

**FEDERAL HOUSING FINANCE BOARD****12 CFR Part 951**

[No. 2005–23]

RIN 3069–AB26

**Affordable Housing Program Amendments****AGENCY:** Federal Housing Finance Board.**ACTION:** Proposed rule.

**SUMMARY:** The Federal Housing Finance Board (Finance Board) is proposing to amend its Affordable Housing Program regulation to remove prescriptive requirements, clarify certain operational requirements, remove certain authorities, and otherwise streamline and reorganize the regulation.

**DATES:** The Finance Board will accept written comments on the proposed rule that are received on or before April 27, 2006.

**ADDRESSES:** Submit comments by any of the following methods:

E-mail: [comments@fhfb.gov](mailto:comments@fhfb.gov).

Fax: 202–408–2580.

Mail/Hand Delivery: Federal Housing Finance Board, 1625 Eye Street, NW., Washington, DC 20006, ATTENTION: Public Comments.

Federal eRulemaking Portal: <http://www.regulations.gov>. Follow the instructions for submitting comments. If you submit your comments to the Federal eRulemaking Portal, please also send it by e-mail to the Finance Board at [comments@fhfb.gov](mailto:comments@fhfb.gov) to ensure timely receipt by the agency.

Include the following information in the subject line of your submission: Federal Housing Finance Board. Proposed Rule: Affordable Housing Program Amendments. RIN Number 3069–AB26. Docket Number 2005–23.

We will post all public comments we receive on this rule without change, including any personal information you provide, such as your name and address, on the Finance Board Web site at [http://www.fhfb.gov/pressroom/pressroom\\_regs.htm](http://www.fhfb.gov/pressroom/pressroom_regs.htm).

**FOR FURTHER INFORMATION CONTACT:**

Charles E. McLean, Associate Director, Office of Supervision, by electronic mail at [mcleanc@fhfb.gov](mailto:mcleanc@fhfb.gov) or by telephone at 202–408–2537; Sylvia C. Martinez, Senior Advisor, Office of Supervision, by electronic mail at [martinezs@fhfb.gov](mailto:martinezs@fhfb.gov) or by telephone at 202–408–2825; or Sharon B. Like, Senior Attorney, Office of General Counsel, by electronic mail at [likes@fhfb.gov](mailto:likes@fhfb.gov) or by telephone at 202–408–2930. You can send regular mail to the Federal Housing Finance Board,

1625 Eye Street, NW., Washington, DC 20006.

**SUPPLEMENTARY INFORMATION:****I. Background**

Section 10(j)(1) of the Federal Home Loan Bank Act (Bank Act) requires each Federal Home Loan Bank (Bank) to establish an affordable housing program (AHP), the purpose of which is to enable Bank members to provide subsidized financing for long-term, low- and moderate-income, owner-occupied and affordable rental housing. See 12 U.S.C. 1430(j)(1). The AHP has played an important role in allowing the Banks to support their members' efforts to meet the housing needs of their communities. Although the AHP is a shallow subsidy program, its strength lies in its capacity to leverage additional public and private resources for housing. Since the inception of the program in 1990, the Banks have awarded more than \$2 billion in AHP subsidies to assist nearly 437,000 housing units. Seventy percent of the units receiving AHP subsidies were for very low-income households. AHP subsidies have proven to be useful in financing projects that present underwriting challenges, such as projects for the homeless and special needs populations, which may include persons with disabilities and the elderly. The AHP also has been used effectively with Low-Income Housing Tax Credits (LIHTC or tax credits) by filling financing gaps, thereby enabling a larger percentage of very low-income households to be served.

The AHP also serves as an important resource for low- or moderate-income homeowners and first-time homebuyers. From 1990 through 2004, the program has assisted in the financing of 102,810 owner-occupied units under the Banks' competitive application programs, and 47,813 units under their homeownership set-aside programs. Some of the units address specific housing needs, such as expanding homeownership opportunities for underserved households.

The Finance Board has promulgated regulations implementing these provisions of the Bank Act, which are codified at 12 CFR part 951. These regulations generally have reflected a prescriptive approach, which was appropriate for rules implementing a newly created program. As the program has matured, however, the Finance Board has revised the AHP regulations a number of times, in part to provide greater responsibility to the Banks in managing the program and in part to implement improvements based on lessons learned in overseeing the operation of the program. The Finance

Board believes, based in part on its review of the AHP on a Bank System level conducted in 2003–2005, *Report of the Horizontal Review of the Affordable Housing Programs of the Federal Home Loan Banks* (March 15, 2005) (Horizontal Review), that there are a number of areas in which the regulation can be further revised to enhance the success of the program.<sup>1</sup>

In proposing these amendments, the Finance Board intends to address seven principal factors. First, additional definitions would be incorporated into the regulation at § 951.1. These definitions would serve to establish the precise use of key terms that are included in the regulation. Second, the proposal would reorganize the regulatory text so that operational provisions relating to the competitive application program and the homeownership set-aside program, respectively, would be fully contained within separate sections of the regulation. Proposed § 951.5 would address the competitive application program, while § 951.6 would address the homeownership set-aside program. The proposed reorganization is intended to make it easier for program sponsors and other interested parties to understand the operation of the competitive application and homeownership set-aside programs. Third, the use of AHP subsidy by loan pools and revolving loan funds would be permitted under the competitive application program, at the discretion of the particular Bank. This proposed change is intended to expand the range of eligible means of supporting affordable housing through the program. Fourth, restrictions on the use of AHP funds by projects located outside a Bank's district and scoring preferences for in-district projects, which the current regulation permits at the Bank's discretion, would no longer be permissible. This proposed change is in response to the expansion of interstate banking among Bank member institutions, which has resulted in many members serving markets outside a Bank's district boundaries. Fifth, provisions in the current regulation that allow a Bank to accelerate AHP contributions from the following year into the current year would be deleted. The Banks have not often used this authority, and it also may present some operational difficulties. Sixth, provisions in the regulation that would increase annually the maximum allowable dollar amount of a Bank's

<sup>1</sup> The Horizontal Review is available on the Housing Programs page of the Finance Board's Web site: <http://www.fhfb.gov/Default.aspx?Page=47>.

allocation to its homeownership set-aside program and maximum allowable dollar acceleration amount under a Bank's competitive application program, based on the annual inflation rate, would be deleted. This change would address the potential for inflation to increase the allocation of AHP contributions to the homeownership set-aside program relative to the competitive application program. Finally, prescriptive monitoring requirements in the current regulation, which detail specific monitoring and control processes with which a Bank must comply, would be replaced by standards based on required outcomes rather than prescribed control processes. The Finance Board invites comments on all aspects of the proposed rule.

## II. Analysis of the Proposed Rule

### A. Definitions: Proposed § 951.1

The proposed rule would revise certain of the existing AHP definitions and would define a number of other terms that are used throughout the regulation. See 12 CFR 951.1. Proposed new definitions are discussed in the context of specific regulatory requirements. The more substantive changes are described below.

*Affordable.* The existing definition would be revised by adding a reference, consistent with the AHP statutory term, to "rent charged to a household," which would be defined to mean the rent that is actually paid by the household occupying the unit. See 12 U.S.C. 1430(j)(13)(D). The existing regulatory language may not be clear on this point and could be read to mean the amount of rent charged by the owner for the unit, which would be greater than the rent actually paid by the occupants if the occupants receive financial assistance for rent payments from other sources.

The proposed rule also would add a new paragraph (2), which would address units that are subsidized with low-income housing assistance under the Department of Housing and Urban Development (HUD) Section 8 program. See 42 U.S.C. 1437f. This provision is intended to clarify that rents charged to a household under a Section 8 agreement will be deemed to be "affordable" for AHP purposes, even if the rent increases after initial occupancy, if the rent met the AHP definition of "affordable" upon initial household occupancy and thereafter has continued to comply with the Section 8 agreement for that household. This provision would be applicable for purposes of the annual adjustment of targeting commitments after initial

occupancy under proposed § 951.7(a)(3) (which is re-designated from current §§ 951.10(d) and 951.11(b)).

*AHP project.* The proposed rule would add a new definition, which would apply to both owner-occupied and rental projects that have been awarded or have received AHP subsidy through the competitive application program. This is intended to codify existing practice and clarify that the term "project" does not apply to direct subsidies, *i.e.*, grants, to households made pursuant to the homeownership set-aside program. The term would apply to both single-family and multifamily projects. The proposed rule also would make conforming changes to the definitions of "owner-occupied project" and "rental project."

*Low- or moderate-income household and very low-income household.* The existing regulation defines "low- or moderate-income household" to mean a household that has an income of 80 percent or less of the median income for the area, with the income limit adjusted for family (*i.e.*, household) size, in a Bank's discretion, in accordance with the methodology of the applicable median income standard. The proposed rule would amend the household-size adjustment provisions in paragraph (3) of the existing definition of "low- or moderate-income household" and (and similarly for the definition of "very low-income household") by changing the household-size adjustment from an optional to a mandatory requirement, provided that if the source for the area median income data has no methodology to adjust the household income limit for household size, the Bank is not required to make such an adjustment. This change would bring the AHP into conformance with other federal programs that adjust for household size.

As further discussed below, the proposed rule would relocate certain provisions of the existing definitions relating to when a household's income must be determined, to proposed §§ 951.5(c)(1) and 951.6(c)(2)(i) for the competitive application program and the homeownership set-aside program, respectively.

*Median income for the area.* The existing definition lists a number of median income standards that a Bank may adopt for purposes of determining household income eligibility. The regulation also provides that a Bank may request Finance Board approval of a median income for any definable geographic area, as published by a federal, state, or local government entity for purposes of that entity's housing programs. The proposed rule would

remove the language "for purposes of that entity's housing programs." This would enable the Finance Board to approve, upon a Bank's request, median income standards from sources, such as the Census Bureau, that publish median income data but do not have their own housing programs.

*Owner-occupied project and rental project.* The proposed rule would amend the existing definitions by clarifying that they apply only to the competitive application program and by deleting language requiring the project to involve "the purchase, construction, or rehabilitation" of owner-occupied housing or rental housing, respectively. That requirement would be relocated to the provisions addressing the eligibility requirements for the use of AHP subsidy, at proposed § 951.5(c)(1)(i) and (ii). The proposed rule also would add manufactured housing to the types of owner-occupied housing and emergency shelters and single-room occupancy (SRO) housing as types of rental housing, which are explicitly referenced in the rule.

*Retention period.* The proposed rule would amend the existing definition to clarify that, in the case of rehabilitated units that currently are occupied by the owner and do not involve a closing, the retention period would commence on the date of completion of the rehabilitation.

*Sponsor.* The proposed rule would amend the existing definition by authorizing a Bank to define certain terms in its AHP Implementation Plan and by adding 2 entities to the definition. The terms "ownership interest" and "integrally involved" are key terms in the existing definition of "sponsor." The proposed rule would retain those terms but would require each Bank to define what they mean in its AHP Implementation Plan. Under the existing definition, a Bank must consider a "sponsor" to include any entity that has an ownership interest in a rental project, regardless of how small or temporary such ownership interest is. Requiring a Bank to define "ownership interest" in its AHP Implementation Plan would allow it to address concerns that some rental projects may manipulate ownership interests in order to receive points as not-for-profit sponsors under the competitive application program's scoring system. The proposed rule also would expand the definition to include revolving loan funds or entities that establish loan pools. Those terms would be used for purposes of implementing proposed amendments to the competitive application program rules, which would

deal with revolving loan funds and loan pools, respectively.

*Subsidy.* The proposed rule would revise the existing definition, principally by deleting the provisions that specify the dates as of which the amount of the subsidy is to be determined. The substance of those provisions would be incorporated into the section that sets forth the eligibility requirements relating to the competitive application program, at proposed § 951.5(c)(12). The proposed rule also would remove the term “homeownership set-aside funds” from the definition of “subsidy” because they are direct subsidies, which are included within the definition of “subsidy.”

*B. Required Annual AHP Contributions; Allocation of Contributions: Proposed § 951.2*

*Annual AHP contributions: Proposed § 951.2(a).* Under the Bank Act, each Bank annually must contribute to its AHP an amount equal to the greater of 10 percent of the Bank’s previous year’s net income or such prorated amount as is required to assure that the aggregate contribution of the 12 Banks is no less than \$100 million. 12 U.S.C. 1430(j)(5)(C). In recent years, the Banks have not used the pro rata allocation method because the annual contributions based on the 10 percent of income formula have exceeded \$100 million. Nonetheless, proposed § 951.2(a)(2) would revise the existing provisions to clarify that if the pro rata formula were to be used in any future year, the required annual contribution for any Bank could not exceed its net earnings for the previous year. This is primarily intended as a safety and soundness measure to avoid the possibility that a Bank might otherwise be required to contribute an amount in excess of its income, thereby reducing its regulatory capital.

*Net earnings of a Bank.* Proposed § 951.1 would revise the existing definition to clarify existing practice with respect to how a Bank’s earnings are determined for purposes of calculating its required AHP contribution. See 12 CFR 951.1. Pursuant to registration of its equity securities with the Securities and Exchange Commission (SEC), each Bank must present its financial statements in its SEC filings in accordance with Generally Accepted Accounting Principles in the United States (GAAP). The application of Statement of Financial Accounting Standards No. 150, *Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity* (SFAS 150), to the Banks requires them to categorize

capital stock subject to a mandatory redemption request as a liability on the statement of condition and requires that they treat the dividends on capital stock subject to a mandatory redemption request as interest expense. The Bank Act provisions related to the AHP provide that each Bank shall make an annual contribution equal to 10 percent of its net earnings for the previous year after reduction for any payment required under 12 U.S.C. 1441b (regarding the Resolution Funding Corporation) and before declaring any dividend. 12 U.S.C. 1430(j)(8). Because the Bank Act requires that the AHP contribution be calculated before the declaration of dividends, net earnings for purposes of calculating the AHP contribution should not be reduced by any dividend declaration, including those associated with mandatorily-redeemable stock, even though those dividends may be treated as interest expense in the calculation of GAAP net income.

*Allocation of contributions: Proposed § 951.2(b).* The proposed rule would relocate the allocation of contributions provisions for the competitive application program and homeownership set-aside program in existing § 951.3(a) to proposed § 951.2(b), as they relate to the requirements for AHP contributions, which are set forth in proposed § 951.2.

