NASLEF

The National Association of State and Local Equity Funds

Statement of Bernard Deasy, President

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Appearing on Behalf of the

National Association of State and Local Equity Funds

Community Reinvestment Act and the Low Income Housing Credit Program

Joint Public Hearings on the

Community Reinvestment Act Regulations

Los Angeles, California

August 17, 2010

Hello. My name is Bernard Deasy and I am appearing here today on behalf of the National Association of State and Local Equity Funds (NASLEF).

I am President of Merritt Community Capital Corporation, a nonprofit organization located in Oakland, California. We raise equity capital for investment in affordable rental housing developments in California using the Low-Income Housing Tax Credit ("LIHTC") program.

I am also a Member of the Board of Directors of the National Association of State and Local Equity Funds ("NASLEF"), a trade association representing similar and largely nonprofit housing syndicators across the country. We have 16 members in NASLEF who fund affordable housing development in 36 states. Since the inception of the LIHTC program, our members have raised over $7 billion of equity capital to develop more than 100,000 rental homes for lower-income families.

Our member organizations raise equity capital ("capital") from institutions for investment in affordable housing properties that utilize the LIHTC. Typically, we have raised this capital in pools where the monies of multiple investors are combined in a fund partnership which then invests in a number of property partnerships.

A considerable portion of the capital we raise is from banks that are incentivized to invest in this housing for two basic reasons: they earn a competitive rate of return and they receive credit under the investment test of the Community Reinvestment Act ("CRA").

I am here today to discuss our recommendations for enhancing the rules which implement the CRA. I want to state at the outset that CRA is absolutely essential for the continued operation of the LIHTC program and is an effective and critically important inducement for bank investment.

Our issue is not with the effectiveness of CRA as a catalyst for investment, but rather, the distortions that CRA creates as to the geographic location of such investment. We believe that CRA has the unintended consequence of steering bank investment in LIHTC properties away from rural areas and smaller metropolitan markets -- and toward the largest metropolitan areas.

The LIHTC has for many years been the nation's primary means of supporting the development of new and rehabilitated affordable rental housing. Until the financial crisis, the LIHTC program, which was originally created in 1986, supported the development of approximately 120,000 to 150,000 rental units annually. It has been widely acclaimed as the most successful housing production program in our nation's history.

However, since the beginning of the financial crisis in 2008, the program has had difficulty raising capital and producing affordable housing. This is not at all related to the performance of the investment which remains outstanding. Across the nation, LIHTC properties have low vacancy rates and virtually no foreclosure activity. Rather, the problem has been: 1) the two largest sources of equity investment, Fannie Mae and Freddie Mac, ceased investing in the LIHTC program because they cannot use the tax benefits, and 2) the capacity of CRA-motivated banks to invest has been significantly reduced because losses in that sector have reduced their capacity to utilize LIHTCs.

In spite of some temporary changes in the program instituted by Congress, production has declined as capital has become more difficult, and thus more expensive to raise.

This difficulty in raising capital has intensified the geographic biases in CRA which distort the placement of capital by banks in the LIHTC program. Those inequities have favored affordable housing development in larger banking centers as compared to other areas of the nation. This has been a particular concern to several NASLEF members who frequently expend resources in rural areas and smaller markets across the country where it has become considerably more difficult to raise investment capital for the LIHTC program.

As a result, we have seen the LIHTC program – which has historically operated in a national market with fairly consistent characteristics across different states – become a two-tiered program, healthy in those markets where CRA incentives have directed investment capital, and less healthy in other markets not favored by CRA motivated investors.

This has caused equity pricing – which is the price paid for each dollar of LIHTCs – to vary widely between different areas of the country. Before the financial crisis, tax credit pricing was fairly consistently in the 85 cent - 95 cent range with variations largely due to the characteristics of the development. Today, credit pricing in many areas where NASLEF members invest is in the 68 - 72 cent range per credit dollar, while in the 50 or so CRA intensive markets prices are materially higher. The price variation is due to supply - demand factors – in lager MSAs where the supply of investment capital is greatest, so is the price of LIHTCs. This means that CRA is making it relatively more difficult and less efficient to utilize the LIHTC in most non urban areas of the country. Consequently, we strongly believe that the CRA program should be more geographically neutral.

