their prepayment rights, a provision that directly contradicted the Rural Housing Service’s mandate that these owners graduate from the Section 515 program as soon as they were financially feasible.<sup>6</sup>

In order to eliminate the prepayment issue for all new housing, Congress then passed the Department of Housing and Urban Development Reform Act of 1989 (P.L. 101-235), precluding prepayment for all Section 515 loans made on or after December 15, 1989. Congress then extended prepayment prevention incentives to borrowers with loans made between December 21, 1979 and December 14, 1989 through the Community Development Act of 1992 (P.L. 102-550).

The Rural Housing Service’s framework to process prepayment requests combines statutory and regulatory requirements then. What this process means for

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<sup>5</sup> National Task Force on Rural Housing Preservation, p. 8.

<sup>6</sup> *Ibid.*, p. 9.

owners qualified to prepay is that (a) they may be able to receive financial incentives to stay in the program; (b) they may be able to prepay without any further obligations; (c) they may be required to carry out the remainder of their restrictive use provisions or protect the existing tenants, after which they can do what they want with the properties; and (d) they may be required to sell at fair market value to a non-profit or public agency. Eventually, owners who do not accept incentives and are not required to sell may therefore convert their properties to market-rate use.

#### **Lack of Funding for Preservation Incentives**

Preservation incentives include equity loans; increased return on investments; Section 8 rents in excess of the amount needed to meet annual operating, maintenance, debt service, and reserve expenses; increased rental assistance; and interest rate write-downs to 1% and/or loan reamortization over the remaining life of the property. Demand for incentives always exceeds supply.

From 1989 to 1994, the Rural Housing Service's total equity loans ranged between \$11,000,000 and \$27,000,000 annually. In 1995, however, when appropriations for the Section 515 program dropped from \$512,000,000 to \$183,000,000, the amount of funding for prepayment equity fell as well. Since this time, the Agency has made approximately \$5,400,000 in prepayment prevention equity loans each year, thereby preserving approximately 1,000 units annually.<sup>7</sup>

For Fiscal Year 2006, the Rural Housing Service has allocated \$4,950,000 to equity loans. Of that amount \$950,000 is available for transfers to non-profits or public bodies. The current backlog of demand for equity loans is about \$20 million. Approximately \$44,000,000 is allocated for repair and restoration of Section 515 developments.

Supply is also uncertain because the amount of rental assistance that Congress appropriates varies from year to year. For example, the current rate for debt forgiveness is \$8 million. In the Fiscal Year 2007 budget, the amount of "debt forgiveness" rental assistance was eliminated. The Rural Housing Service uses debt forgiveness rental assistance also to supplement equity loans. It is therefore vital to making prepayment prevention incentives work for properties that do not have full rental assistance coverage.

The fundamental issue regarding Section 515 prepayment, however, is the lack of resources to provide incentives for long-term use, the financing of the repair and rehabilitation of developments, and rental subsidies for tenants that may be displaced.

#### **Comments on HR 5039**

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<sup>7</sup> In Fiscal Year 2003, RHS provided a total of \$21.5 million in equity loans. However, only \$5.8 million was for prepayment prevention incentives. RHS also made \$10.5 million in equity loans to transfer 20 Idaho properties to a new owner, per the settlement agreement of *Atwood-Liesman v. United States*. Finally, RHS made \$5.2 million in equity loans to support innovative transfers outside of the prepayment process.

In 2004, the Department of Agriculture released an assessment of the Section 515 program. It also noted that over 10% of the portfolio is located in hot markets and that owners in those areas may be financially able to convert the projects to other uses. The report correctly recognized that capital is needed to repair and revitalize its portfolio. The Department's report also indicated that the vast majority of the remaining projects are in markets where their best use is as affordable housing. The report projects the cost to repair and restore the developments at \$2.6 billion over 20 years.

The policy recommendation stemming from this report is that the government should allow these hot market projects, and presumably others the right to prepay. The report contends that the vast majority of projects are in markets where their only use is as low income housing so with some revitalization they may be preserved for use under section 515 or similar programs. This is more or less the policy framework for HR 5039.

We appreciate the work of the sponsors in attempting to craft legislation to solve these difficult issues. H.R. 5039 is a substantial improvement over previous drafts that were circulated. The bill narrows the number of projects eligible for prepayment and establishes a much needed restructuring program with a favorable maximum rent requirement. We also support the right of first refusal provision and would like to work with the Committee to strengthen the legislative language. In addition, we appreciate the tenant notification provisions but believe that they may be improved, particularly with respect to providing more notice to tenants. Therefore, in the details of the legislation, there is much to support, and we believe that we can work with the Committee to improve the other provisions.

The Coalition has concerns, however, with the overall framework for the legislation. H.R. 5039 repeals provisions of current law – particularly 502(c) of the Housing Act of 1949 -- that regulates prepayment of Section 515 developments and establishes incentives for their long term use. If this bill becomes law, it is possible that families living in Section 515 units will be displaced without assistance and without alternative housing.