*Homeownership set-aside allocation: Proposed § 951.2(b)(2).* AHP subsidies are disbursed through a Bank’s competitive application program and its homeownership set-aside program. Under the existing rules, a Bank may set aside annually up to the greater of \$3 million or 25 percent of its annual required AHP contribution to provide funds to members through its homeownership set-aside programs. See 12 CFR 951.3(a)(1)(i). If member demand in a given year exceeds the AHP subsidy amount available for that year, a Bank may accelerate or “borrow” additional amounts from the following year’s AHP contribution, up to the greater of \$3 million or 25 percent of the Bank’s projected contribution for the following year, to the current year’s set-aside program.

In addition to those amounts, a Bank may set aside annually up to the greater of \$1.5 million or 10 percent of its annual required AHP contribution to fund a set-aside program to be used solely to provide financial assistance to first-time homebuyers. See 12 CFR 951.3(a)(1)(ii). If member demand for that set-aside program exceeds the amount of available AHP subsidy for a particular year, a Bank may accelerate or “borrow” additional amounts from the

following year’s AHP contribution, up to the greater of \$1.5 million or 10 percent of the Bank’s projected contribution for the following year, to the current year’s first-time homebuyer set-aside program. These maximum allowable dollar amounts are adjusted annually by the Finance Board to reflect any percentage increase in the preceding year’s Consumer Price Index (CPI). See 12 CFR 951.3(a)(1)(iii).

The proposed rule would remove the annual CPI adjustment of the caps on the dollar amounts that may be allocated to the set-aside programs, principally because it has the potential over time to increase the amounts allocated to the set-aside programs at the expense of the competitive application program. As such, the CPI adjustment could potentially affect the balance between amounts allocated to owner-occupied housing and rental housing, respectively. Similarly, because the provision allowing acceleration of the maximum allowable dollar allocation under the competitive application program into the current year from the subsequent year would be eliminated, the provision authorizing a CPI adjustment of the accelerated amount, as provided under existing § 951.3(a)(2), would be eliminated as a conforming amendment.

The Finance Board is proposing to make a number of other changes regarding the allocation of AHP funds to the homeownership set-aside programs, as noted below.

*Consolidation of separate program authorities: Proposed § 951.2(b)(2).* Proposed § 951.2(b)(2) would retain the maximum allowable aggregate allocation of AHP dollars to the homeownership set-aside programs, *i.e.*, the greater of \$4.5 million or 35 percent of a Bank’s annual required AHP contribution, but would eliminate the first-time homebuyer set-aside program authority as a separate and distinct authority. See 12 CFR 951.3(a)(1). The proposed rule would replace the separate first-time homebuyer set-aside program provision with a requirement that at least one-third of a Bank’s aggregate annual homeownership set-aside allocation be targeted for first-time homebuyers, which should be functionally equivalent to the results under the current structure. The Finance Board understands that most of the Banks currently dedicate a substantial portion of their general homeownership set-aside allocation to first-time homebuyers before setting aside funds under the separate homeownership set-aside authority that specifically targets first-time homebuyers. Therefore, the Finance

Board believes the proposed change would simplify the regulation but would not cause a substantive change in the allocation of homeownership set-aside funds to first-time homebuyers.

*Removal of acceleration authority.* The Finance Board also is proposing to remove the existing provisions that permit a Bank to accelerate or “borrow” AHP funds from the subsequent year to fund the current year’s homeownership set-aside programs. See 12 CFR 951.3(a)(1)(i) and (ii). The Banks have not often used that authority (in 2004 only two Banks did so) and it presents operational difficulties because it requires the Banks to project future earnings in order to determine how much they may accelerate into the current year, and these projections may not prove to be accurate. Deleting this provision would eliminate some unnecessary complexity to the administration and monitoring of the AHP fund as well as to a Bank’s balance sheet. For much the same reason, the Finance Board is proposing to eliminate the provision allowing acceleration of competitive application program allocations, as provided under existing § 951.3(a)(2).

#### *C. AHP Implementation Plan: Proposed § 951.3*

Proposed § 951.3(a) would reorganize and streamline requirements for a Bank’s AHP Implementation Plan to conform them to amendments that are being proposed to other parts of the AHP regulation. See 12 CFR 951.3(b). The proposed amendments to the specific program operating requirements for AHP Implementation Plans are discussed elsewhere in this preamble in the context of the particular operating requirements. The proposed rule also would add a requirement that the AHP Implementation Plan include the Banks’ retention agreement requirements.

Proposed § 951.3(c) would require a Bank to notify the Finance Board within 30 days of amending its AHP Implementation Plan and proposed § 951.3(d) would require a Bank to make the amended Plan publicly available through its Web site within 30 days after adoption of the amendments. Under the current rules, the Bank must submit all amendments to the Finance Board and must make its Plan available to members of the public upon request. See 12 CFR 951.3(b)(4)–(5). Making the AHP Implementation Plan available through the Banks’ websites is intended to provide the public with easy access to important information about the AHP as well as to promote greater transparency and accountability in the program.

#### *D. Advisory Councils: Proposed § 951.4*

The proposed rule would make a number of revisions to the provisions dealing with the Advisory Councils of the Banks, many of which are intended to clarify but not change the substance of the existing rule. See 12 CFR 951.4. The provisions that have a substantive effect are described below.

*Terms of Advisory Council members: Proposed § 951.4(b).* Section 951.4(b) of the proposed rule is intended to enhance the effectiveness of the Advisory Councils by lessening the likelihood that the terms of more than one-third of the Advisory Council members will expire in any 1 year. To that end, the proposed rule would require each Bank to adopt policies governing how it would conduct the appointment process and would require each Bank to appoint members to terms of “up to” 3 years. The intent of the latter change is to allow the Banks to appoint some individuals to terms of 1 or 2 years as a means of ensuring an appropriate balance of experience and service among members of the Council as a whole. Under the current rules, the Banks must appoint members of the Council for a 3 year term. See 12 CFR 951.4(d).

*Election of officers: Proposed § 951.4(c).* Section 951.4(c) would impose on the Advisory Council an affirmative obligation to elect certain officers, which is intended to ensure that each Advisory Council has in place a chairman and vice chairman. The current rule permits, but does not require, such officers. See 12 CFR 951.4(e).

*Duties: meetings with the Banks: Proposed § 951.4(d)(1).* Section 951.4(d)(1) of the proposed rule would revise the duties of the Advisory Council principally by adding a list of specific matters on which the Advisory Council must provide recommendations to the Bank’s board of directors. See 12 CFR 951.4(f)(1). Those matters include: the relative allocation of AHP subsidy between the competitive application and homeownership set-aside programs; eligibility criteria for each program; scoring criteria and related definitions for the competitive application program; any priority criteria for the homeownership set-aside program; and the AHP Implementation Plan.

Proposed § 951.4(d)(3) also would extend the deadline by which the Advisory Council must submit its annual analysis of the low- and moderate-income housing and community lending activity of the Bank to the Finance Board. See 12 CFR 951.4(f)(3). The proposed rule would

extend that deadline from March 1 to May 1 and would require each Bank to publish the analysis on a publicly available website within 30 days of its submission to the Finance Board. The proposed change in the due date responds to requests received from some of the Advisory Councils, which meet quarterly, for additional time after the end of each calendar year to prepare, review, and approve their report. Making the Advisory Councils’ analyses available to the public through the Banks’ websites is intended to promote greater transparency and accountability in the Banks’ AHP and in the work of the Banks’ Advisory Councils.

*No delegation: Proposed § 951.4(f).* Proposed § 951.4(f) would prohibit a Bank’s board of directors from delegating to Bank officers or other Bank employees its responsibility for appointing Advisory Council members or for meeting with the Advisory Council. This provision is intended to ensure that each board of directors fulfills its statutory obligations with regard to its interaction with the Advisory Council and is consistent with findings of the Finance Board’s Horizontal Review, which indicated that Bank boards in general could improve how they interact with their Advisory Councils. See 12 U.S.C. 1430(j)(11).

#### *E. Competitive Application Program: Proposed § 951.5*

The proposed rule would consolidate existing regulatory provisions governing the operation of the competitive application program into a single section of the AHP rule—proposed § 951.5. Under the current regulation, a number of those provisions are located in different sections of the AHP regulations. The principal revisions to the existing regulatory structure are described below.

*Eligible applicants: Proposed § 951.5(b)(2).* Section 951.5(b)(2) of the proposed rule would eliminate the current provision that allows a Bank to accept AHP applications from institutions that are not members of the Bank, but that have applied for membership. See 12 CFR 951.6(b)(1). At one time, that provision may have encouraged institutions to become members of their district Bank but the Finance Board believes that given the growth in membership in recent years such an incentive is no longer necessary.

*Eligibility requirements: Proposed § 951.5(c).* Under the proposed rule, § 951.5(c) would set out all of the various eligibility requirements that may apply in connection with the

receipt of AHP subsidies under the competitive application program.

*Timing of household income-eligibility determination: Proposed § 951.5(c)(1).* With regard to the timing of when a household's income eligibility must be determined, the proposed rule would relocate the current provisions from the definitions of "low- or moderate-income household" and "very low-income household" in § 951.1 to proposed § 951.5(c)(1). The proposed rule also would incorporate into this section, without change, the requirements in the existing definitions of "owner-occupied project" and "rental project" that the AHP subsidy be used for the purchase, construction, or rehabilitation of owner-occupied or rental housing.

*Need for subsidy, project costs, project feasibility: Proposed §§ 951.5(c)(2), 951.5(c)(3), and 951.5(c)(4).* The proposed rule would make several changes to the project eligibility requirements applicable to the Banks in determining whether a project is eligible for funding. The Banks currently review projects to assess their "need for subsidy," reasonableness of "project costs," and "feasibility." In determining a project's eligibility, the existing regulation requires that the project demonstrate a need for the subsidy, based on its estimated total sources and uses of funds. See 12 CFR 951.5(b)(2). The proposed rule would maintain this requirement but eliminate a related requirement that the estimated sources and uses of funds analysis include estimates of the market value of in-kind donations and volunteer professional labor or services. See 12 CFR 951.5(b)(2)(i)(B). Experience since 1998 indicates that estimates of non-cash costs generally do not affect the amount of subsidy needed for a project. Elimination of this requirement also would obviate the need for the Finance Board's Regulatory Interpretation 1999-03, which addresses non-cash sources and uses.<sup>2</sup> The proposed rule also would make the need for subsidy requirement independent of the project developmental and operational feasibility requirements. The changes are intended to provide the Banks with more opportunities to assist smaller projects and projects with higher production or operating costs, such as projects with services or more common space.

Section 951.5(c)(3)(i) of the proposed rule would clarify that the determination of project costs is a separate eligibility requirement and would remove a requirement that project costs be "customary" and determined according to "industry standards" in accordance with the Bank's project feasibility guidelines. See 12 CFR 951.5(b)(2)(ii). In lieu of that requirement, the proposal would require a Bank to determine whether a project's costs are reasonable by taking into account the location of the project, development conditions, and other non-financial household or project characteristics, such as housing for the elderly or for persons with disabilities. The changes are intended to make the eligibility review process more adaptive to deeply subsidized projects such as those serving special needs populations.

The existing regulation does not differentiate between the developmental feasibility of a project and, in the case of rental housing, the operational feasibility of the project over time. The proposed rule, at § 951.5(c)(4), would separate these two aspects of project feasibility. Proposed § 951.5(c)(4)(i) would require that a project be developmentally feasible, which is defined as the likelihood that the project will be completed and occupied, based on relevant factors contained in the Bank's project feasibility guidelines, including the project's development budget, market analysis, and the sponsor's experience in providing the requested assistance to households. Proposed § 951.5(c)(4)(ii) would require that a rental project be operationally feasible, which is defined as the ability of the project to operate in a financially sound manner, in accordance with the Bank's project feasibility guidelines, as projected in the project's operating pro forma or similar statement of operational feasibility.

*Financing costs: Proposed § 951.5(c)(5).* The proposed rule would make a technical reorganizing change by relocating the provision regarding interest rates, points, fees, and other charges for loans financing the project from existing § 951.5(b)(2)(iii) to proposed § 951.5(c)(5). See 12 CFR 951.5(b)(2)(iii).

*Refinancing: Proposed § 951.5(c)(8).* Proposed § 951.5(c)(8) would make a technical change regarding the use of AHP subsidies in connection with a refinancing of a project. See 12 CFR 951.5(b)(6). The proposal would clarify that such refinancing is permitted only if it generated equity proceeds and if the proceeds are used to purchase, construct, or rehabilitate eligible housing units. The proposal also would

clarify that the requirement regarding use of the equity proceeds applies only to an amount of equity proceeds that is at least equal to the amount of AHP subsidy in the project.

*Project sponsor qualifications: Proposed § 951.5(c)(10).* Proposed § 951.5(c)(10) would revise existing § 951.5(b)(8) by requiring a Bank to adopt written policies regarding the project sponsor qualifications for revolving loan funds and loan pools, which issues are discussed separately below. See 12 CFR 951.5(b)(8).

*Calculation of AHP subsidy: Proposed § 951.5(c)(12).* Proposed § 951.5(c)(12), which relates to the calculation of the AHP subsidy, would incorporate, without change, the provisions regarding the time at which the calculation of subsidy is to be made. Those provisions are currently included as part of the definition of "subsidy" in § 951.1.

*Use of AHP subsidy by revolving loan funds and loan pools: Proposed §§ 951.5(c)(13) and 951.5(c)(14).* The proposed rule would explicitly authorize the Banks, at their discretion, to allow two uses of AHP subsidy under their competitive application program, which would be for revolving loans funds and loan pools. The current rule defines the term "sponsor" to include certain organizations or public entities that have an ownership interest in a rental project, or that are integrally involved in an owner-occupied project. See 12 CFR 951.1. As noted previously, the proposed rule would expand that definition to add revolving loan funds and entities that establish loan pools to the list of eligible sponsors. A revolving loan fund is a capital fund that makes loans that comply with the requirements of the AHP rule, and then uses the proceeds received from principal payments on those loans to make additional loans to other borrowers. A loan pool is a group of AHP-eligible loans that are purchased, held in trust, and pledged as security for a financial instrument, such as a mortgage-backed security. Definitions of the two terms would be added in proposed § 951.1. Such entities that specialize in community development lending are able to leverage additional funds for low-income borrowers or bring added value to the services provided by non-profit corporations and local governments. These entities also may provide technical assistance in packaging loans, or may service loans, manage affordable housing revolving loan funds, or purchase and sell loans that cannot otherwise be sold in the mainstream secondary market due to their unique characteristics. Proposed

<sup>2</sup> Regulatory Interpretation 199-03 is available in the Freedom of Information Act Reading Room on the Finance Board's Web site: <http://www.thib.gov/Default.aspx?Page=59&ListCategory=8#8>.

