NATIONAL ASSOCIATION OF HOME BUILDERS

Testimony Of

James R. Rayburn

First Vice President of the

National Association of Home Builders

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On

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Introduction

Thank you Mr. Chairman for the opportunity to testify before the Subcommittee on Housing and Community Opportunity on housing in rural America. I am Bobby Rayburn, a home builder and developer from Jackson, Mississippi. My company, Rayburn Associates, has constructed more than 3,000 single family and multifamily homes. Providing affordable homeownership and rental housing opportunities in rural America is, and has been, a major focus of my 30 years in home building. I also serve as the 2003 First Vice President of the 211,000-member National Association of Home Builders (NAHB), which I am representing today. NAHB represents more than 800 state and local home builder associations across the country, and NAHB members will build approximately 80 percent of the nearly 1.7 million new housing units that are projected for construction in 2003.

NAHB and its 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, the existing rental stock is aging and in need of renovation, and access to competitively priced credit for potential home buyers remains a problem in many rural areas.

Nearly all federal efforts to address rural housing needs are currently undertaken through the Rural Housing Service (RHS) of the U.S. Department of Agriculture (USDA). Appropriations for these programs have declined dramatically and current funding levels are inadequate across the board. In addition, a number of RHS programs are in need of major reforms, particularly the multifamily management activities, and its portfolio of properties has deteriorated to an alarming degree.

Remedies are urgently needed. While there are many possible approaches to meeting the need for the production of new units and preservation of the existing stock, there are two common elements that are crucial to success – more resources must be committed and a range of interests beyond the Department of Agriculture must join in the effort.

The Role of USDA Rural Development Programs in Rural Housing

RHS serves a unique role by providing loans and loan guarantees in areas of the nation that, in many cases, are not well served by conventional lenders. Some of the programs offered by RHS, such as the Section 502 direct loan program, provide below-market rate loans to families who would otherwise not be able to achieve homeownership. The delivery mechanism for this program is also unique because these loans are arranged though local Rural Development staff. The Section 502 Guaranteed Rural Housing program provides guarantees for loans originated by private sector lenders and serves moderate-income rural Americans.

Similarly, the Section 515 and 538 multifamily loan programs provide direct loans and loan guarantees, respectively, which have been critical in providing affordable rental housing in rural communities where such housing otherwise would not exist.

A group of NAHB members recently met with the Under Secretary for USDA Rural Development, and the RHS Administrator. NAHB believes RHS is attempting to fix the problems that exist, particularly with regard to the multifamily area, and, if sufficient funding can be found, these programs will be better equipped to meet future needs.

NAHB also firmly believes that support for RHS programs should be elevated to a higher priority within the Department of Agriculture. Emphasis needs to be placed on encouraging new construction of multifamily housing and the preservation of the existing affordable rental stock. Funding levels to support both single family and multifamily programs should be adequate to meet the housing needs of rural Americans. In addition, partnerships between private, for-profit entities, state and local governments and non-profit groups should continue to be encouraged and supported at the highest levels within the Department.

Funding for Rural Housing Service Programs

NAHB believes that there continues to be a critical need for the production and preservation of affordable rental housing in rural areas as well as programs that make homeownership possible for deserving families. As such, NAHB strongly believes that support for the Rural Housing Service programs within the USDA, from Congress, and by many rural stakeholder organizations is essential to ensuring that affordable housing opportunities are available to low- and moderate-income rural Americans.

Multifamily Rental Housing

The Section 515 direct loan program provides mortgage loans, with interest rates as low as one percent, to developers to provide affordable multifamily rental housing for very low-, low- and moderate-income families. In fact, in new Section 515 projects, 95 percent of tenants must have very-low incomes and, in addition, many of those served by the program are elderly households.