As we have noted, the population in Section 515 developments is low income and mostly elderly persons with disabilities. It is not a very, mobile population either. In many rural communities, the only decent affordable housing in town is the Section 515 developments. If those units disappear, many families may have no place to go.

In 2004, the Committee considered H.R. 3995 which proposed changes to the Section 515 prepayment process. The Committee agreed to make prepayment contingent on tenants having a voucher and the owner agreeing to take the voucher. H.R. 5039 does not contain this provision, which means that low income and elderly tenants could be displaced without vouchers and without a place to live.

In cases of prepayment it is possible that the Rural Housing Service will move quickly, as they recently did in Georgia, to get vouchers to families. It is also possible that an owner may decide to convert the Section 515 financed housing to some other use

and not accept vouchers. In that case, how likely is it that displaced families will receive a voucher and find alternative affordable housing in the community?

We support preserving Section 515 projects. The Coalition therefore believes that it is far more preferable to continue current law under Section 502(c) of the Housing Act and provide adequate incentives to owners for long term use.

While we know a lot about the current status of the portfolio, we do not know how owners and tenants will react to prepayment, displacement, and restructuring. There may be some answers in the Fiscal Year 2006 Agriculture Appropriations Act though. In that bill, Congress included \$16,000,000 for vouchers for displaced families designed along the lines of the Section 8 program. The appropriations legislation also included \$9,000,000 for a portfolio restructuring demonstration. The Rural Housing Service has recently released a Notice of Funding Availability (NOFA) for those funds. A total of \$173,000,000 of assistance in the form of deferred mortgages, revitalization grants, subordinated debt subsequent loans, transfer and consolidations as also included in the bill. We urge the Committee to monitor the implementation of the restructuring and the voucher program funded in this year's appropriations process.

As some contend, it may that owners would rather have assistance for restructuring and stay in the program. As a result, there will be fewer prepayments and displacements than originally predicted. However, we do not know if that will be the case. The Coalition therefore believes it would be useful for Congress to see the Fiscal Year 2006 voucher and restructuring work before enacting such far reaching legislation as H.R. 5039.

#### Comments and Recommendations on HR 5039

##### A. Prepayment

The legislation allows prepayments of section 515 loans made prior to December 15, 1989 provided that these projects have met their 20 year restrictions and have not received not received preservation incentives and have not had any servicing actions. Loans made after the December, 1989 date did not include the right to prepay. The legislation requires a 75 day right of first refusal for buyers willing to maintain the project as affordable housing for at least 20 years. Owners are required to give 90 days notice to tenants of the prepayment.

NRHC recommends that the right of first refusal language be strengthened and the 90 day notice period be extended to at least 180 days. ( section 544 (j) (B)

##### B. Vouchers

The bill authorizes vouchers, along the lines of section 8. The tenant contribution on the vouchers is in most cases 30% of income. An owner who prepays may not refuse a voucher for a household living in the project. For communities with a lack of affordable housing, USDA can provide an enhanced voucher as authorized under the section 8 statute.

NRHC Recommendation: The bill does not contain a dollar authorization for vouchers and that is obviously necessary to provide future appropriations.

C. Restructuring:

The bill authorizes a restructuring assistance program. In return for such assistance, the owner must agree to a use restriction of an additional 20 years or the balance of the loan term whichever is longer. The legislation establishes a planning process for the owner and USDA to determine the need of the physical and financial needs of the project, future rents (that are affordable to eligible households under section 515) and projects a rate of return to the owner that is comparable to other, similar properties. Restructuring assistance can include reduction or elimination of interest on the loans, deferral of loan payments, loan forgiveness, subordination of the loan, re-amortization of the loan, grants payments of project cost for the long term plan of the project, third party investments and a direct loan or guarantee. At the end of the use restriction term USDA and the owner divide the proceeds. Maximum rents for restructured projects are 30% of income. Minimum rents are set at the lower of 30% of income or \$25.

NRHC strongly supports that maximum rent provision as a way to ensure that restructured projects continue to be affordable to low income families.

D. Section 544 (j)(1)(B) authorizes the Secretary of Agriculture to process any request for section 515 prepayment regardless of implementation of other provisions of this legislation. We urge the Committee to revise this provision. If the intent of this legislation is to preserve as many units as possible within section 515 and to protect tenants by having vouchers available, then RHS should have those resources authorized in this bill available before prepayments are processed.

Thank you for this opportunity to testify. I would be happy to answer any questions the Committee might have.



**Council for Affordable and Rural Housing**

*Serving the Affordable Housing Needs of Rural America*

Testimony of Robert L. Rice, Jr.