§ 951.5(c)(13) and (c)(14) would establish limitations on how such revolving loan funds and loan pools, respectively, may use the AHP subsidies, as described below.

*Use of AHP subsidy by revolving loan funds: Proposed § 951.5(c)(13).* The proposal would authorize the Banks to accept applications from members for projects in which the sponsor would use the AHP subsidy in a revolving loan fund, which in turn would make AHP loans to eligible projects. In order to exercise this authority, a Bank first must consult with its Advisory Council and then must adopt written policies and procedures governing the disbursement of the AHP subsidy through this type of entity. Both the initial loans made by the revolving loan fund, as well as any subsequent loans made with amounts received from repayments of the initial loans, must meet all of the applicable AHP eligibility requirements. The intent in referring to "applicable" AHP eligibility requirements is to make clear that those regulatory requirements that apply to AHP applications that involve a specific project, such as cost and feasibility requirements, will not automatically be applied to an AHP application from a revolving loan fund, which may not have identified a specific project at the outset.

The revolving loan fund also must assure that the initial loans are made to projects and households that meet the commitments in the approved AHP application and that they will be met for the full AHP retention period. Any subsequent lending of repaid AHP subsidy must be used for low- or moderate-income households (in the case of owner-occupied projects) or for rental projects where 20 percent or more of the units are occupied by and affordable for very low-income households, subject to the AHP retention period, monitoring and recapture requirements that the Bank must adopt. As a result of those requirements, AHP funds disbursed through a revolving loan fund may not be used for other purposes, such as to pay for operating costs or other uses unrelated to the purchase, construction, or rehabilitation of housing. In general, the Finance Board requests comment on how the revolving loan fund authority could be used within the requirements of the AHP.

*Use of AHP subsidy in loan pools: Proposed § 951.5(c)(14).* The proposed rule would authorize a Bank to provide AHP subsidies to its members under circumstances in which another entity would receive the subsidy and then commit to purchase AHP-eligible loans in order to pool them and sell interests

in the pool of loans, such as through loan participations or a mortgage-backed security. For example, the proposed rule would allow a Bank to make a subsidized advance to a member with the understanding that the member would make a subsidized loan to another entity, which would commit to purchase similarly subsidized loans from other originators. In order to exercise this authority, a Bank first must consult with its Advisory Council, and then must adopt written policies and procedures governing the disbursement of the AHP subsidy through this type of arrangement. The proposed rule includes a number of provisions that are intended to ensure that subsidies disbursed through a loan pool actually benefit AHP-eligible households. Specifically, the proposal would require that a loan pool sponsor demonstrate that its use of the subsidy will meet all applicable eligibility requirements under the AHP regulation. The loan pool sponsor must provide to the Bank the acceptance standards that it intends to use in determining which loans to include in the pool, as well as the underwriting characteristics for such loans, and the number of eligible households (including their income levels) that have obtained loans over a given time period. The proposal would prohibit the use of AHP funds for the loan pool's operating costs, for secondary market transaction costs, or for providing liquidity to the originators or holders of the purchased loans.

In order to ensure that the AHP subsidy benefits eligible households, the proposed rule would require that the manager or trustee of the loan pool purchase the loans pursuant to a forward commitment that identifies the characteristics of the loans to be originated with principal or interest rate reductions, as specified in the approved AHP application. Where AHP direct subsidy is being used, the AHP subsidy must be used for a standard upfront buy-down of the interest rate or a reduction in the principal of the loans in the pool, as specified in the approved AHP application. All loans purchased by the loan pool, including both the initial loans and any subsequent loans that are intended to replace loans that have been paid off, must conform to the terms of the forward commitment. In general, the Finance Board requests comment on how the loan pool authority could be used within the requirements of the AHP. The proposed rule is silent on the length of time that a project sponsor would have, as specified in the forward commitment, for the sponsor to expend the full

amount of the AHP subsidy. The Finance Board requests comment on whether it is preferable to establish a time limit by regulation and if so, the duration of that time limit, or to allow a Bank to establish a time limit as part of its AHP Implementation Plan, as proposed.

In the alternative, the loan pool would be permitted to purchase an initial round of loans that are not purchased pursuant to a forward commitment, provided that the entities from which the loans are purchased are required to use the proceeds from the initial loan purchases within time limits specified in the Bank's AHP Implementation Plan. The proceeds must assist households that are income-eligible under the approved AHP application during subsequent rounds of lending, and the assistance must be provided in the form of a principal reduction or a below-market AHP subsidized interest rate, as specified in the approved AHP application.

In addition, each AHP-assisted owner-occupied unit receiving AHP direct subsidy would be required to be subject to an AHP 5-year retention agreement. As currently written, the proposed rule explicitly permits the use of AHP subsidy in loan pools backed by owner-occupied units. The Finance Board requests comment on whether, in addition to loans for AHP-assisted owner-occupied units, rental housing loans should also be eligible under the AHP loan pool authority, and if so, what kinds of loans and activities, consistent with the AHP requirements, should be eligible.

*Out-of-district projects eligibility requirement: Proposed § 951.5(c)(15).* The proposed rule would remove the existing provision that allows a Bank, at its discretion, to require as an eligibility requirement that a project assisted with AHP subsidy must be located in the Bank's district. See 12 CFR 951.5(b)(10)(i)(B). Proposed § 951.5(c)(17) also would prohibit a Bank from establishing an eligibility requirement that a project must be located in the Bank's district. See the further discussion of this issue below, under AHP projects outside the district.

*Minimum Bank credit product usage requirement: Proposed § 951.5(c)(15).* The current rule authorizes a Bank to require its members to have used a minimum amount of the Bank's other credit products within the previous 12 months as a condition to applying for additional amounts of AHP subsidy. See 12 CFR 951.5(b)(10)(i)(C). The Finance Board is proposing to remove this requirement in the belief that AHP funding should go, without restriction,

to applications from members that score highest under a Bank's competitive application scoring criteria.

*Counseling requirement: Proposed § 951.5(c)(15)(ii).* The proposed rule would authorize a Bank to require homebuyer or homeowner counseling as an optional eligibility requirement for owner-occupied projects under the competitive application program. Under such a requirement, the Banks could limit AHP subsidies to owner-occupied projects that provide this resource for low- or moderate-income households. Such counseling can contribute to successful, long-term homeownership, which the Finance Board has recognized in supporting such counseling for low- or moderate-income households receiving home purchase assistance under the AHP homeownership set-aside program. See 12 CFR 951.5(a)(2)(ii).

*Prohibited use of AHP subsidy: prepayment fees: Proposed § 951.5(c)(16)(i).* The current rule allows a project to use AHP subsidy to pay prepayment fees imposed by a Bank on a member if the member prepays a subsidized advance, provided that the project continues to comply with the terms of the approved AHP application for the duration of the original retention period and any unused AHP subsidy is returned to the Bank and made available for other AHP projects. See 12 CFR 951.5(b)(4)(i). The proposed rule would eliminate this provision, consistent with the principle that AHP funds should be used for purchase, construction, or rehabilitation of housing.

*Changes to the scoring system: Proposed § 951.5(d).* The proposed rule would retain the current provisions that require each Bank to adopt written scoring guidelines for its AHP applications and to allocate 100 points among 9 scoring criteria. See 12 CFR 951.6(b)(4). The proposal would not make any substantive changes to those criteria, except for those relating to disaster areas and out-of-district projects, but would make a number of technical revisions to the current rules and would codify certain staff interpretations.

The proposed rule would retain the provisions relating to fixed-point and variable-point scoring criteria, but would make technical changes to the latter, the effect of which would be to codify a current staff interpretation that allows a Bank to implement variable-point scoring criteria either through a fixed scale or on a scale relative to the other applications that are to be scored in the same funding round. See 12 CFR 951.6(b)(4)(iii). That provision would be

located at § 951.5(d)(3)(ii) of the proposed rule.

Section 951.5(d)(5)(iii)(A) of the proposed rule would remove a provision of the existing rule, which allows a Bank to score rental projects according to the targeting commitments made by the project to a governmental or tax-credit allocating entity that provides funds or tax credits, respectively, to the project. See 12 CFR 951.6(b)(4)(iv)(C)(1). That provision would no longer be necessary because of other proposed changes to the rule, to be located at § 951.7(a)(2)(ii)(B), discussed further below, which would allow a Bank to rely on monitoring by governmental or tax-credit monitoring agencies.

The proposed rule also would clarify regulatory practice relating to the scoring criterion for income targeting in owner-occupied projects. That provision, which would be located at § 951.5(d)(5)(iii)(B), would clarify that a Bank may determine in its AHP Implementation Plan how to award scoring points on a declining scale, taking into consideration the percentages of units and targeted income levels.

*Disaster areas and displaced households scoring criterion: Proposed § 951.5(d)(5)(vi)(E).* The current regulation permits the Banks to award scoring points to the financing of housing that is located in federally declared disaster areas. See 12 CFR 951.6(b)(4)(iv)(F)(5). Because disasters may displace families from their homes, the Finance Board believes that this criterion should be expanded to address such situations. Accordingly, in order to accommodate families that have been displaced from a disaster area, § 951.5(d)(5)(vi)(E) of the proposed rule would permit a Bank to award scoring points for applications that would provide housing for persons located in a disaster area, as well as for applications proposing to provide housing for low- or moderate-income households that have been displaced from a federally declared disaster area due to a disaster, irrespective of the household's current residential location.

*AHP projects outside the district: Proposed §§ 951.5(c)(17) and 951.5(d)(5)(vii).* Under the current regulation, a Bank may, at its discretion, deny consideration of applications to the AHP competitive application program from members proposing to fund projects located outside a Bank's district. Another provision of the current rule permits a Bank to give scoring point preference to the creation of housing located within the Bank's district. See 12 CFR 951.5(b)(10)(i)(B)

and 951.6(b)(4)(iv)(F)(12). The proposed rule would rescind the Banks' authority to prohibit or restrict applications to fund projects located outside a Bank's district. This authority may have been appropriate when all Bank members did business only within the boundaries of a state within the Bank's district. As a result of interstate branching, however, many members now do business in communities outside their Bank district. The authority to restrict AHP projects to the Bank's district, if exercised, would limit a member's ability to support otherwise eligible AHP projects in certain of the communities that it serves solely because those communities were located outside the Bank's district boundaries.

The Bank Act does not set up the AHP as a geographically targeted program. Rather, it requires each Bank to establish a program to provide subsidized funding to its members. See 12 U.S.C. 1430(j)(1). Restrictions on out-of-district projects can disadvantage members with geographically dispersed operations to the extent the Bank limits funding of projects outside of its boundaries, irrespective of the market areas served by its members. Such restrictions could also serve to disadvantage communities that are served by financial institutions headquartered in a state located in a different Bank district. The Finance Board believes that AHP projects should be awarded funds based on the merits of each particular application. If an application has sufficient merit to compete successfully, it should be awarded AHP funds irrespective of the project location, so long as the project is within a community served by a member.

Finally, the existing authority in the current AHP regulation has not been extensively invoked by the Banks. In 2004, only one Bank prohibited the use of AHP funds for out-of-district projects and only two Banks elected to give scoring preference to in-district projects. Nor has there been a significant outflow of AHP funds as a result of member financing of projects outside the district. Out of 10,391 AHP projects funded since the beginning of the program in 1990, only 323 projects, or 3.1 percent, have been located outside a Bank's district. These findings support a conclusion that funding of out-of-district projects has a minimal impact on the AHP. Therefore, a prohibition against out-of-district projects or a preference for projects within a district may not be warranted.

As a result of all these considerations, the proposed rule would eliminate the two provisions in the existing regulation



that preclude or limit the ability of a member to receive AHP subsidies for projects located outside its district, and proposed § 951.5(c)(17) would expressly prohibit a Bank from requiring that a project be located within its district. In addition, proposed § 951.5(d)(5)(vii) would prohibit a Bank from adopting as its Second District Priority a scoring preference for projects located in the Bank's district. See 12 CFR 951.6(b)(4)(iv)(G).

*Modifications of approved applications: Proposed § 951.5(f).* The proposed rule would codify current practice by adding a requirement that a Bank must document in writing its analysis and justification for any modification of a previously approved project. See 12 CFR 951.7(a).

*Progress towards use of AHP subsidies: Proposed § 951.5(g)(2).* The proposed rule would require each Bank to establish policies and procedures, such as time limits, for determining whether progress is being made towards drawdown and use of AHP subsidies by approved projects, and whether to cancel an application approval for lack of such progress. Progress requirements must be included in the Bank's AHP Implementation Plan. Affordable housing projects often may encounter delays due to changes in funding, legal, or community challenges, or other events. These delays may affect the ability of a project to progress towards its scheduled drawdown and use of the AHP subsidy. The current AHP regulation requires a Bank to specify a time period in its AHP Implementation Plan for the drawdown and use of the AHP subsidy. If a project does not do so within such period, the Bank must cancel its approval of the application. See 12 CFR 951.8(c)(1). The rigidity of this requirement sometimes has impaired the ability of the Banks to determine whether the delays are significant enough to affect a particular project's ability to draw down and use the subsidy. While the Banks have extended the time period for certain projects in an effort to take into account such delays, the requirement that a fixed time period be stated in the AHP Implementation Plan limits a Bank's ability to manage this process. Accordingly, the proposed rule would give the Banks greater capacity to manage this process by requiring them to adopt policies and procedures that address how they will make such determinations.