The characteristics of the CRA rules which give rise to this situation are not new - they are just newly revealed. The emergence of the distortion in part can be traced to the demise of Fannie Mae and Freddie Mac as major investors in the Housing Credit program. For many years the two GSEs accounted for approximately 40 percent of the investment capital in the LIHTC program. Banks, in an effort to satisfy the CRA, accounted for perhaps another 40 to 50 percent of the investment capital.

When LIHTC syndicators, such as Merritt Capital, raise their pools of capital, the portion supplied by non – CRA driven investors traditionally does not have to be specifically allocated. This, in turn, provides more flexibility when allocating a bank's investment to properties located within specific assessment areas. Following the departure of the GSEs, these same investment funds, due to a higher concentration of bank investors, became more sensitive to investing in CRA qualifying assessment areas. As a result, we have found it more difficult to fund property developments throughout the states we operate in, specifically in localities not within the priority assessment areas of our bank investors.

While the "Interagency Questions and Answers Regarding Community Reinvestment" do make accommodation for community development qualified investments that benefit a regional area that includes an institution's assessment areas, our experience has been that in most areas of the country this is not an effective means of facilitating investment outside bank assessment areas.

The answer to question §__12(h)--7 provides that "as long as an institution has adequately addressed the community development needs of its assessment area(s), it will receive ***consideration*** for community development activities that benefit geographic areas or individuals located somewhere within the broader statewide or regional area that includes the institution's assessment area(s), even if those activities do not benefit its assessment area(s)."

We endorse the objective of this language but believe the challenge resides with its implementation. Based on our diverse experience in different areas of the country, bank examiners are not consistent in their interpretation of this language. In some areas it has a practical effect and banking institutions are willing to make investments in a LIHTC fund that includes properties in areas of the state or region beyond the institution's assessment areas. In most cases, however, that has not been the case and as a result, banks are reluctant to make investments outside their assessment areas.

We see at least three problems with this: 1) the language is not being interpreted uniformly between bank regulatory agencies and even within a single agency in different regions, 2) the extent of the discount that an examiner will impose on investments that benefit an area larger than the assessment area is not known so banks cannot rely on receiving credit, and 3) the provision is applied prospectively if a bank is judged to be "adequate" in its assessment area in the future, rather than having been determined to be "adequate" in the past.

We recommend modifying the language to provide that an institution ***that has been determined*** on its last exam to have adequately addressed the community development needs of its assessment area(s) will receive ***full*** credit for community development activities that benefit geographic areas located somewhere within the broader statewide or regional area that includes the institution's assessment area(s), even if those activities do not benefit its assessment area(s).

All NASLEF members believe it would be preferable to limit this concept to investment in areas outside the assessment area but within the same state. Similarly, there are NASLEF members who are also comfortable applying this more broadly to investments in areas within the same region, as provided in the current Qs and As.

Alternatively, this proposal could be structured more narrowly to apply only to LIHTC investments rather than to all community development activities that benefit a broader geographical area. We believe this more limited approach for LIHTC investments would be consistent with the purpose of CRA which is to ensure that banks serve lower-income, traditionally under-served populations within the areas in which they do business.

Congress created the LIHTC program with a similar motivation to help support the development of affordable housing for lower-income populations. Indeed the LIHTC program -- which serves households with incomes at or under 60 percent of area median income -- arguably targets a population whose incomes are considerably lower than the typical population served by a bank pursuant to its CRA lending, investing and servicing requirements.

I would like to thank the bank regulatory agencies for your efforts in reviewing the Community Reinvestment Act to make sure that it fully fulfills its purpose. This is a valuable exercise that has the potential to improve the lives of millions of Americans and we look forward to continuing to work with you on this project.