On

H.R. 5039, "Saving America's Rural Housing Act"

The U.S. House of Representatives  
Committee on Financial Services  
Subcommittee on Housing and Community Opportunity

April 25, 2006

**TESTIMONY OF ROBERT L. RICE, JR. ON H.R. 5039 ON BEHALF OF THE  
COUNCIL FOR AFFORDABLE AND RURAL HOUSING  
BEFORE THE SUBCOMMITTEE ON HOUSING AND COMMUNITY  
OPPORTUNITY, HOUSE COMMITTEE ON FINANCIAL SERVICES**

**APRIL 25, 2006**

Mr. Chairman and Members of the Subcommittee:

I am Robert Rice, president of Crest Realty of Frankenmuth, Michigan. I have been involved in the rural housing industry for over 30 years. My company is a full service real estate company with an emphasis on the management of affordable multifamily housing. I am appearing here in my capacity as President of the Council for Affordable and Rural Housing ("CARH").

CARH is a national organization headquartered in Alexandria Virginia. Our membership is comprised of for-profit and non-profit developers, managers, owners, syndicators, public agencies and others interested and involved in providing affordable housing to low-income families in rural areas. Thank you, Mr. Chairman, for holding hearings today on H.R. 5039, "Saving America's Rural Housing Act of 2006."

The major federal program to subsidize rental housing in rural areas, Section 515 of the Housing Act of 1949, has been operational for over 40 years, back to the early 1960's. The program reduces the cost of operating a project by providing construction loans with an interest rate as low as one percent. It became apparent, however, that families at the lowest income levels could not reasonably afford to pay the rent needed to cover the full operating costs of the project, including the build-up of reserves, and

repayment of the principal of the loan plus interest at one percent. In the mid-1970's a program of rental assistance was authorized which provides subsidy to keep rental and utility costs to very low income tenants at 30 percent of their adjusted income.

Approximately 57 percent of the roughly 460,000 units in the 515 program are occupied by tenants with rental assistance.

Rents for 515 units must be approved by the Rural Housing Service ("RHS"). Over the years, RHS has tried to balance the need for adequate rents to support a project with the reality that the 515 subsidy is often too shallow to serve the lowest income ranges. Although rental assistance, where it is available, is very helpful, RHS has attempted to stretch limited budget resources for that program by keeping rents lower than prudent for the long-term viability of projects. Rents and rental assistance, system wide, have been held down too far for too long, creating a crisis in resources. Coupled with the fact that owners, by and large, have not been allowed out of the program to recapitalize, a situation has been created often referred to as a "toll road with no exits".

We are gratified, therefore, that RHS two years ago conducted a comprehensive review of the condition of the 515 housing stock and proposed remedial legislation to correct the imbalance between income and expenses for many projects and to facilitate the injection of new capital and equity into the projects. This "revitalization" program will involve budget authority for the reduction, elimination or deferral of debt service on a 515 loan and for grants in some cases. The assistance is in the form of a deferred loan, repayable by the owner at end of the 515 loan term. To process efficiently a large volume of projects, RHS should use the services of private entities and state and local

agencies to develop project financial plans, particularly those entities that gained experience by participating in HUD's mark-to-market restructuring program, and we are pleased that H.R. 5039 authorizes the use of outside contractors..

The success of this revitalization program, as contained in H.R. 5039, depends on how well it is administered by RHS, and whether rents are established and periodically adjusted at adequate levels to meet operating costs and to maintain reserves to pay for future capital needs.

In this regard, a provision in H.R. 5039 would lessen the effectiveness of the revitalization program by creating a new, unfunded cost to the program. H.R. 5039 imposes a maximum rent for all tenants in revitalized projects of 30 percent of adjusted income. The 515 program does not now provide this benefit, and while we agree that such a benefit is desirable, providing an unfunded cost requirement is not reasonable or workable. The rent limitation has to be accompanied by a subsidy component to be workable, such as rental assistance. Otherwise, such a requirement will negate the positive impact of the revitalization assistance provided in H.R. 5039.

Two other parts of H.R. 5039 revise existing loan prepayment restrictions on 515 owners and authorize tenant protection vouchers for low-income tenants in projects whose loans are prepaid. Upon prepayment, not only is the 515 loan subsidy eliminated but any rental assistance is also terminated, thus necessitating a new form of subsidy for tenants.

Legislation enacted in the late 1980's and early 1990's imposed on owners of certain HUD projects and 515 projects restrictions on prepaying their loans and terminating subsidies even though their contracts with the government permitted unrestricted prepayment. Congress ended its restriction on prepayments for HUD project owners ten years ago, in 1996, and authorized enhanced section 8 vouchers to enable tenants either to remain in a project or to move elsewhere. The restrictions on 515 loan prepayments, however, continue to this day. We are pleased that RHS and this Committee are receptive to ending these restrictions.. Extensive litigation over these restrictions on 515 and HUD projects have led to numerous court decisions holding that the statutes were a breach of contract or a Fifth Amendment Taking of contract and property rights, and ordering damages to be paid by the government and in some jurisdictions also requiring prepayment to be accepted by RHS.