*Compliance upon disbursement: Proposed § 951.5(g)(3).* Section 951.5(g)(3) of the proposed rule would require a Bank to establish policies and procedures for determining, prior to

initial disbursement of AHP subsidy, and prior to subsequent disbursement if the need for AHP subsidy has changed, whether the project continues to meet the applicable eligibility requirements and all obligations committed to in the approved AHP application. The Bank's requirements must be included in its AHP Implementation Plan. Under the current AHP regulation, a Bank is required to verify compliance with eligibility requirements and application commitments prior to each disbursement of AHP subsidy. See 12 CFR 951.8(c)(2). The requirement to repeatedly verify project compliance during every stage of the disbursement process may be more than is necessary to ensure compliance with the rules, and effectively precludes a Bank from using its best judgment to determine whether the circumstances of a particular AHP project warrant repeated verification of compliance with the rules. The proposed amendment would give the Banks greater latitude in determining when it is appropriate to verify compliance prior to disbursing AHP funds.

*Bank board of directors duties and delegation: Proposed § 951.5(h).* The proposed rule would set forth the Bank board of directors' various duties regarding establishment and implementation of the competitive application program requirements in one section, proposed § 951.5(h), and would reiterate that the Bank's board cannot delegate these responsibilities to Bank officers or other Bank employees.

#### *F. Homeownership Set-Aside Program: Proposed § 951.6*

The proposed rule would reorganize the existing regulation, generally by combining various homeownership set-aside program provisions into one section, to be located at proposed § 951.6.

*Eligible applicants: Proposed § 951.6(b).* The existing AHP regulations permit a Bank to accept applications for homeownership set-aside program subsidies from an institution that is not a member of the Bank, but which has pending an application for membership. See 12 CFR 951.6(a). The proposed rule would eliminate this provision and would require an applicant to be a member of the Bank at the time that it submits an AHP application. The rationale for this revision was discussed in connection with a similar amendment that is proposed for the competitive application program.

*Timing of household income-eligibility determination: Proposed § 951.6(c)(2)(i).* Section 951.6(c)(2)(i) of the proposed rule would clarify that a

household's income eligibility is to be determined at the time that it is enrolled in the set-aside program. This change is intended to address confusion with respect to the income eligibility, for example, of a household that is enrolled in a matched savings account program, an Individual Development Account program, a Welfare-to-Work program, or any other similar empowerment program designed to assist low-income households accumulate assets. The existing regulation has been interpreted by some Banks as requiring that the household's income qualification for purposes of the AHP be determined at the time that the household is qualified for a loan. See 12 CFR 951.1 and 951.5(a)(2)(i). The proposal would permit income eligibility to be determined at the time that the household is accepted by the member and the Bank to enroll in the AHP set-aside program, even though at that time the household may not qualify for a mortgage. This clarification is consistent with existing Finance Board policy and reflects the Finance Board's understanding that the purpose of these programs is to prepare households for homeownership. Activities designed to qualify low- or moderate-income households for mortgages should be encouraged. Such programs, however, require careful administration by a Bank and the participating member and should be subject to reasonable Bank policies and procedures on the timely use of AHP subsidy. Moreover, it is the Finance Board's expectation that Bank policies will preclude use of the program by individuals whose low- or moderate-income eligibility is a temporary condition, such as students, who would ordinarily have a reasonable prospect for a substantial increase in income upon entering the workforce.

*Counseling: Proposed § 951.6(c)(2)(ii).* Under the existing regulation, all households receiving AHP funds under a Bank's homeownership set-aside program must complete a homeowner or homebuyer counseling program. See 12 CFR 951.5(a)(2)(ii). The Finance Board is proposing to make this an option rather than a requirement, for obtaining subsidies under the homeownership set-aside program. As a practical matter, not all households will necessarily require such counseling. Moreover, there are some areas of the country in which such counseling may not be readily available, and the quality of the counseling can also vary. Accordingly, § 951.6(c)(2)(ii) of the proposed rule would allow each Bank to determine whether to include counseling as an eligibility requirement in its AHP Implementation Plan. These



revisions are consistent with the proposed change that would allow a Bank to adopt such a counseling requirement under its competitive application program, which is located at proposed § 951.5(c)(15)(ii).

Notwithstanding the change, the Finance Board encourages the Banks to consider requiring homeowner and homebuyer counseling when they believe it to be appropriate. Proposed § 951.6(c)(8) would retain the current provision that allows homeownership set-aside funds to be used to pay for the costs of obtaining such counseling for those homebuyers that actually purchase an AHP-assisted unit. See 12 CFR 951.5(a)(7).

*Member financial incentives: Proposed § 951.6(c)(6).* The proposed rule would revise the existing regulation by requiring a Bank to establish incentives for members to provide financial or other assistance in connection with providing the homeownership set-aside subsidy. Under existing § 951.5(a)(6), a member that provides mortgage financing to a participating household under the set-aside program must also provide financial or other incentives in connection with the mortgage financing. See 12 CFR 951.5(a)(6). Some Banks have observed that this requirement may place small members, such as those located in rural areas, at a disadvantage and may encourage them to pass the AHP subsidy to a larger institution, which may or may not be a member of that Bank. The existing requirement may thus place a greater obligation to provide subsidized financing on a member than on a nonmember mortgage provider and may result in a disincentive for member financing. The Finance Board specifically requests comment on: (1) Whether it should require all originators of AHP-assisted mortgage loans to provide financial or other incentives in connection with the mortgage financing, irrespective of whether the originator is a member or nonmember; (2) whether the current financial incentive requirement should remain as a mandatory requirement or be made a matter of discretion for the Bank, as a preferential selection criterion for its homeownership set-aside program(s); and (3) whether additional incentives should be required, such as a matching funds requirement, member-provided financing, or preference to a member working in partnership with a nonprofit sponsor assisting first-time homebuyers to qualify for a mortgage.

*Financing costs: Proposed § 951.6(c)(7).* Section 951.5(a)(6) of the current regulations requires that the rate

of interest, points, fees, and other charges imposed by the member not exceed a reasonable market rate. See 12 CFR 951.5(a)(6). As currently worded, the requirement applies only to situations in which the member provides the financing, but not if a third party does so. The Finance Board is concerned that the existing language has the potential to create opportunities for using AHP funds in conjunction with the origination of loans with interest rates, points, fees, and other charges that exceed a reasonable market rate, if the loans are originated by a nonmember. In order to avoid that possibility, § 951.6(c)(7) of the proposed rule would revise the regulation to state that such charges that are “used directly or indirectly in conjunction with the AHP direct subsidy” must not exceed a reasonable market rate. That revision is consistent with the statutory requirement that Finance Board regulations must “ensure that subsidies provided by Banks to member institutions \* \* \* are passed on to the ultimate borrower.” See 12 U.S.C. 1430(j)(9)(E).

*Progress towards use of AHP subsidy: Proposed § 951.6(c)(9).* For reasons similar to those discussed above under the competitive application program, proposed § 951.6(c)(9) would revise the existing regulation by requiring that progress be made towards draw-down and use of the AHP direct subsidies by eligible households pursuant to policies and procedures adopted by the Bank. See 12 CFR 951.5(a)(8).

*Cash backs: Proposed § 951.6(c)(10).* The Finance Board’s Horizontal Review identified problems in the operations of the homeownership set-aside programs at some of the Banks. Although those problems were limited to a few situations, the proposed rule seeks to address them by clearly identifying ineligible uses of AHP set-aside funds. Therefore, § 951.6(c)(10) of the proposed rule would expressly prohibit a member from providing cash back to a household at the closing on the mortgage loan and would require a member to use any AHP subsidy beyond what is needed for closing costs and the approved mortgage amount to further reduce the principal of the mortgage loan.

*Progress towards use of AHP subsidies: Proposed § 951.6(e)(2).* For reasons similar to those discussed above under the competitive application program, proposed § 951.6(e)(2) would require a Bank to establish policies and procedures, such as time limits, for determining whether progress is being made towards drawdown and use of homeownership set-aside funds by

eligible households, and whether to cancel application approvals for lack of such progress. See 12 CFR 951.8(b)(1). The requirements must be specified in the Bank’s AHP Implementation Plan. A Bank would be required to determine, pursuant to such policies and procedures, whether progress is being made by eligible households, and whether to cancel any application approvals for lack of progress.

#### *G. Monitoring: Proposed § 951.7*

The proposed rule would retain the current requirement for annual certifications by rental project owners to the Bank under the competitive application program, but would make a number of changes to the monitoring provisions under both the competitive application and homeownership set-aside programs. A number of the current monitoring provisions are prescriptive in nature and set deadlines by which the Bank and other parties must undertake certain actions. See 12 CFR 951.10 and 951.11. The proposed rule would replace those provisions with more broadly stated performance objectives, which are intended to allow the Banks more latitude in determining the type and frequency of reports and certifications that are best suited for monitoring a particular project’s compliance with the AHP rules. The proposed amendments would accomplish this goal by requiring the Banks to adopt policies and procedures for monitoring progress made towards project completion and compliance with other AHP requirements.

#### 1. Monitoring Requirements for the Competitive Application Program: Proposed § 951.7(a)

*Initial monitoring policies and procedures: Proposed § 951.7(a)(1).* For both owner-occupied and rental projects under the competitive application program, the proposed rule would require each Bank to adopt written policies and procedures for monitoring AHP projects prior to, and within a reasonable period of time after, project completion. Specifically, a Bank’s monitoring policies and procedures must enable it to determine: Whether the construction or rehabilitation is progressing satisfactorily; whether a completed project is progressing satisfactorily toward occupancy by eligible households; and whether a project is meeting the commitments made in the approved AHP application and is otherwise in compliance with applicable AHP requirements within a reasonable time after the project has been completed. The proposed rule would remove the existing requirement

that the Banks must monitor project habitability, and also would remove the definition of "habitable" from the existing definitions. See 12 CFR 951.1 and 951.10(a)(2)(ii)(B)(2) and (c). Proposed § 951.7(a)(1)(ii) would require a Bank's monitoring policies and procedures to include provisions requiring Bank review of back-up documentation regarding household incomes and rents that are maintained by the project sponsor or owner, and would allow a Bank to include requirements for maintenance and Bank review of other project documentation, at the Bank's discretion.

*Long-term monitoring policies and procedures: Proposed § 951.7(a)(2).* The proposed rule would require a Bank to adopt written policies and procedures for monitoring completed rental projects, commencing in the second year after project completion and continuing for the full 15-year retention period. The monitoring policies must enable a Bank to determine whether household income, rents, and populations served comply with the respective commitments made in the AHP application. The proposed rule would remove the existing requirement that the Banks monitor project habitability for the full AHP retention period. See 12 CFR 951.11(a)(3). The policies also must take into account various risk factors and could allow the Bank to use a reasonable risk-based sampling plan.

Proposed § 951.7(a)(2)(iii) would require that monitoring policies include provisions addressing: Bank review of annual certifications by project owners that household incomes and rents comply with commitments made in the AHP application and other AHP requirements; Bank review of back-up project documentation regarding household incomes and rents, as maintained by the project owner; and maintenance and Bank review of such other project documentation that the Bank deems necessary.

The current regulation requires the Banks to select from 1 of 3 approved methods for long-term monitoring of rental projects: (1) Monitoring by a federal, state, or local government entity in connection with a project that also is receiving tax credits or funds from that entity, subject to certain other limits stated in the rule; (2) monitoring of such projects by a contractor; or (3) monitoring by the Bank, its members, and project owners. See 12 CFR 951.11(a). The existing regulation contains prescriptive procedural requirements for projects monitored by the Banks, their members, and project owners under the third option. It details

specific monitoring and certification duties for the parties and includes deadlines for submission of specific monitoring reports. These deadlines may not comport with construction and development schedules and can result in regulatory noncompliance for reasons that do not reflect the actual performance of a project. The existing regulation requires a Bank to review project documentation and verify compliance with rent, income, and project habitability requirements according to a schedule based on the amount of AHP subsidy received by a project, such that projects receiving greater amounts of subsidy have more stringent and frequent monitoring requirements. See 12 CFR 951.11(a)(3)(iii).

Such prescriptive monitoring requirements do not necessarily promote accurate assessments of program effectiveness or take into account the true risks to the Bank's AHP. The existing monitoring requirements also may fail to capture adequately the operational risk, financial performance risk, location risk, or other relevant performance factors affecting the Bank's AHP project portfolio. Moreover, the prescriptive nature of the regulations implies that the particular approach to monitoring that is embodied in the regulation is the optimal approach for such matters, irrespective of the risk characteristics that may be associated with a particular AHP project or the compliance record of the participating member, sponsor, or owner.

Proposed § 951.7(a)(2) would require a Bank to develop written policies and procedures for long-term monitoring of rental projects, taking into account various risk factors. Those policies and procedures would be subject to Finance Board examination annually. A Bank's policies and procedures would be required to take into account certain risk factors, such as the amount of AHP subsidy in the project, the type, size, and location of the project, sponsor experience, and any monitoring provided by a federal, state, or local entity, as discussed further in the following section.

*Reliance on other monitoring: Proposed § 951.7(a)(2)(ii)(B).* Section 951.7(a)(2)(ii)(B) of the proposed rule would expand the ability of the Banks to rely on the monitoring of AHP-assisted rental projects by other governmental agencies that are providing tax credits or other funds to the projects. In the case of AHP projects that also receive tax credits or other governmental funds, the existing regulation permits a Bank to rely on the

monitoring conducted by the federal, state, or local government entity providing the tax credits or funds, or by certain third parties, provided that the income targeting, rents, and retention period requirements monitored by such entities for their own programs are the same as, or more restrictive than, those committed to in the approved AHP application. See 12 CFR 951.11(a)(1).

The LIHTC, which often is used by projects that receive some form of AHP subsidy, has two elective eligibility standards related to the units in the project and the income of the households occupying the units: (1) that 20 percent of the units must be occupied by households with incomes at or below 50 percent of the area median income; or (2) that 40 percent of the units must be occupied by households with incomes at or below 60 percent of the area median income. See 26 U.S.C. 42(g)(1). The Bank Act imposes similar limits on the use of AHP subsidies for rental housing, *i.e.*, eligible rental projects must have at least 20 percent of the units occupied by households with incomes at or below 50 percent of the area median income. See 12 U.S.C. 1430(j)(2)(B). Because this AHP standard is identical to the first tax credit standard, the Finance Board has deemed it to be substantively equivalent to the income eligibility standard required for an LIHTC project. For AHP-assisted tax credit projects that employ the first standard, the current AHP regulation permits a Bank to accept the project monitoring that is conducted by, or on behalf of, the government agencies that have provided the tax credits.