We are very disappointed to note that, again, the administration's FY 2004 budget request failed to provide any funding for Section 515 direct loans for *new* multifamily construction projects and, instead, included only $71 million, which is earmarked for repair and rehabilitation purposes. The RHS says that it must concentrate on preserving the existing portfolio and its substantial rehabilitation needs. The agency undertook an internal study of the new construction program last year, but has not taken steps to implement any changes to the program, nor has it published any of its findings. NAHB stands ready to participate in discussions that focus on improving the new construction program.

In the meantime, however, NAHB believes that a portion of monies allocated to the Section 515 program must be directed toward new construction, and we support a funding level of $300 million. We urge Congress to give significant consideration to providing the program with a level of funding that will allow for much-needed new production, as well as for rehabilitation of existing stock.

NAHB supports a funding level of $200 million for the Section 538 guaranteed loan program, for which $100 million has been proposed by the administration. This program is intended to finance the construction, acquisition or rehabilitation of rural multifamily housing for lower-income residents. The residents of these rental housing units must be very low- to moderate-income households with incomes that do not exceed 115 percent of the median income of the surrounding area. An adequate level of funding would enable the RHS to have a broad range of tools by which to meet the affordable housing needs of these rural residents. While the Section 538 program got off to a slow start, the RHS has made extensive efforts to address issues raised by lenders and the secondary market that prevented the program from being attractive. RHS currently has a proposed rule for the Section 538 program out for comment that would make several more important regulatory changes, which NAHB supports.

With regard to the Section 521 Rental Assistance Program, NAHB is pleased that the president's budget provides $740 million, an increase of $28 million over last year's funding level. Rent subsidies under this program help to ensure that the low-income residents of multifamily housing units financed by the RHS are able to afford rent payments. However, we remain very concerned that without a larger funding increase for this program, the proposed level would only support existing programs, without providing an opportunity to fund new rental contracts. Therefore, we encourage a funding level of $850 million for this account.

Multifamily Management

Key to the success of preserving the existing RHS multifamily portfolio and providing much-needed new affordable rental housing is the ability of the agency to address management issues. Inconsistencies in how the projects are monitored occur from state to state, management fees have wide variations, and it seems to be difficult to remove bad property managers or owners. In addition, RHS staff can present roadblocks to potential purchasers of existing properties who plan to improve the properties. In one instance, a potential purchaser who had financing in hand to solve a significant health and safety problem at a property was told by RHS staff that additional physical improvements to the property, not related to health and safety, had to be made before a sale would be approved. The cost of such improvements surpassed the amount of financing available, and the potential purchaser abandoned the deal. The RHS needs a viable management and preservation strategy, which must include the ability to respond more effectively to such situations.

NAHB understands that some of these types of issues will be addressed in RHS' recently issued proposed regulatory changes to its multifamily programs (Sections 514, 515, 516 and 521). These changes are intended to streamline and consolidate 13 regulations into one, as well as address concerns raised by the Office of the Inspector General. NAHB supports such efforts and encourages RHS to move towards simplifying its regulations as much as possible, as well as strengthening its ability to address its portfolio responsibilities. NAHB is reviewing the proposed rule and will submit comments to the agency.

Single Family Housing

With Section 502 housing loan guarantees, low- and moderate-income individuals and families can purchase homes without making a downpayment because they may borrow up to 100 percent of the appraised value of the home. Since a common barrier to owning a home for many is the lack of funds to make a downpayment, this program makes the possibility of owning a home a reality for many Americans in rural communities. NAHB continues to support full funding for this program, which will support approximately $2.7 billion in loan production.

In addition, NAHB continues to support increased funding for the Section 502 direct loan program. Under this program, individuals and families are able to receive a home loan directly from the RHS at an affordable interest rate. Most of these loans are made to families with incomes below 80 percent of the median income level in the communities where they live. Because the RHS provides loans to those who will not qualify for a conventional loan, the program creates homeownership opportunities for many more Americans than might otherwise be possible.