The new statutory prepayment framework in H.R. 5039, however, raises several issues. First, it is essential that a notice be given to tenants, RHS, and other interested parties sufficiently in advance of the prepayment date to permit processing of tenant protection vouchers, which involves determining whether the units in the project meet housing quality standards and whether a tenant is eligible for the voucher.

However, H.R. 5039 requires a notice to be given, not 90 days before prepayment, but 90 days before "any action" to prepay is taken. This provision is ambiguous and could lead to disputes and litigation, as well as to a spate of premature notices. "Any action" could apply to any number of preliminary steps an owner might take before deciding whether to prepay, such as conducting a market study, inquiring about a

refinancing loan, applying for a tax credit, or even making an inquiry at RHS about prepayment. Until these preliminaries have been completed and a decision to prepay has been made by the owner, tenants should not be told there will be a prepayment nor should the voucher process be started. Experience with HUD programs indicates that many tenants, particularly the elderly, experience anxiety when told their subsidies will expire, even if informed about vouchers. Some tenants leave their projects prior to prepayment, even though that action disqualifies them for a tenant protection voucher. Therefore, we suggest that notice be given at least 90 days prior to prepayment, a point at which a firm decision to prepay should have been made by an owner.

Second, H.R. 5039 directs RHS to establish a procedure to administer prepayments and requires RHS to “encourage and facilitate” an owner who has decided to prepay its loan to maintain its project as affordable housing to the low-income residents or to sell the project to another owner who will maintain affordability. What this language will entail is unclear but we are concerned that it could lead to delays and roadblocks to prepayment which might constitute new breaches of contracts that provide unrestricted prepayment rights. Indeed, current RHS guidance provides a similar standard and it has led to delays in processing as RHS and program participants have struggled to give this sort of phrase meaning.

Third, H.R. 5039 prohibits an owner who has decided to prepay its loan from selling the project to any purchaser other than a purchaser who will extend use restrictions for 20 years. This prohibition extends for 75 days, all or a part of which could occur before prepayment, with the owner having control over when the 75-day

period starts. We do not know what the point of this prohibition is other than to set a precedent for later expansion. Congress has not imposed such a restriction on the exercise of property rights in any of the HUD programs involving loan prepayment or non-renewal of section 8 contracts. Should this prohibition or a similar one become law, additional litigation could be expected.

Fourth, H.R. 5039 contains unclear provisions that could constitute additional breaches of contract prepayment rights. Owners who in the past accepted incentives from RHS, such as an equity loan, not to prepay, agreed to new or extended use restrictions. When these restrictions expire, the owners have a contractual right to prepay the loan but H.R. 5039 appears to prohibit prepayment even after the expiration of the restrictive use period. A similar prohibition appears to apply after the expiration of restrictive use agreements entered into by an owner in return for RHS approval of a transfer of the project or other assistance to the project.

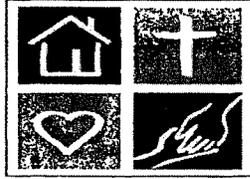
Finally, H.R. 5039 changes current law by prohibiting prepayment during a period in which there is a restrictive use agreement. Under current law, prepayment may be approved by RHS under several circumstances while a use restriction is in effect, such as where RHS finds there no longer is a need for the housing in the area, with the use restriction either terminated or continued after prepayment, depending on the circumstances.

We would appreciate the opportunity to work with the Committee to resolve these issues in a manner that does not create new uncertainties and legal disputes, and that carries out one of the stated purposes of H.R. 5039 “to avoid further costly litigation”.

With respect to tenant protection, we would only note that the language of H.R. 5039 should be clearer as to whether the amount of assistance remains fixed at the year one level or rises as comparable market and project rents rise. We support the latter as providing a better measure of protection, particularly for elderly or disabled tenants, who may want to remain in the same project for several years but would find it difficult to do so if the voucher assistance did not increase as rents increased.

In summary, while we have some issues, which we hope can be addressed, overall H.R. 5039 is promising legislation, and we thank the Administration, the sponsors of H.R. 5039 and this Subcommittee for moving forward the important initiatives contained in this bill.

Thank you very much and I will be happy to answer any of your questions.



**Mercy Housing, Inc.**  
MERCY HOUSING SYSTEM

Testimony of

Charles Wehrwein

Senior Vice President  
Mercy Housing, Inc.

Before the

Committee on Financial Services, Subcommittee on  
Housing and Community Opportunity

U.S. House of Representatives

April 25, 2006

Testimony by

Charles Wehrwein  
Senior Vice President  
Mercy Housing, Inc.