With respect to AHP-assisted tax credit projects that employ the second standard, under which 40 percent of the units must be occupied by households with incomes at or below 60 percent of the area median income, the current AHP regulation allows a Bank to rely on monitoring conducted by or on behalf of other governmental agencies only if those entities also monitor the project for compliance with the AHP standard. Because this tax credit standard differs from the AHP standard, a Bank may be required to negotiate agreements with various state agencies or contractors to conduct their monitoring of the project in accordance with the AHP standard, which is common to both programs. Such additional monitoring entails additional costs to the Bank, which a number of the Banks have contended is not an effective means of monitoring the project, as it is largely duplicative of existing monitoring conducted by other parties. A number of AHP users also have contended that this level of

monitoring is superfluous and adds unnecessary burdens to the project.

After reviewing several studies on the performance of the LIHTC, the Finance Board has concluded that the overwhelming majority of these tax credit projects—irrespective of their income eligibility standard—meet the AHP income eligibility standard in a substantially equivalent manner. A 1997 General Accounting Office study found that 75 percent of households in tax credit projects had incomes under 50 percent of the area median income, which would be well within the AHP requirement that 20 percent of units be occupied by households with incomes at or below 50 percent of the area median income. Other subsequent studies, such as those prepared by Abt Associates for HUD, and one by Ernst and Young, have come to similar conclusions regarding the targeting of tax credit projects to very low-income households. Moreover, the Finance Board notes that the length of the retention periods for AHP rental projects and tax credit projects is the same, and that noncompliance with the income-eligibility requirements by tax credit projects is relatively rare, as it would lead to adverse tax consequences for investors in such projects. The Finance Board also notes that the affordability standard for tax credit projects, *i.e.*, the rent requirement, is substantially equivalent to the AHP rent requirement that the rents charged may not exceed 30 percent of the targeted household income. *See* 12 U.S.C. 1430(j)(13)(D) and 26 U.S.C. 42(g)(2). Accordingly, the Finance Board is proposing to amend the AHP regulation to allow a Bank to rely on the monitoring by the state-designated housing credit agency administering the tax credits of the income targeting, rent, and retention period requirements applicable under the LIHTC, provided that the compliance profiles of the AHP and the LIHTC continue to be substantively equivalent.

In addition, for AHP projects that receive funds from federal, state, or local government entities, the proposed rule would allow a Bank to rely on the monitoring by such entities of the income targeting, rent, and retention period requirements applicable under their programs, provided that: The income targeting, rent, and retention period requirements for those programs are substantively equivalent to those of the AHP; the entity has demonstrated and continues to demonstrate its ability to monitor the project; the entity agrees to provide reports to the Bank on the project's incomes and rents for the full 15-year AHP retention period; and the

Bank reviews the reports from the monitoring entity to confirm that they comply with the Bank's monitoring policies and procedures.

#### 2. Monitoring Requirements for the Homeownership Set-Aside Program: Proposed § 951.7(b)

The proposed rule would retain the member certification requirements from the existing regulation and would require a Bank to adopt and implement its own written monitoring policies and procedures for determining compliance with the requirements of its homeownership set-aside programs. *See* 12 CFR 951.8(b)(2). The Banks would be allowed to use a reasonable sampling plan to select the households to be monitored and to review the back-up and any other documentation received by the Bank. The proposed rule also would provide that the Bank's monitoring policies and procedures must include requirements for the Bank to review back-up documentation regarding household incomes maintained by the member, and may include requirements for maintenance and Bank review of other documentation, in the Bank's discretion.

#### H. Remedial Actions for Noncompliance: Proposed § 951.8

Proposed § 951.8 would reorganize and streamline the language in the existing regulations regarding remedial actions for noncompliance with the AHP regulations in order to eliminate redundancy and provide greater clarity. *See* 12 CFR 951.12.

*Repayment of AHP subsidy by project sponsor or owner: Proposed § 951.8(b)(2).* Proposed § 951.8(b)(2) would add a provision allowing a Bank to determine whether a project sponsor or owner must repay AHP subsidies directly to the Bank or to the member, which would then repay the Bank, in the event that the project fails to comply with any of the AHP requirements. Under the existing regulation, project sponsors or owners are required to repay AHP subsidies to the member, which in turn is required to repay the subsidies to the Bank. *See* 12 CFR 951.12(b). The proposed change would give the Banks greater flexibility in managing how AHP subsidies are required to be repaid in the event of a failure to comply with the rules.

*Finance Board approval of settlements: Proposed § 951.8(d)(2).* The proposed rule also would revise provisions of the existing regulation that allow a Bank to obtain approval from the Board of Directors of the Finance Board to settle a disputed claim regarding an AHP subsidy. *See* 12 CFR

951.12(c)(2)(ii). As revised, the rule would allow the Bank to obtain the approval from "the Finance Board," which would allow Finance Board staff to approve the Bank's proposed settlements relating to the AHP subsidy.

*Bank reimbursement of AHP fund: Proposed § 951.8(e)(1).* The proposed rule would add a provision requiring a Bank to reimburse its AHP fund in the amount of any AHP subsidies (plus interest, if appropriate) misused as a result of the Bank's actions or omissions, even without a Finance Board order to do so. *See* 12 CFR 951.12(c)(3). Where noncompliance with AHP requirements is the result of a Bank's actions or omissions, the Bank should reimburse its AHP fund without the Finance Board having to order it to do so.

*Parties to enforcement proceedings.* The proposed rule would remove an existing regulatory provision, located at 12 CFR 951.12(d), that allows a Bank to enter into a written agreement with a member, project sponsor, or project owner under which it consents to be a party to a Finance Board enforcement action regarding the repayment of AHP subsidies that it has received or to suspension or debarment, provided that it has agreed to be bound by the Finance Board's final determination in the enforcement proceeding. This provision would be removed because regulatory authorization is not necessary for a Bank to enter into such an agreement.

*Re-use of repaid AHP direct subsidies in same project: Proposed § 951.8(f)(2).* The proposed rule would clarify that a Bank must consult with its Advisory Council in determining whether to allow the re-use of AHP direct subsidies in the same project, as is authorized under this section. *See* 12 CFR 951.12(e)(2). That provision also would clarify that a Bank's board of directors cannot delegate to Bank officers or other Bank employees the responsibility to adopt any Bank policies on re-use of repaid AHP direct subsidies in the same project under this section.

#### I. Agreements: Proposed § 951.9

The existing regulations require each Bank to have in place with each member that receives AHP subsidies a written agreement that includes certain provisions set out in the regulation. *See* 12 CFR 951.13. The proposed rule, at § 951.9, would revise the provisions of the existing regulation in order to eliminate redundancy and provide greater clarity.

*Notification of member: Proposed § 951.9(a)(1).* The proposed rule, at § 951.9(a)(1), would add a provision requiring the AHP agreements to

acknowledge that the member has been notified of the AHP requirements and all Bank policies relevant to the member's approved AHP application.

*Monitoring agreements: Proposed § 951.9(a)(5).* Proposed § 951.9(a)(5) would revise the provisions relating to monitoring in order to conform them to the changes proposed elsewhere to the substantive monitoring requirements. See 12 CFR 951.13(b)(4). Under the proposed change, the Banks' agreements with their members would have to set forth the members' specific monitoring responsibilities, as required under the Banks' monitoring policies and procedures. In addition, these agreements would have to require the member to have in place its own agreement with each project sponsor and project owner setting forth the specific monitoring responsibilities of those sponsors and owners, as required under the Banks' monitoring policies and procedures.

*Refinancing of owner-occupied units: Proposed § 951.9(a)(7)(ii)(A).* Proposed § 951.9(a)(7)(ii)(A) would revise existing § 951.13(c)(4)(i)(B) by providing that, in the case of a refinancing prior to the end of the 5-year retention period of a permanent mortgage loan that was funded by an AHP subsidized advance, the household would not have to repay the AHP subsidy it already used in the unit. See 12 CFR 951.13(c)(4)(i)(B). The existing regulation requires the household to repay the full amount of the AHP subsidy received (*i.e.*, the value of the interest rate subsidy for the time the household has been paying on the mortgage loan) from any net gain realized upon the refinancing, unless the unit continues to be subject to a retention agreement. The proposed change would be consistent with the existing regulatory provision providing that a household subsidized with AHP direct subsidy that refinances an owner-occupied unit must repay only the amount of AHP subsidy that has not been used (*i.e.*, the subsidy required to be repaid is reduced for every year the household owned the unit). See 12 CFR 951.13(d)(1)(iii). In addition, the proposed change would help remove a possible deterrent to refinancing by households that seek to make their units more affordable or obtain equity for purposes of their economic betterment.

*Relocation of households in rental projects: Proposed § 951.9(a)(8)(iii)(B).* Proposed § 951.9(a)(8)(iii)(B) would revise the existing regulation by providing that, in the case of a sale or refinancing of an AHP-assisted rental project prior to the end of the retention period, the AHP subsidy would not have to be repaid to the Bank if the

households are relocated to another property that is made subject to a deed restriction or other legally enforceable retention agreement or mechanism incorporating the income-eligibility and affordability restrictions committed to in the approved AHP application for the remainder of the retention period. See 12 CFR 951.13(c)(5)(iii) and 951.13(d)(2)(iii). The proposed change would allow Banks to deal with situations where approved rental projects are forced to relocate for reasons such as the exercise of eminent domain or a need for additional units or services, and the project sponsors will be transferring the same residents to a new building. Currently, the AHP regulation treats these situations as a sale that requires the repayment of the entire amount of AHP subsidy, thereby releasing the project from its AHP commitments and making the AHP subsidy available for other AHP-eligible projects, unless the property continues to be subject to a deed restriction or other legally enforceable retention agreement or mechanism incorporating the income-eligibility and affordability restrictions committed to in the AHP application for the remainder of the retention period. Allowing project sponsors to transfer the AHP subsidies, along with the corresponding income-eligibility and affordability commitments, to a new building would result in the retention of the affordable units for the duration of the original retention period and ensure that existing tenants are not adversely affected.

*Agreements between Banks and project sponsors or owners: Proposed § 951.9(b).* As discussed above, proposed § 951.8(b)(2) would allow a Bank to determine whether to require a project sponsor or owner to repay AHP subsidies directly to the Bank in the event of noncompliance, in contrast to the existing regulation which requires project sponsors or owners to repay AHP subsidies to the member, which in turn repays the subsidies to the Bank. Under proposed § 951.9(b), if a Bank intends to require project sponsors or owners to repay AHP subsidies directly to the Bank, the Bank first must have in place an agreement with each project sponsor or project owner under which the party agrees to repay the AHP subsidies directly to the Bank.

*Application to existing projects: Proposed § 951.9(c).* The proposed rule would streamline the language in existing § 951.16, which addresses the application of the regulation to existing AHP projects, and relocate the provision to proposed § 951.9(c). See 12 CFR 951.16.

*J. Conflicts of Interest: Proposed § 951.10*

The proposed rule would relocate the provisions governing the adoption of conflict of interest policies from existing § 951.3(c) to proposed § 951.10. See 12 CFR 951.3(c). The proposed rule also would add new provisions that would prohibit Bank directors or employees or Advisory Council members, and their family members, from engaging in the conflicts of interest prohibited by the conflict of interest policies. Proposed § 951.10(c) would prohibit a Bank's board of directors from delegating to any Bank officers or other Bank employees its responsibility to adopt the conflict of interest policies.

*K. Temporary Suspension of AHP Contributions: Proposed § 951.11*

Proposed § 951.11 would remove various procedural requirements in existing § 951.14, leaving these decisions to the discretion of the Finance Board in the event an application is received from a Bank for a temporary suspension of its required annual AHP contribution. See 12 CFR 951.14. In addition, certain of the information required to be provided by the Banks is readily obtainable by the Finance Board without the necessity of a regulatory requirement.

*L. Affordable Housing Reserve Fund: Proposed § 951.12*

Proposed § 951.12 would remove the requirements in existing § 951.15 that a Bank report by January 15th of each year the amount of any unused and uncommitted AHP funds from the prior year that will be deposited in an Affordable Housing Reserve Fund (Reserve Fund), and that the Finance Board notify the Banks of the total amount of funds, if any, available in the Reserve Fund. See 12 CFR 951.15. The amount of any unused and uncommitted AHP funds is readily obtainable by the Finance Board without imposing such a regulatory mandate. Moreover, the Finance Board has never had to establish a Reserve Fund and does not expect to in the future, given the high demand for AHP funds that has always exceeded the amount of AHP funds available.

**III. Paperwork Reduction Act**

The information collection contained in the current AHP regulation, entitled "Affordable Housing Program (AHP)," has been assigned control number 3069-0006 by the Office of Management and Budget (OMB). The OMB control number is due to expire on July 31, 2007. This proposed rule, if adopted as a final rule, will not substantively or

materially modify the approved information collection. Consequently, the Finance Board has not submitted any information to OMB for review under the Paperwork Reduction Act of 1995 (PRA).<sup>3</sup>

#### IV. Regulatory Flexibility Act

The proposed rule, if adopted as a final rule, will apply only to the Banks, which do not come within the meaning of "small entities," as defined in the Regulatory Flexibility Act (RFA). See 5 U.S.C. 601(6). Therefore, in accordance with section 605(b) of the RFA, 5 U.S.C. 605(b), the Finance Board hereby certifies that the proposed rule, if promulgated as a final rule, will not have a significant economic impact on a substantial number of small entities.

#### List of Subjects in 12 CFR Part 951

Community development, Credit, Federal home loan banks, Housing, Reporting and recordkeeping requirements.