Without adequate funding levels, the Section 502 direct loan program will not be able to meet the needs of very low- and low-income rural residents because the need for Section 502 loans consistently exceeds budgeted levels. As it is, only one out of every four applicants receives a direct loan from RHS under this program. The FY 2004 budget request includes $168 million in funding to support $1.37 billion in Section 502 direct loans. NAHB recommends that, at a minimum, a program level of $1.5 billion be approved for this program. To meet current needs, however, it would take three times this level.

HUD Funding

NAHB is also disappointed that the administration is proposing, for the third year in a row, to eliminate the Rural Housing and Economic Development program in the budget of the U.S. Department of Housing & Urban Development (HUD). This program provides funding to nonprofits and other community groups in rural areas for capacity building at the state and local level for rural housing and economic development and to support innovative housing and economic development activities in rural areas. In the past, Congress has not supported the elimination of this program, and NAHB urges that you continue to provide $25 million in funding for the program in FY 2004.

Partnerships to Address Rural Housing Needs

Even with more funding, RHS cannot do the job alone. NAHB is pleased that the RHS is undertaking partnerships with HUD, the Federal Deposit Insurance Corporation (FDIC), the Federal Home Loan Bank System, the Federal Reserve, Fannie Mae, Freddie Mac, Rural Local Initiatives Support Corporation (LISC), the Neighborhood Reinvestment Corporation, state housing finance agencies, rural employers and other organizations to promote rural homeownership initiatives and to find ways to leverage RHS' assets. These types of partnerships are essential given RHS' limited resources and the large and often remote geographical areas that must be covered. More extensive efforts in this direction are requisite to adequately addressing rural housing needs.

Most of the partnership efforts outlined above are aimed at addressing homeownership needs. NAHB believes that partnerships also are needed to address the affordable rental housing needs of rural residents. Because affordable rental properties in rural areas tend to be small when compared to typical urban projects, many larger lenders will not make such loans. The RHS has made some progress working with the secondary market to make its multifamily loans acceptable for their portfolios. Freddie Mac has purchased a few Section 538 loans, and Fannie Mae is interested in a preservation strategy that pools Section 515 loans. But neither of these efforts to date has resulted in a significant number of successful deals. We were pleased to learn recently that Ginnie Mae will be seeking legislation from Congress that would permit it to guarantee securities that are backed by the RHS, which would help expand the secondary market for Section 538 loans. NAHB strongly supports this initiative.

The RHS alone does not have the capacity or funding to provide the level of loans needed. Local lenders, state housing finance agencies (HFAs) and other financial entities also need to participate. HFAs have great potential for rural lending and, in fact, many Section 515 projects now include Low Income Housing Tax Credits or tax-exempt bonds issued by the HFAs. Some HFAs are trying to pool small loans that can be included in one bond issue, which greatly reduces the transactions costs for small loans. More programs of this type should be developed. In addition, HUD should overhaul its small projects product, which currently is too cumbersome to be an effective financing tool.

Financial Literacy for Rural Families

One of the most significant barriers to homeownership in rural areas is the lack of financial literacy by potential home buyers. NAHB was pleased that USDA and the FDIC recently signed a memorandum of understanding to promote broad use of the FDIC's "Money Smart" program. When coupled with home buyer education programs, which are funded by HUD and delivered by HUD-approved education providers, Money Smart will help to make rural families more knowledgeable, more creditworthy, and less likely to fall prey to unscrupulous lending practices. In the past, RHS had a modest budget of $1 million to fund home buyer education. In the administration's FY 2004 budget, this line item has been dropped, with the explicit intention that funding for rural home buyer education would be drawn from HUD's budget. Steps must be taken to ensure that sufficient educational resources are directed to rural areas.

Housing Goals for Fannie Mae and Freddie Mac

Fannie Mae and Freddie Mac, which are government-sponsored enterprises (GSEs), are required by law to meet annual housing goals established by HUD. Under the housing goals, the GSEs must meet annual percent of business goals for three categories: low- and moderate-income, underserved areas, and special affordable. The first set of goals were established by regulation in 1995, and were updated in 2000 to cover the years 2001 – 2003. Current goals levels, as a percent of annual purchases, are: 50% for low-moderate; 31% for underserved areas; and, 20% for special affordable goal. Revisions to the goals for 2004 and beyond are currently under review by HUD.