April 25, 2006

Good morning Mr. Chairman. My name is Charles Wehrwein. I am a Senior Vice President of Mercy Housing and have also held posts overseeing multifamily housing programs at USDA's Rural Development and HUD. Mercy Housing has direct and significant experience with owning, acquiring and restructuring federally assisted properties, working within and using the Mark-to-Market program at HUD, using tools made available in the MAHRA legislation passed in 1997, and we led one of the largest rural portfolio acquisitions by a non-profit, know as the Cobble Knoll portfolio in Washington state. I appreciate the opportunity to offer my comments today on HR 5039.

**Introduction: Mercy Housing**

Mercy Housing is a non-profit affordable housing developer, owner and manager headquartered in Denver, CO, with real estate interests in many other regions throughout the nation. In our 25-year history, we have developed or preserved over 18,500 units of affordable housing serving more than 55,000 low-, very low- and extremely low-income Americans on any given day. Mercy Housing regards the preservation of affordable rental housing as essential to the stability and revitalization of communities and the residents who so desperately need this housing, both now and in the future. Mercy and

others who work in the community development field remain deeply concerned about the future of preservation in general and the rural portfolio specifically. Mercy is a member of the Steward of Affordable Housing for the Future, or SAHF (say "SAFE"); whose members include some of the largest non-profit affordable housing developers and owners in the United States. The organization's policy agenda focuses exclusively on policy and marketplace barriers to the preservation and long-term ownership of affordable housing.

**HR 5039**

We would like to extend our appreciation to the bill's sponsors on recognizing the need to respond to the desperate preservation needs of the rural portfolio. The proposed bill is a very good start towards rectifying the issues spelled out in the November 2004 report titled "Rural Rental Housing – Comprehensive Property Assessment and Portfolio Analysis". We would like to offer some suggestions based upon our experience in preservation, and specifically the recent preservation of a large rural portfolio, about how the existing bill can be improved not only to respond to the existing situation, but also to serve as a proactive launching pad to spur preservation by organizations such as ours that intend to provide and extend quality affordable housing for the long term.

Given the brief time available today and the broad experience represented by the other panelists, our comments today will focus on elements of the proposed bill that effect the ease and likelihood of the transfer of these assets to owners who will sustain the housing as affordable for the long term. However, we remain concerned about the adequacy of

funding levels, the impact of the proposals on residents and the permanent loss of the only decent affordable rental housing in some rural areas.

**Case Study: Mercy Housing's Acquisition of the Cobble Knoll Rural Portfolio**

Mercy Housing recently completed the purchase and is finalizing the rehabilitation of a 30 property, 926 unit rural portfolio located throughout Washington State, commonly known as the Cobble Knoll portfolio. Because of the large number of assets, Mercy developed and implemented a plan to acquire the portfolio in 2 phases during 2003 and 2004, in one group of 17 properties and a second group of 13 properties. In September 2003, Mercy acquired the first 17 properties (507 units), located in 12 communities, after 18 months and considerable upfront time and capital spent analyzing the financial and physical condition and arranging financing. Mercy decided to split the portfolio into 2 acquisition phases due to the large number of assets. The purchase price was approximately \$31,000 per unit. We negotiated purchase prices and structured the financing in order to address the capital improvement needs, both immediate and over time, and to ensure the long term financial and physical viability of the housing.

The total development cost of the 30 properties will be about \$42 million, including about \$8,000 per unit in initial repairs and deposits to reserves. The Washington State Housing Finance Commission issued approximately \$10.35 million in tax exempt 501©3 bonds. A major bank purchased the bonds, which have a 30 year term and a fixed rate of interest. Rural Development (RD) originated about \$8.8 million in new Sec. 515 loans and subordinated the \$20.7 million in existing Sec. 515 debt on all of the properties to the

new bondholder. The State Department of CTED provided Housing Trust Funds to each property, which has made it possible for the properties to obtain property tax exemptions, and thus, reduce the operating costs to the government and the owner. Rural Development also provided additional units of Rental Assistance, approved significant increases in rent subsidy necessary to support additional debt and approved increases in annual deposits to replacement reserves in order to fund reserve contributions for future capital improvements. The sellers transferred all existing reserves and accounts belonging to the properties and made a charitable donation to Mercy to reduce the purchase prices.

Mercy Housing's goals in acquiring the Cobble Knoll portfolio were as follows:

- To preserve and strengthen these 926 units of deeply affordable housing for the poor rural seniors and families who depend on this resource;
- To test if rural preservation could be done a large and efficient scale;
- To attempt to structure the new ownership so that it was economically viable for a non-profit with a long-term ownership horizon; and
- To call out the tools that are useful in making rural preservation happen at scale, and the impediments in pursuing this strategy.