For the reasons stated in the preamble, the Finance Board proposes to revise 12 CFR, chapter IX, part 951, to read as follows:

#### PART 951—AFFORDABLE HOUSING PROGRAM

- Sec.
- 951.1 Definitions.
  - 951.2 Required annual AHP contributions; allocation of contributions.
  - 951.3 AHP implementation plan.
  - 951.4 Advisory Councils.
  - 951.5 Competitive application program.
  - 951.6 Homeownership set-aside programs.
  - 951.7 Monitoring.
  - 951.8 Remedial actions for noncompliance.
  - 951.9 Agreements.
  - 951.10 Conflicts of interest.
  - 951.11 Temporary suspension of AHP contributions.
  - 951.12 Affordable Housing Reserve Fund.

**Authority:** 12 U.S.C. 1430(j).

##### § 951.1 Definitions.

As used in this part:

*Affordable* means that:

(1) The rent charged to a household for a unit that is to be reserved for occupancy by a household with an income at or below 80 percent of the median income for the area, does not exceed 30 percent of the income of a household of the maximum income and size expected, under the commitment made in the AHP application, to occupy the unit (assuming occupancy of 1.5 persons per bedroom or 1.0 persons per unit without a separate bedroom); or

(2) The rent charged to a household, for rental units subsidized with Section 8 assistance under 42 U.S.C. 1437f, if the rent complied with this § 951.1 at the time of the household's initial occupancy and continues to comply with the Section 8 agreement for that household.

*AHP project* means a single-family or multifamily housing project for owner-occupied or rental housing that has been awarded or has received AHP subsidy under the competitive application program.

*Competitive application program* means a program established by a Bank under which the Bank awards and disburses AHP subsidy through a competitive application scoring process pursuant to the requirements of § 951.5.

*Cost of funds* means, for purposes of a subsidized advance, the estimated cost of issuing Bank System consolidated obligations with maturities comparable to that of the subsidized advance.

*Direct subsidy* means an AHP subsidy in the form of a direct cash payment.

*Eligible household* means a household that meets the income limits and other requirements specified by a Bank for its competitive application program and homeownership set-aside programs, provided that:

(1) In the case of owner-occupied housing, the household's income may not exceed 80 percent of the median income for the area; and

(2) In the case of rental housing, the household's income in at least 20 percent of the units may not exceed 50 percent of the median income for the area.

*Eligible project* means a project eligible to receive AHP subsidy pursuant to the requirements of this part.

*Family member* means any individual related to a person by blood, marriage, or adoption.

*Funding period* means a time period, as determined by a Bank, during which the Bank accepts AHP applications for subsidy.

*Homeownership set aside program* means a program established by a Bank under which the Bank disburses AHP direct subsidy pursuant to the requirements of § 951.6.

*Household* means one or more persons living in a dwelling unit.

*Loan pool* means a group of mortgage or other loans meeting the requirements of this part that are purchased, held in trust, and pledged as security for a financial instrument.

*Low- or moderate-income household* means a household that has an income of 80 percent or less of the median income for the area, with the income

limit adjusted for household size in accordance with the methodology of the applicable median income standard, unless such median income standard has no household size adjustment methodology.

*Low- or moderate-income neighborhood* means any neighborhood in which 51 percent or more of the households have incomes at or below 80 percent of the median income for the area.

*Median income for the area* means one or more of the following median income standards as determined by a Bank, after consultation with its Advisory Council, in its AHP implementation plan:

(1) The median income for the area, as published annually by HUD;

(2) The median income for the area obtained from the Federal Financial Institutions Examination Council;

(3) The applicable median family income, as determined under 26 U.S.C. 143(f) (Mortgage Revenue Bonds) and published by a state agency or instrumentality;

(4) The median income for the area, as published by the United States Department of Agriculture; or

(5) The median income for an applicable definable geographic area, as published by a federal, state, or local government entity, and approved by the Finance Board, at the request of a Bank, for use under the AHP.

*Multifamily building* means a structure with five or more dwelling units.

*Net earnings of a Bank* means the net earnings of a Bank for a calendar year after deducting the Bank's annual contribution to the Resolution Funding Corporation required under section 21B of the Act (12 U.S.C. 1441b), and before declaring or paying any dividend under section 16 of the Act (12 U.S.C. 1436). For purposes of this part, "dividend" includes any dividends on capital stock subject to a redemption request even if under GAAP, those dividends are treated as an "interest expense."

*Owner-occupied project* means, for purposes of the competitive application program, one or more owner-occupied units in a single-family or multifamily building, including condominiums, cooperative housing, and manufactured housing.

*Owner-occupied unit* means a dwelling unit occupied by the owner of the unit. Housing with two to four dwelling units consisting of one owner-occupied unit and one or more rental units is considered a single owner-occupied unit.

<sup>3</sup> See 44 U.S.C. 3501 *et seq.* This proposed rule does not incorporate the proposed changes to AHP data reporting discussed in detail in the PRA notice published in April 2005. See 70 FR 21411 (Apr. 26, 2005).

*Program* means the Affordable Housing Program established pursuant to this part.

*Rental project* means, for purposes of the competitive application program, one or more dwelling units for occupancy by tenants or households that are not owner-occupants, including overnight and emergency shelters, transitional housing for homeless households, mutual housing, and single-room occupancy housing.

*Retention period* means the following period of time during which AHP-assisted owner-occupied units or rental projects must meet the applicable income targeting and rent commitments in the approved AHP application for subsidy:

(1) Five years from closing for an AHP-assisted owner-occupied unit, or in the case of rehabilitation of a unit currently occupied by the owner where there is no closing, 5 years from the date of completion of the rehabilitation; and

(2) Fifteen years from the date of project completion for a rental project.

*Revolving loan fund* means a capital fund established to make mortgage or other loans meeting the requirements of this part whereby loan principal is repaid into the fund and re-lent to other borrowers.

*Single-family building* means a structure with one to four dwelling units.

*Sponsor* means a not-for-profit or for-profit organization or public entity that:

(1) Has an ownership interest (including any partnership interest), as defined by the Bank in its AHP implementation plan, in a rental project;

(2) Is integrally involved, as defined by the Bank in its AHP implementation plan, in an owner-occupied project, such as by exercising control over the planning, development, or management of the project, or by qualifying borrowers and providing or arranging financing for the owners of the units;

(3) Establishes a loan pool; or

(4) Is a revolving loan fund.

*Subsidized advance* means an advance to a member at an interest rate reduced below the Bank's cost of funds, by use of a subsidy.

*Subsidy* means:

(1) A direct subsidy, provided that if a direct subsidy is used to write down the interest rate on a loan extended by a member, sponsor, or other party to a project, the subsidy must equal the net present value of the interest foregone from making the loan below the lender's market interest rate; or

(2) The net present value of the interest revenue foregone from making a subsidized advance at a rate below the Bank's cost of funds.

*Very low-income household* means a household that has an income at or below 50 percent of the median income for the area, with the income limit adjusted for household size in accordance with the methodology of the applicable median income standard, unless such median income standard has no household size adjustment methodology.

*Visitable* means, in either owner-occupied or rental housing, at least one entrance is at-grade (no steps) and approached by an accessible route such as a sidewalk, and the entrance door and all interior passage doors are at least 2 feet, 10 inches wide, offering 32 inches of clear passage space.

#### **§ 951.2 Required annual AHP contributions; allocation of contributions.**

(a) *Annual AHP contributions.* Each Bank shall contribute annually to its Program the greater of:

(1) 10 percent of the Bank's net earnings for the previous year; or

(2) That Bank's pro rata share of an aggregate of \$100 million to be contributed in total by the Banks, such proration being made on the basis of the net earnings of the Banks for the previous year, except that the required annual AHP contribution for a Bank shall not exceed its net earnings in the previous year.

(b) *Allocation of contributions.* Each Bank, after consultation with its Advisory Council and pursuant to written policies adopted by the Bank's board of directors, shall allocate its annual required AHP contribution as follows:

(1) *Competitive application program.* Each Bank shall allocate annually that portion of its annual required AHP contribution that is not set aside to fund homeownership set-aside programs under paragraph (b)(2) of this section, to provide funds to members through a competitive application program, pursuant to the requirements of this part.

(2) *Homeownership set-aside programs.* (i) *Allocation amount; first-time homebuyers.* A Bank, at its discretion, may set aside annually, in the aggregate, up to the greater of \$4.5 million or 35 percent of the Bank's annual required AHP contribution to provide funds to members participating in homeownership set-aside programs established by the Bank, provided that at least one-third of the Bank's aggregate annual set-aside allocation to such programs shall be to assist first-time homebuyers, pursuant to the requirements of this part. A Bank may establish one or more homeownership set-aside programs pursuant to written

policies adopted by the Bank's board of directors.

(ii) *No delegation.* A Bank's board of directors shall not delegate to Bank officers or other Bank employees the responsibility for adopting its homeownership set-aside program policies.

#### **§ 951.3 AHP implementation plan.**

(a) *Adoption; no delegation.* Each Bank, after consultation with its Advisory Council, shall adopt a written AHP implementation plan, and shall not amend the plan without first consulting its Advisory Council. The Bank's board of directors shall not delegate to Bank officers or other Bank employees the responsibility to consult with the Advisory Council prior to adopting or amending the AHP implementation plan. The AHP implementation plan shall set forth, at a minimum:

(1) The applicable median income standard or standards adopted by the Bank consistent with the definition of median income for the area in § 951.1;

(2) The Bank's requirements for its competitive application program established pursuant to § 951.5, including the schedule for AHP funding periods, definition of sponsor, project cost, and feasibility guidelines, any additional optional District eligibility requirements, scoring guidelines, and related definitions, requirements for timely use of AHP subsidies, and requirements for determining compliance upon disbursement of AHP subsidies;

(3) The Bank's requirements for any homeownership set-aside programs established by the Bank pursuant to § 951.6, including eligibility requirements and priority criteria and related definitions, AHP funding requirements, and requirements for timely use of the AHP subsidy;

(4) The Bank's requirements for funding revolving loan funds, if adopted by the Bank pursuant to § 951.5(c)(13);

(5) The Bank's requirements for funding loan pools, if adopted by the Bank pursuant to § 951.5(c)(14);

(6) The Bank's requirements for monitoring under its competitive application program and any Bank homeownership set-aside programs, adopted pursuant to § 951.7;

(7) The Bank's requirements, including time limits, for re-use of repaid AHP direct subsidy, if adopted by the Bank pursuant to § 951.8(f)(2); and

(8) Retention agreement requirements for projects and households under the competitive application program and any Bank homeownership set-aside

programs, pursuant to § 951.9(a)(7) and (a)(8).

(b) *Advisory Council review.* Prior to the adoption or amendment of a Bank's AHP implementation plan, the Bank shall provide its Advisory Council an opportunity to review the document, and the Advisory Council shall provide its recommendations to the Bank's board of directors.

(c) *Notification of plan amendments to the Finance Board.* A Bank shall notify the Finance Board of any amendments made to its AHP implementation plan within 30 days after the date of their adoption by the Bank's board of directors.

(d) *Public access.* A Bank shall publish its current AHP implementation plan on a publicly available website, and shall publish any amendments to the plan on the website within 30 days after the date of their adoption by the Bank's board of directors.

#### § 951.4 Advisory Councils.

(a) *Appointment.* (1) Each Bank's board of directors shall appoint an Advisory Council of from 7 to 15 persons who reside in the Bank's District and are drawn from community and not-for-profit organizations that are actively involved in providing or promoting low- and moderate-income housing, and community and not-for-profit organizations that are actively involved in providing or promoting community lending, in the District.

(2) Each Bank shall solicit nominations for membership on the Advisory Council from community and not-for-profit organizations pursuant to a nomination process that is as broad and as participatory as possible, allowing sufficient time for responses.

(3) The Bank's board of directors shall appoint Advisory Council members from a diverse range of organizations so that representatives of no one group shall constitute an undue proportion of the membership of the Advisory Council, giving consideration to the size of the Bank's District and the diversity of low- and moderate-income housing and community lending needs and activities within the District.

(b) *Terms of Advisory Council members.* Pursuant to policies adopted by the Bank's board of directors, Advisory Council members shall be appointed by the Bank's board of directors to serve for terms of up to 3 years, and such terms shall be staggered to provide continuity in experience and service to the Advisory Council. No Advisory Council member may be appointed to serve for more than three full consecutive terms. An Advisory Council member appointed to fill a

vacancy shall be appointed for the unexpired term of his or her predecessor in office.

(c) *Election of officers.* Each Advisory Council shall elect from among its members a chairperson, a vice chairperson, and any other officers the Advisory Council deems appropriate.

(d) *Duties.* (1) *Meetings with the Banks.* (i) The Advisory Council shall meet with representatives of the Bank's board of directors at least quarterly to provide advice on ways in which the Bank can better carry out its housing finance and community lending mission, including, but not limited to, advice on the low- and moderate-income housing and community lending programs and needs in the Bank's District, and on the use of AHP subsidies, Bank advances, and other Bank credit products for these purposes.

(ii) The Advisory Council's advice shall include recommendations on:

(A) The amount of AHP subsidies to be allocated to the Bank's competitive application program and any Bank homeownership set-aside programs;

(B) The AHP implementation plan and any subsequent amendments thereto;

(C) The scoring criteria, related definitions, and any additional optional District eligibility requirements for the competitive application program; and

(D) The eligibility requirements and any priority criteria for any Bank homeownership set-aside programs.

(2) *Summary of AHP applications.* The Bank shall comply with requests from the Advisory Council for summary information regarding AHP applications from prior funding periods.

(3) *Annual analysis; public access.* (i) Each Advisory Council shall submit to the Finance Board annually by May 1 its analysis of the low- and moderate-income housing and community lending activity of the Bank by which it is appointed.

(ii) Within 30 days after the date the Advisory Council's annual analysis is submitted to the Finance Board, the Bank shall publish the analysis on a publicly available website.

(e) *Expenses.* The Bank shall pay Advisory Council members' travel expenses, including transportation and subsistence, for each day devoted to attending meetings with representatives of the board of directors of the Bank and meetings requested by the Finance Board.

(f) *No delegation.* A Bank's board of directors shall not delegate to Bank officers or other Bank employees the responsibility to appoint persons as members of the Advisory Council or to

meet with the Advisory Council at least quarterly.

#### § 951.5 Competitive application program.

(a) *Establishment of program.* A Bank shall establish a competitive application program pursuant to the requirements of this part.