To this point the GSE housing goals have had little, if any, impact in improving the availability of housing credit in rural areas. In the 2000 revision of the goals, the underserved areas goal was increased from 24 to 31 percent, but there has been only a limited increase in the role of Fannie Mae and Freddie Mac in rural housing finance. During development of the 2000 rule, NAHB commented that HUD should encourage increased participation in rural areas by Fannie Mae and Freddie Mac through the use of bonus points or double credit for purchases of loans in rural areas. HUD did not include this recommendation in the final rule, but we plan to revisit this issue during the revision to the goals for 2004.

According to the latest regulatory agenda, HUD intends to propose new housing goals in August. HUD has not released any information about possible changes in the goals. However, the administration's 2004 budget analysis suggests that HUD may incorporate new factors into the goals for 2004 and beyond to encourage improved performance from the GSEs in serving low- and moderate-income and minority families. NAHB urges HUD to include improved rural housing credit in that policy agenda.

NAHB supported HUD's increase in the goals for the 2001 – 2003 period. NAHB feels that more needs to be done to encourage the GSEs to further increase their rural activities and we look forward to working with HUD in an effort to address rural housing needs during the current goals review.

Rural Housing and the Community Reinvestment Act

NAHB strongly supports the goal of the Community Reinvestment Act (CRA), which is to encourage federally insured financial institutions to help meet the credit needs of their entire communities. Again, however, the CRA process has brought little or no benefit to borrowers in rural areas. NAHB believes the needs of rural and other underserved areas could be more sufficiently addressed if the CRA were modified to encourage financial institutions to serve those areas.

The CRA has been in existence for 25 years, and yet, there are still many geographic areas, particularly rural communities, that are not receiving adequate levels of financial services or that are being neglected altogether. For example, our members report instances where several banks in proximity to an underserved community declined to finance proposed housing projects because that community was not considered to be in their assessment areas. The financial institutions apparently felt no incentive to lend in communities considered outside of their assessment areas since they probably would not receive CRA credit for such lending. As a result, many communities and their residents are falling through the cracks.

NAHB believes that Congress should consider encouraging efforts to provide financial services in geographic areas that an institution can be reasonably expected to serve. Currently there is no incentive for financial institutions to lend, invest or provide financial services in rural areas. We understand that many projects intended to revitalize or stabilize rural communities do not qualify under the current regulatory definition of community development because those activities are not located in low- or moderate-income geographies, as defined in the regulations.

We also believe that it is important to provide greater CRA credit for initiatives that serve areas that previously did not have adequate access to credit. NAHB believes such a revision would provide incentives for institutions to establish branches and lending relationships in more difficult to serve areas.

The federal banking regulators currently are reviewing the CRA regulations. NAHB is participating in that process, and we hope the Congress will join us in urging reform to improve rural credit availability.

Conclusion

In conclusion, Mr. Chairman, NAHB thanks you for bringing attention to and supporting the cause of rural housing during Homeownership Month. As you know, the problems of housing rural Americans extend to both affordable homeownership and rental opportunities.

NAHB believes that, under the leadership of Under Secretary Thomas Dorr and RHS Administrator Arthur Garcia, Rural Development is attempting to address its severe problems and is doing a better job of promoting the use of partnerships among a broad base of housing stakeholders. However, much more work remains to be done, and the federal government must commit more resources to the task. Meeting the housing needs in rural areas requires not only that housing be elevated as a priority within the Department of Agriculture, but that a broad range of other entities, including HUD and the GSEs, become committed participants and partners in the effort.

NAHB stands ready to work with RHS, HUD, the GSEs and all other supporters of rural housing to improve the programs and to develop creative solutions to maximize the use of scarce resources in addressing these critical needs.