Our experiences, in summary are:

- A high-capacity not-for-profit can bring significant benefits to a large-scale transaction;
- Restructuring tools made available to the Department such as subordination, new debt, debt restructuring and in limited cases, debt forgiveness are key to creating

extended affordable use, as is the ability to reallocate rental assistance resources to raise some partially assisted properties to 100% assisted;

- Projects with 100% rental assistance, under either Sec. 8 or Sec. 521 are much more likely to be candidates for a successful restructuring and to be economically viable going forward;
- Project-based rental assistance is critical to achieve effective underwriting from market-sector lenders, with longer-terms providing more comfort and therefore more private-sector resources;
- Projects with partial or no rental assistance, especially those in remote or low cost areas, are extremely difficult to restructure using housing finance tools available today and will likely need debt forgiveness, new or transferred rental assistance and/or grants to be viable;
- The Rural Development field staff is made up of well trained generalists with a strong commitment to this housing and to rural communities in general. However, they have little experience with modern housing finance tools and strategies being used outside of the USDA today;
- The Department lacks expert restructuring agents; and
- The USDA's structure and culture is very decentralized, resulting in poor sharing of best practices, little capability or willingness of the national office to direct strategies based on best practices to the entire field, and a maddeningly variable application of rules from state to state, and even county to county.

As I noted earlier, Mercy Housing has preserved many other affordable homes in addition to the rural acquisition noted above. We have worked with HUD, specifically its offices of Multifamily Housing – OHAP and its predecessor, OMHAR in utilizing the tools commonly know as Mark-to-Market that were established under MAHRA. This experience is entirely relevant to the discussion today, and I would offer a few comments based upon our experiences:

- Creating and empowering a central unit to direct the implementation of preservation policy at HUD is a model of efficiency and good government.
- The team assembled first at OMHAR and now at its successor, OAHF are housing finance and restructuring professionals who delegate effectively to HUD field offices and to contractors (participating administrative entities, or PAEs).
- The policy and implementation of preservation and restructuring acquisitions with this approach have created a relatively smooth and consistent process with the appropriate amount of safeguards and incentives to foster long-term sustainability.
- These tools and their implementation have preserved scores of affordable homes and saved the taxpayers' money.
- I'd like to note that the tools used under MAHRA are about to expire on September 30, 2006, and we would also strongly encourage their extension.

The key tools used by HUD have been:

- Debt restructuring;
- The creation of and ability to assign junior cash flow notes to qualified non-profits; and

- The authority of the Secretary to provide for exception rents in a limited number of instances.

A final point I would like to make about the lessons learned from other preservation experiences is that not all owners share the goals of meeting property needs, assuring renewed and extended affordability, and engaging in long-term ownership. MAHRA specifically recognized the unique role of high capacity non-profit owners, Mercy Housing and others like us are in this for the long haul and our missions are congruent with the government's - to provide decent, safe and sanitary affordable homes for the long run. Promoting the transfer to and restructuring of these assets to qualified non-profits means that Congress will not have to come back to the table with new programs down the road to further extend the affordability of these homes.

#### **Suggestions to enhance the effectiveness of Rural Preservation**

With the foregoing experience in mind, we offer the following suggestions for improving this bill, so that this rare opportunity to change rural housing policy is maximized:

- Create or contract with a unit of expert housing restructuring staff such as exists in HUD's Office of Multifamily Housing – OAHP
- Empower this expert unit to promulgate policy, tools and best practices that will be used consistently across the country; for example, OAHP staff at HUD developed an Additional Funds policy that resulted in a significantly greater amount of rehab per unit.

- For any owner or purchaser seeking it, **require** the Secretary to provide a formal commitment as part of the long-term viability plan, failure to do so would leave the current or future owner uncertain of the Department's ability and commitment to carry through on the commitments and will chill their interest in engaging with the Department
- Provide for the ability to accelerate the replacement of systems that are due to be exhausted or obsolete within the next seven years in order to make better use of the state and local resources, to be consistent with state or local policy around rehabilitation, and to enhance the efficiency of the developer attempting to preserve these units.
- Provide the Secretary with the authority to split current USDA loans into multiple loans, some with fully amortizing terms, others with cash flow only terms, so that this debt might be preserved and used to increase tax credit basis, and therefore the amount of Low Income Housing Tax Credits (LIHTC) that can be attracted to these projects
- Eliminate the 75% rule under Sec 3(b)(6)(B) of the proposed legislation. It will not work with LIHTCs and essential debt products. We would be happy to assist the Committee with new wording that takes into consideration the complicated structure of today's multiple source financings
- Clarify that the 30% rents under Sec. 3(b)(7)(B) of the proposed legislation relates to how much a tenant contributes, not the level at which rents are to be set and that this limit on rental contributions applies only to rental assisted units. Failure

to do so would cause rents to be different for each tenant in all Sec. 515 financed properties.

- The notice of prepayment and sale is too short at 90 days and should be extended to six months to both help the tenants in finding replacement housing if needed, and to provide for more time for interested preservation buyers to become aware of and enter into negotiations with the seller
- Encourage transfer to high capacity not-for-profit owners by:
  - Mandating an Asset Management fee of the greater of \$1,000/unit/year, or \$15,000 per building/per year in the operating budget of the project. Currently, not-for-profit owners have all of the risks and responsibilities of ownership without being appropriately compensated for their internal costs of providing oversight of these assets and reporting to various lenders, governmental regulators and investors.
  - Following on the authority to create junior cash flow notes above, allow for the assignment of these notes to qualified not-for-profit purchasers/owners of Sec. 515 properties to encourage the transfer and long-term ownership of these properties to mission-driven stewards.