(b) *Funding periods and application process.* (1) *Funding periods.* A Bank may accept applications for AHP subsidy under its competitive application program during a specified number of funding periods each year, as determined by the Bank.

(2) *Eligible applicants.* A Bank shall accept applications for AHP subsidy under its competitive application program only from institutions that are members of the Bank at the time the application is submitted to the Bank.

(3) *Submission of applications.* A Bank shall require applications for AHP subsidy to contain information sufficient for the Bank to:

(i) Determine that the proposed AHP project meets the eligibility requirements of paragraph (c) of this section; and

(ii) Evaluate the application pursuant to the scoring guidelines adopted by the Bank pursuant to paragraph (d) of this section.

(4) *Review of applications submitted.* A Bank shall review the applications for AHP subsidy to determine that the proposed AHP project meets the eligibility requirements of paragraph (c) of this section, and shall evaluate the applications pursuant to the Bank's scoring guidelines adopted pursuant to paragraph (d) of this section.

(c) *Minimum eligibility requirements.* Projects receiving AHP subsidies pursuant to a Bank's competitive application program must meet the following eligibility requirements:

(1) *Owner-occupied or rental housing.* The AHP subsidy shall be used exclusively for:

(i) *Owner-occupied housing.* The purchase, construction, or rehabilitation of an owner-occupied project by or for very low-income or low- or moderate-income households. A household must have an income meeting the income targeting commitments in the approved AHP application at the time it is qualified by the project sponsor for participation in the project; or

(ii) *Rental housing.* The purchase, construction, or rehabilitation of a rental project, where at least 20 percent of the units in the project are occupied by and affordable for very low-income households. A household must have an income meeting the income targeting commitments in the approved AHP application upon initial occupancy of



the rental unit, or for projects involving the purchase or rehabilitation of rental housing that already is occupied, at the time the application for AHP subsidy is submitted to the Bank for approval.

(2) *Need for subsidy.* The project's estimated cash uses of funds shall equal its estimated cash sources of funds as reflected in the project's development budget. A project's cash sources of funds shall include estimates of funds the project sponsor intends to obtain from other sources but which have not yet been committed to the project.

(3) *Project costs.* (i) *In general.* Project costs, as reflected in the project's development budget, must be reasonable, in accordance with the Bank's project cost guidelines, taking into consideration the geographic location of the project, development conditions, and other non-financial household or project characteristics.

(ii) *Cost of property and services provided by a member.* The purchase price of property or services, as reflected in the project's development budget, sold to the project by a member providing AHP subsidy to the project, or, in the case of property, upon which such member holds a mortgage or lien, may not exceed the market value of such property or services as of the date the purchase price was agreed upon. In the case of real estate owned property sold to a project by a member providing AHP subsidy to the project, or property sold to the project upon which the member holds a mortgage or lien, the market value of such property is deemed to be the "as-is" or "as-rehabilitated" value of the property, whichever is appropriate. That value shall be reflected in an independent appraisal of the property performed by a state certified or licensed appraiser, as defined in 12 CFR 564.2(j) and (k), within 6 months prior to the date the Bank disburses AHP subsidy to the project.

(4) *Project feasibility.* (i) *Developmental feasibility.* The project must be likely to be completed and occupied, based on relevant factors contained in the Bank's project feasibility guidelines, including, but not limited to, the development budget, market analysis, and project sponsor's experience in providing the requested assistance to households.

(ii) *Operational feasibility of rental projects.* A rental project must be able to operate in a financially sound manner, in accordance with the Bank's project feasibility guidelines, as projected in the project's operating pro forma or similar statement of operational feasibility.

(5) *Financing costs.* The rate of interest, points, fees, and any other charges for all loans financing the project shall not exceed a reasonable market rate of interest, points, fees, and other charges for loans of similar maturity, terms, and risk.

(6) *Timing of AHP subsidy use.* The AHP subsidy must be likely to be drawn down by the project or used by the project to procure other financing commitments within 12 months of the date of approval of the application for AHP subsidy funding the project.

(7) *Counseling costs.* AHP subsidies may be used to pay for counseling costs only where:

(i) Such costs are incurred in connection with counseling of homebuyers who actually purchase an AHP-assisted unit; and

(ii) The cost of the counseling has not been covered by another funding source, including the member.

(8) *Refinancing.* The project may use AHP subsidies to refinance an existing single-family or multifamily mortgage loan, provided that the refinancing produces equity proceeds and such equity proceeds up to the amount of the AHP subsidy in the project shall be used only for the purchase, construction, or rehabilitation of housing units meeting the eligibility requirements of this paragraph (c).

(9) *Retention.* The AHP-assisted projects are, or are committed to be, subject to retention agreements as follows:

(i) *Owner-occupied projects.* Each AHP-assisted unit in an owner-occupied project is, or is committed to be, subject to a 5-year retention agreement described in § 951.9(a)(7).

(ii) *Rental projects.* AHP-assisted rental projects are, or are committed to be, subject to a 15-year retention agreement described in § 951.9(a)(8).

(10) *Project sponsor qualifications.* (i) *In general.* A project's sponsor must be qualified and able to perform its responsibilities as committed to in the application for AHP subsidy funding the project.

(ii) *Revolving loan fund.* Pursuant to written policies adopted by a Bank's board of directors, a project sponsor that is a revolving loan fund shall:

(A) Provide evidence of sound business practices and fiscal sustainability;

(B) Provide audited statements or equivalent evidence that its operations are consistent with acceptable business practices; and

(C) Demonstrate the ability to revolve subsidy repayments on a timely basis and track the use of the AHP subsidy.

(iii) *Loan pool.* Pursuant to written policies adopted by a Bank's board of directors, a project sponsor that establishes a loan pool shall:

(A) Provide evidence of sound asset/liability management practices and fiscal sustainability;

(B) Provide audited statements or equivalent evidence that its operations are consistent with acceptable business practices; and

(C) Demonstrate the ability to track the use of the AHP subsidy.

(11) *Fair housing.* The project, as proposed, must comply with applicable federal and state laws on fair housing and housing accessibility, including, but not limited to, the Fair Housing Act, the Rehabilitation Act of 1973, the Americans with Disabilities Act of 1990, and the Architectural Barriers Act of 1969, and must demonstrate how the project will be affirmatively marketed.

(12) *Calculation of AHP subsidy.* (i) Where an AHP direct subsidy is provided to a project to write down the interest rate on a loan extended by a member, sponsor, or other party to a project, the net present value of the interest foregone from making the loan below the lender's market interest rate shall be calculated as of the date the application for AHP subsidy is submitted to the Bank, and subject to adjustment under paragraph (g)(4) of this section.

(ii) Where an AHP subsidized advance is provided to a project, the net present value of the interest revenue foregone from making a subsidized advance at a rate below the Bank's cost of funds shall be determined as of the earlier of the date of disbursement of the subsidized advance or the date prior to disbursement on which the Bank first manages the funding to support the subsidized advance through its asset/liability management system, or otherwise.

(13) *Use of AHP subsidy by revolving loan funds.* Pursuant to written policies adopted by a Bank's board of directors after consultation with its Advisory Council, a Bank, in its discretion, may provide AHP subsidies to members for lending by revolving loan funds to eligible projects and households under a Bank's competitive application program, provided the following requirements are met:

(i) *Initial use of subsidy.* (A) The revolving loan fund's initial lending of the AHP subsidy shall meet all applicable eligibility requirements under this paragraph (c).

(B) The revolving loan fund's initial lending of the AHP subsidy shall be to projects and households meeting the commitments in the approved

application for AHP subsidy, and the income eligibility and affordability commitments in such application shall be met for the full AHP retention period.

(ii) *Revolving uses of repaid subsidy.*

(A) The revolving loan fund's subsequent lending of repaid AHP subsidy shall meet all applicable eligibility requirements under this paragraph (c).

(B) The revolving loan fund's subsequent lending of repaid AHP subsidy shall be for low- or moderate-income households in the case of owner-occupied projects, or for rental projects where at least 20 percent of the units are occupied by and affordable for very low-income households, subject to retention period, monitoring and recapture requirements that the Bank shall adopt.

(iii) The revolving loan fund shall return to the Bank any repaid AHP subsidy that will not be used according to the requirements in this paragraph (c)(13).

(14) *Use of AHP subsidy in loan pools.* Pursuant to written policies adopted by a Bank's board of directors after consultation with its Advisory Council, a Bank, at its discretion, may provide AHP subsidies to members for projects involving the purchase of eligible AHP-assisted loans to AHP-eligible households for inclusion in a loan pool under a Bank's competitive application program, provided the following requirements are met:

(i) *Eligibility requirements.* The loan pool's use of the AHP subsidies shall meet all applicable eligibility requirements under this paragraph (c)(14), and shall not be for the sole purpose of providing liquidity to the originator or holder of the loans. The loan pool sponsor must provide to the Bank proposed loan acceptance standards for the pool, the number of eligible households and income levels of loans served in a given time period, and the sponsor must make available to the Bank for its review and approval the underwriting characteristics of loans that the loan pool will purchase.

(ii) *Forward commitment.* (A) The loan pool sponsor shall purchase the loans pursuant to a forward commitment that identifies the loans to be originated with principal or interest rate reductions as specified in the approved AHP applications to the targeted low- or moderate-income households. Both initial purchases of loans for the AHP loan pool and subsequent purchases of loans to substitute for repaid loans in the pool shall be made pursuant to the terms of such forward commitment and subject to time limits on the use of the AHP

subsidy as specified by the Bank in its AHP implementation plan under § 951.3(a)(2) and the Bank's agreement with the loan pool sponsor.

(B) In the alternative, the loan pool shall purchase an initial round of loans that are not purchased pursuant to a forward commitment, provided that the originator or holder of the loans is required to use the proceeds from the initial loan purchases within time limits on use of the AHP subsidy as specified by the Bank in its AHP implementation plan under § 951.3(a)(2) and the Bank's agreement with the loan pool sponsor. The proceeds shall assist households that are income-eligible under the approved AHP applications for subsidy during subsequent rounds of lending, and such assistance shall be provided in the form of a principal reduction or a below-market AHP-subsidized interest rate as specified in the approved AHP application.

(iii) Each AHP-assisted owner-occupied unit receiving AHP direct subsidy shall be subject to an AHP 5-year retention agreement as required under paragraph (c)(9)(i) of this section.

(iv) Where AHP direct subsidy is being used in connection with the purchase of a loan or loans from a member or other party, the loan pool sponsor shall use the AHP direct subsidy for a standard upfront buy-down of the interest rate on such loan or loans, or a reduction in the principal of the loans.

(15) *Optional District eligibility requirements.* A Bank may require a project receiving AHP subsidies to meet one or more of the following additional eligibility requirements adopted by the Bank's board of directors after consultation with its Advisory Council:

(i) *AHP subsidy limits.* A requirement that the amount of AHP subsidy requested for the project does not exceed limits established by the Bank as to the maximum amount of AHP subsidy available per member each year, or per member, per project, or per project unit in a single funding period.

(ii) *Counseling.* A requirement that a household must complete a homebuyer or homeowner counseling program provided by, or based on one provided by, an organization recognized as experienced in homebuyer or homeowner counseling, respectively.

(16) *Prohibited uses of AHP subsidies.* The project shall not use AHP subsidies to pay for:

(i) *Prepayment fees.* Prepayment fees imposed by a Bank on a member for a subsidized advance that is prepaid.

(ii) *Cancellation fees.* Cancellation fees and penalties imposed by a Bank on

a member for a subsidized advance commitment that is canceled.

(iii) *Processing fees.* Processing fees charged by members for providing direct subsidies to a project.

(17) *Prohibited eligibility requirement for in-District projects.* A Bank shall not establish a requirement that a project be located in the Bank's District.

(d) *Scoring of applications.* (1) *In general.* A Bank shall adopt written scoring guidelines setting forth the Bank's AHP competitive application program scoring criteria and related definitions and point allocations, and implementing other applicable requirements pursuant to this paragraph (d). A Bank shall not adopt additional scoring criteria or point allocations, except as specifically authorized under this paragraph (d).

(2) *Point allocations.* (i) A Bank shall allocate 100 points among the 9 scoring criteria identified in paragraph (d)(5) of this section.

(ii) The scoring criterion for targeting identified in paragraph (d)(5)(iii) of this section shall be allocated at least 20 points.

(iii) The remaining scoring criteria shall be allocated at least five points each.

(3) *Fixed point and variable point scoring criteria.* A Bank shall designate each scoring criterion as either a fixed-point or a variable-point criterion, defined as follows:

(i) Fixed-point scoring criteria are those which cannot be satisfied in varying degrees and are either satisfied or not, with the total number of points allocated to the criterion awarded by the Bank to an application meeting the criterion.

(ii) Variable-point criteria are those where there are varying degrees to which an application can satisfy the criteria, with the number of points that may be awarded to an application for meeting the criterion varying, depending on the extent to which the application satisfies the criterion, based on a fixed scale or on a scale relative to the other applications being scored. A Bank shall designate the targeting and subsidy-per-unit scoring criteria identified in paragraphs (d)(5)(iii) and (d)(5)(viii), respectively, of this section, as variable-point criteria.

(4) *Satisfaction of scoring criteria.* A Bank shall award scoring points to applications for proposed projects based on satisfaction of the scoring criteria adopted by the Bank pursuant to paragraph (d)(5) of this section.

(5) *Scoring criteria.* An application for a proposed project may receive scoring points based on satisfaction of the following nine scoring criteria:

(i) *Use of donated or conveyed government-owned or other properties.* The financing of housing using a significant proportion of:

(A) Land or units donated or conveyed by the federal government or any agency or instrumentality thereof; or

(B) Land or units donated or conveyed by any other party for an amount significantly below the fair market value of the property, as defined by the Bank in its AHP implementation plan.

(ii) *Sponsorship by a not-for-profit organization or government entity.* Project sponsorship by a not-for-profit organization, a state or political subdivision of a state, a state housing agency, a local housing authority, a Native American Tribe, an Alaskan Native Village, or the government entity for Native Hawaiian Home Lands.