This concludes my testimony. We stand ready to assist the Committee, its staff and the Administration in any way possible to assure that the valuable affordable housing

resources created over the years are enhanced and sustained, not lost. Thank you very much for your consideration.

**STATEMENT OF**

**The National Association of Home Builders**

**TO THE**

**House Committee on Financial Services  
Subcommittee on Housing and Community  
Opportunity**

**Hearing on**

**H.R. 5039  
Saving America's Rural Housing Act of 2006**

**April 25, 2006**

The National Association of Home Builders (NAHB) would like to submit for the record a statement on H.R. 5039, "Saving America's Rural Housing Act of 2006," which was recently introduced by Representative Geoff Davis (R-KY). NAHB has long supported the U.S. Department of Agriculture's (USDA) rural housing programs, which are administered by the Rural Development (RD) office. NAHB members place a high priority on providing safe, affordable, high quality housing for rural Americans. While much progress has been made in improving housing in rural America, considerable unmet needs remain, particularly for very-low and low-income rural households. Specifically, there is a significant shortage of affordable rural rental housing and the existing rental stock is aging and in need of renovation.

Therefore NAHB is pleased to have the opportunity to comment on this important bill. H.R. 5039 will begin the process of preserving and revitalizing the Section 515 multifamily rental housing portfolio. The purposes of the bill are to establish and carry out a revitalization program, preserve the availability of affordable rental housing, provide for affordable rents and protect tenants from displacement. NAHB strongly supports these goals. The bill also provides for a repeal of the prohibition against prepayment of pre-1989 Section 515 loans, which NAHB also supports.

NAHB believes that the bill contains the elements that are essential for a successful revitalization and preservation program. For example, H.R. 5039 would allow owners of existing Section 515 properties to voluntarily enter into long-term viability plans with the Secretary of Agriculture. The plan would set forth the terms of the restructuring and would include a comprehensive needs assessment and a financial plan.

Among other provisions, the financial plan would provide the project owner with a long-term rate of return on new capital, including any portion of Low Income Housing Tax Credit (LIHTC) proceeds used for hard construction costs. NAHB supports this provision. However, the preservation deals will also have significant costs not related to hard construction, for example, fees for tax-exempt bond financing (if that is the form of new debt), legal fees and architectural costs. In addition, the acquisition price for the purchase of a Section 515 property in a high cost area would normally include a significant amount of equity being paid to the seller. It would be expected that a large portion of the LIHTC equity raised would be applied to the acquisition price, rather than hard construction, thereby becoming ineligible for an owner's return on investment. NAHB suggests that a long-term rate of return be provided on LIHTC proceeds used for total development costs, rather than just hard construction costs.

H.R. 5039 permits the Secretary to contract with third parties, such as Participating Administrative Entities (PAEs) to administer the program. NAHB supports the use of PAEs to administer the revitalization program. This approach has proven to be successful with the U.S. Department of Housing and Urban Development's (HUD) market-to-market program for its assisted properties. It makes good sense to learn from the experiences of HUD and adopt the practices that have worked effectively as RD implements its program.

Of critical importance, the bill makes voucher assistance available to tenants in properties whose owners prepay their Section 515 loan, thereby ensuring that tenants are protected from displacement. NAHB strongly supports providing voucher assistance to tenants in properties that prepay, including those tenants who were not already receiving rural rental assistance.

The bill requires the Secretary to develop a plan to administer requests to prepay not made in connection with a revitalization plan. The goal is to encourage owners of projects to maintain the projects or transfer them to owners who will maintain them as affordable housing to low-income tenants. NAHB supports the development of such a plan and would appreciate the opportunity to comment on it at the appropriate time.

NAHB also believes that it is worthwhile for the Secretary to encourage owners to maintain their properties as affordable or transfer them to owners who will make the same commitment to housing affordability. NAHB, in its discussions with the RD office, has consistently taken the position that it is worthwhile to try to preserve as many Section 515 properties as possible. However, while the plan should provide for such opportunities, the process should not unnecessarily delay an owner from moving forward on a prepayment request.

Another important element of H.R. 5039 is the provision to give adequate notice to tenants about an owner's intent to prepay. The bill requires the project owner to give notice of prepayment to tenants no less than 90 days before "taking any action" to prepay the loan or sell the project. NAHB supports this notification requirement, but suggests that "taking any action" is somewhat ambiguous and may cause confusion as to what constitutes "taking action." More precise language would ensure that tenants are receiving accurate and timely notice and that the owner is not delayed because of disagreements over whether timely notice was provided. NAHB recommends that the language be revised to require that notice be given no less than 90 days before the date of prepayment.

The bill also provides that an owner must agree to terms that determine how the proceeds of a sale are to be divided at the end of the restructured loan period. The owner must pay the lesser of the sum of all loan write-downs, write-offs, interest subsidies, outstanding principal and interest and any non-loan funds provided by the Secretary, or 75 percent of the appraised value of the project. NAHB believes it would be worthwhile to discuss this provision more fully with industry members.

NAHB does have concerns with two provisions of H.R. 5039 and offers the following comments:

Maximum Rents. The bill requires that the maximum monthly rent charged to any eligible household may not exceed 30 percent of the adjusted income of the eligible household. NAHB believes that rents must cover operating expenses, debt service and contributions to a reserve to ensure that future maintenance and capital needs are covered. In addition, setting rents at a percentage of each individual household's income would

make it impossible to underwrite the financing of the property. Every single unit would have a different rent which would be unrelated to unit size. Artificially capping rents at a level too low to provide for the operation of the property will defeat the purposes of the revitalization and preservation program and put the property into financial jeopardy.

In addition, it is essential that the standards governing rent increases are realistic and do not result in downward adjustments to the rents. Current RD practice is to tie rent adjustments to operating costs. HUD uses an operating cost adjustment factor (OCAF), which also ties rent adjustments to changes in operating costs. NAHB supports these methodologies to determine rent adjustments.

NAHB supports public policy that does not allow households to pay more than 30 percent of their adjusted income for rent. Rental assistance should be available to provide the subsidy needed to cover the difference between the rent and 30 percent of adjusted household income. Without the commitment to provide rental assistance, the revitalization and preservation program will not be successful.

Sale Restrictions. H.R. 5039 requires, upon notice to the Secretary that an owner intends to prepay, that the owner cannot sell the property for 75 days except to a purchaser who agrees to buy the property at market rate and continue the low-income affordability restriction for 20 years. The owner is not prohibited from soliciting or receiving any offers of sale or purchase during this time. The bill directs the Secretary to establish and maintain a database of potential buyers who will maintain the low-income housing affordability requirements.

NAHB does not support a 75-day period during which an owner may only sell the property to a purchaser who agrees to maintain the low-income affordability use for 20 years. There are no such restrictions on HUD-assisted properties that are prepaying loans or opting out of Section 8 contracts, and there was no such statutory requirement for pre-1989 loans. The seller of the property should be able to move forward without delay once the decision to prepay has been made. NAHB supports the establishment and maintenance of a database of purchasers who may wish to buy Section 515 properties, which certainly would be useful to sellers who would like immediate access to potential buyers. However, the seller should be able to exercise his/her rights to prepay without delays.

NAHB appreciates the opportunity to provide this statement to members of the Subcommittee. H.R. 5039 will allow the Section 515 portfolio to remain the most important affordable rental housing resource to rural households. NAHB looks forward to working with members of Congress, RD and our housing industry colleagues to strengthen this important legislation and work towards enactment of H.R. 5039.



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500 New Jersey Avenue, N.W.  
Washington, DC 20001-2024  
202.383.1194 Fax 202.383.7584  
www.realtors.org/government/affairs

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President

Dale A. Sinton  
EVP/CEO

GOVERNMENT AFFAIRS  
Jerry Giovaniello, Senior Vice President  
Walter J. Witke, Jr., Vice President

April 24, 2006

Subcommittee on Housing and Community Opportunity  
Committee on Financial Services  
U.S. House of Representatives  
Washington, DC 20515

Dear Representative:

On behalf of the 1.3 million members of the National Association of REALTORS® (NAR), we would like to thank Congressman Geoff Davis (R-KY) for introducing H.R. 5039, the "Saving American's Rural Housing Act of 2006" and commend the subcommittee for holding a hearing on this measure. NAR looks forward to working with the subcommittee in the hopes that this legislation continues to progress through the legislative process.

H.R. 5039 seeks to encourage the retention of Section 515 housing properties for long-term use and the repair and preservation of these properties through financial incentives. NAR believes every resource should be made available to keep, maintain, and expand affordable housing in rural communities.

Additionally, H.R. 5039 would preserve the availability of affordable rural housing by providing a mechanism for owners of multifamily rural housing projects with loans under Section 515 to enter into loan restructuring agreements to provide capital for revitalization activities. Furthermore, H.R. 5039 would enable rents to remain affordable in revitalized properties as well as protect tenants who live in properties where the loan is prepaid.

The National Association of REALTORS® supports the goals of H.R. 5039 and believes it is a reasonable approach towards revitalizing rural housing programs in the United States. Affordable housing needs to be readily available in Rural America, and NAR stands committed to this goal and ready to help.

Sincerely,

Thomas M. Stevens, CRB, CRS, GRI  
2006 President, National Association of REALTORS®

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