(iii) *Targeting.* The extent to which a project provides housing for very low- and low- or moderate-income households, as follows:

(A) *Rental projects.* An application for a rental project shall be awarded the maximum number of points available under this scoring criterion if 60 percent or more of the units in the project are reserved for occupancy by households with incomes at or below 50 percent of the median income for the area. Applications for projects with less than 60 percent of the units reserved for occupancy by households with incomes at or below 50 percent of the median income for the area shall be awarded points on a declining scale based on the percentage of units in a project that are reserved for households with incomes at or below 50 percent of the median income for the area, and on the percentage of the remaining units reserved for households with incomes at or below 80 percent of the median income for the area.

(B) *Owner-occupied projects.* Applications for owner-occupied projects shall be awarded points based on a declining scale to be determined by the Bank in its AHP implementation plan, taking into consideration percentages of units and targeted income levels.

(C) *Separate scoring.* For purposes of this scoring criterion, applications for owner-occupied projects and rental projects may be scored separately.

(iv) *Housing for homeless households.* The financing of rental housing, excluding overnight shelters, reserving at least 20 percent of the units for homeless households, the creation of transitional housing for homeless households permitting a minimum of 6 months occupancy, or the creation of permanent owner-occupied housing

reserving at least 20 percent of the units for homeless households, with the term "homeless households" as defined by the Bank in its AHP implementation plan.

(v) *Promotion of empowerment.* The provision of housing in combination with a program offering employment; education; training; homebuyer, homeownership, or tenant counseling; daycare services; resident involvement in decision making affecting the creation or operation of the project; or other services that assist residents to move toward better economic opportunities, such as welfare to work initiatives.

(vi) *First District priority.* The satisfaction of one of the following criteria, or one of a number of the following criteria, as recommended by the Bank's Advisory Council and adopted by the Bank's board of directors and set forth in the Bank's AHP implementation plan, as long as the total points available for meeting the criterion or criteria adopted under this category do not exceed the total points allocated to this category:

(A) *Special needs.* The financing of housing in which at least 20 percent of the units are reserved for occupancy by households with special needs, such as the elderly, mentally or physically disabled persons, persons recovering from physical abuse or alcohol or drug abuse, or persons with AIDS; or the financing of housing that is visitable by persons with physical disabilities who are not occupants of such housing.

(B) *Community development.* The financing of housing meeting housing needs documented as part of a community revitalization or economic development strategy approved by a unit of a state or local government.

(C) *First-time homebuyers.* The financing of housing for first-time homebuyers.

(D) *Member financial participation.* Member financial participation (excluding the pass-through of AHP subsidy) in the project, such as providing market rate or concessionary financing, fee waivers, or donations.

(E) *Disaster areas and displaced households.* The financing of housing located in federally declared disaster areas, or for households displaced from federally declared disaster areas due to a disaster.

(F) *Rural.* The financing of housing located in rural areas.

(G) *Urban.* The financing of urban in-fill or urban rehabilitation housing.

(H) *Economic diversity.* The financing of housing that is part of a strategy to end isolation of very low-income households by providing economic

diversity through mixed-income housing in low- or moderate-income neighborhoods, or providing very low- or low- or moderate-income households with housing opportunities in neighborhoods or cities where the median income equals or exceeds the median income for the larger surrounding area, such as the city, county, or Primary Metropolitan Statistical Area, in which the neighborhood or city is located.

(I) *Fair housing remedy.* The financing of housing as part of a remedy undertaken by a jurisdiction adjudicated by a federal, state, or local court to be in violation of title VI of the Civil Rights Act of 1964 (42 U.S.C. 2000d *et seq.*), the Fair Housing Act (42 U.S.C. 3601 *et seq.*), or any other federal, state, or local fair housing law, or as part of a settlement of such claims.

(J) *Community involvement.* Demonstrated support for the project by local government, other than as a project sponsor, in the form of property tax deferral or abatement, zoning changes or variances, infrastructure improvements, fee waivers, or other similar forms of non-cash assistance, or demonstrated support for the project by community organizations or individuals, other than as project sponsors, through the commitment by such entities or individuals of donated goods and services, or volunteer labor.

(K) *Lender consortia.* The involvement of financing by a consortium of at least two financial institutions.

(vii) *Second District priority: defined housing need in the District.* The satisfaction of a housing need in the Bank's District, as defined and recommended by the Bank's Advisory Council and adopted by the Bank's board of directors. The Bank may, but is not required to, use one of the criteria listed in paragraph (d)(5)(vi) of this section, provided it is different from the criterion or criteria adopted by the Bank under such paragraph. The Bank may not adopt as its scoring criterion under this paragraph (d)(5)(vii) the financing of housing located in the Bank's District.

(viii) *AHP subsidy per unit.* (A) *Amount of subsidy.* The extent to which a project proposes to use the least amount of AHP subsidy per AHP-targeted unit. In the case of an application for a project financed by a subsidized advance, the total amount of AHP subsidy used by the project shall be estimated based on the Bank's cost of funds as of the date on which all applications are due for the funding period in which the application is submitted.

(B) *Separate scoring.* For purposes of this scoring criterion, applications for owner-occupied projects and rental projects may be scored separately.

(ix) *Community stability.* The promotion of community stability, such as by rehabilitating vacant or abandoned properties, being an integral part of a neighborhood stabilization plan approved by a unit of state or local government, and not displacing low- or moderate-income households, or if such displacement will occur, assuring that such households will be assisted to minimize the impact of such displacement.

(e) *Approval of AHP applications.* (1) A Bank shall approve applications for AHP subsidy in descending order starting with the highest scoring application until the total funding amount for the particular funding period, except for any amount insufficient to fund the next highest scoring application, has been allocated.

(2) The Bank also shall approve at least the next four highest scoring applications as alternates and, within 1 year of approval, may fund such alternates if any previously committed AHP subsidies become available.

(f) *Modifications of approved AHP applications.* (1) *Modification procedure.* If, prior to or after final disbursement of funds to a project from all funding sources, there is or will be a change in the project that would change the score that the project application received in the funding period in which it was originally scored and approved, had the changed facts been operative at that time, a Bank, in its discretion, may approve in writing a modification to the terms of the approved application, provided that:

(i) The project, incorporating any such changes, would meet the eligibility requirements of paragraph (c) of this section;

(ii) The application, as reflective of such changes, continues to score high enough to have been approved in the funding period in which it was originally scored and approved by the Bank; and

(iii) There is good cause for the modification, and the analysis and justification for the modification are documented by the Bank in writing.

(2) *AHP subsidy increases; no delegation.* Modifications involving an increase in AHP subsidy shall be approved or disapproved by a Bank's board of directors. The authority to approve or disapprove such requests shall not be delegated to Bank officers or other Bank employees.

(g) *Procedure for funding.* (1) *Disbursement of AHP subsidies to*

*members.* (i) A Bank may disburse AHP subsidies only to institutions that are members of the Bank at the time they request a draw-down of the subsidies.

(ii) If an institution with an approved application for AHP subsidy loses its membership in a Bank, the Bank may disburse AHP subsidies to a member of such Bank to which the institution has transferred its obligations under the approved application, or the Bank may disburse AHP subsidies through another Bank to a member of that Bank that has assumed the institution's obligations under the approved AHP application.

(2) *Progress towards use of AHP subsidies.* A Bank shall establish policies and procedures, such as time limits, for determining whether progress is being made towards draw-down and use of AHP subsidies by approved projects, and whether to cancel AHP application approvals for lack of such progress. Pursuant to such policies and procedures, a Bank shall determine whether progress is being made by approved projects, and whether to cancel any AHP application approvals. If a Bank cancels any AHP application approvals, it shall make the AHP subsidies available for other AHP-eligible projects.

(3) *Compliance upon disbursement of AHP subsidies.* A Bank shall establish policies and procedures for determining, prior to its initial disbursement of AHP subsidies for an approved project, and prior to subsequent disbursement if the need for AHP subsidy has changed, that the project meets the eligibility requirements of paragraph (c) of this section and all obligations committed to in the approved AHP application.

(4) *Changes in approved AHP subsidy amount where a direct subsidy is used to write down prior to closing the principal amount or interest rate on a loan.* If a member is approved to receive AHP direct subsidy to write down prior to closing the principal amount or the interest rate on a loan to a project and the amount of AHP subsidy required to maintain the debt service cost for the loan decreases from the amount of AHP subsidy initially approved by the Bank due to a decrease in market interest rates between the time of approval and the time the lender commits to the interest rate to finance the project, the Bank shall reduce the AHP subsidy amount accordingly. If market interest rates rise between the time of approval and the time the lender commits to the interest rate to finance the project, the Bank, in its discretion, may increase the AHP subsidy amount accordingly.

(5) *AHP outlay adjustment.* If a Bank reduces the amount of AHP subsidy

approved for a project, the amount of such reduction shall be returned to the Bank's AHP fund. If a Bank increases the amount of AHP subsidy approved for a project, the amount of such increase shall be drawn first from any currently uncommitted or repaid AHP subsidies and then from the Bank's required AHP contribution for the next year.

(6) *Project sponsor notification of re-use of repaid AHP direct subsidy.* Prior to disbursement by a project sponsor of AHP direct subsidy repaid to and retained by such project sponsor pursuant to a subsidy re-use program authorized by the Bank under § 951.8(f)(2), the project sponsor shall provide written notice to the member and the Bank of its intent to disburse the repaid AHP subsidy to a household satisfying the requirements of this part and the commitments in the approved AHP application.

(h) *Bank board duties and delegation.* (1) *Duties.* A Bank's board of directors, after consultation with its Advisory Council, shall be responsible for:

(i) The establishment of any optional District eligibility requirements;

(ii) The establishment of any policies and procedures for use of AHP subsidies by revolving loan funds or loan pools;

(iii) The establishment of scoring criteria and related definitions and point allocations; and

(iv) Approving or disapproving the applications for AHP subsidy.

(2) *No delegation.* The Bank's board of directors shall not delegate to Bank officers or other Bank employees the responsibilities set forth in paragraph (h)(1) of this section.

#### **§ 951.6 Homeownership set-aside programs.**

(a) *Establishment of program.* A Bank may establish one or more homeownership set-aside programs pursuant to the requirements of this part.

(b) *Eligible applicants.* A Bank shall accept applications for AHP direct subsidy under its homeownership set-aside programs only from institutions that are members of the Bank at the time the application is submitted to the Bank.

(c) *Minimum eligibility requirements.* A Bank's homeownership set-aside programs must meet the following eligibility requirements:

(1) *Member allocation criteria.* AHP direct subsidies shall be provided to members pursuant to allocation criteria established by the Bank in its AHP implementation plan.

(2) *Eligible households.* Members shall provide AHP direct subsidies only to households that:

(i) Have incomes at or below 80 percent of the median income for the area at the time the household is accepted for enrollment by the member and the Bank in the Bank's homeownership set-aside program; and

(ii) Meet the first-time homebuyer requirement, in the case of households receiving funds pursuant to the first-time homebuyer requirement in § 951.2(b)(2), and meet such other eligibility criteria that may be established by the Bank in its AHP implementation plan, such as a matching funds requirement, counseling requirement, or criteria that give priority for the purchase or rehabilitation of housing in particular areas or as part of a disaster relief effort.

(3) *Maximum grant amount.* Members shall provide AHP direct subsidies to households as a grant, in an amount up to a maximum of \$15,000 per household, as established by the Bank in its AHP implementation plan, which limit shall apply to all households.

(4) *Eligible uses of AHP direct subsidy.* Households shall use the AHP direct subsidies to pay for down payment, closing cost, counseling, or rehabilitation assistance in connection with the household's purchase or rehabilitation of an owner-occupied unit, including a condominium or cooperative housing unit, to be used as the household's primary residence.

(5) *Retention agreement.* An owner-occupied unit purchased or rehabilitated using AHP direct subsidy shall be subject to a 5-year retention agreement described in § 951.9(a)(7).

(6) *Member financial incentives.* The Bank shall establish incentives for members to provide financial or other assistance in connection with providing the AHP direct subsidy.

(7) *Financing costs.* The rate of interest, points, fees, and any other charges for loans used directly or indirectly in conjunction with the AHP direct subsidy shall not exceed a reasonable market rate of interest, points, fees, and other charges for loans of similar maturity, terms, and risk.

(8) *Counseling costs.* The AHP direct subsidies may be used to pay for counseling costs only where:

(i) Such costs are incurred in connection with counseling of homebuyers who actually purchase an AHP-assisted unit; and

(ii) The cost of the counseling has not been covered by another funding source, including the member.

(9) *Progress towards use of AHP subsidy.* Progress shall be made towards draw-down and use of the AHP direct subsidies by eligible households

pursuant to the requirements in the Bank's policies and procedures.

(10) *No cash back to household.* A member shall not provide cash back to a household at closing on the mortgage loan, and shall use any AHP subsidy beyond what is needed at closing for closing costs and the approved mortgage amount to further reduce the principal of the mortgage loan.

(d) *Approval of AHP applications.* The Bank shall approve applications for AHP direct subsidy in accordance with the Bank's criteria governing the allocation of funds.

(e) *Procedure for funding.* (1) *Disbursement of AHP subsidies to members.* (i) A Bank may disburse AHP direct subsidies only to institutions that are members of the Bank at the time they request a draw-down of the subsidies.

(ii) If an institution with an approved application for AHP direct subsidy loses its membership in a Bank, the Bank may disburse AHP direct subsidies to a member of such Bank to which the institution has transferred its obligations under the approved AHP application, or the Bank may disburse AHP direct subsidies through another Bank to a member of that Bank that has assumed the institution's obligations under the approved AHP application.

(2) *Progress towards use of AHP subsidies.* A Bank shall establish policies and procedures, such as time limits, for determining whether progress is being made towards draw-down and use of the AHP direct subsidies by eligible households, and whether to cancel AHP application approvals for lack of such progress. Pursuant to such policies and procedures, a Bank shall determine whether progress is being made towards such draw-down and use, and whether to cancel any AHP application approvals. If the Bank cancels any AHP application approvals, it shall make the AHP direct subsidies available for other applicants for AHP direct subsidies under the homeownership set-aside program or for other AHP-eligible projects.

#### § 951.7 Monitoring.

(a) *Competitive application program.*

(1) *Initial monitoring policies and procedures.* (i) A Bank shall adopt and implement written policies and procedures for monitoring of owner-occupied and rental projects prior to, and within a reasonable period of time after, project completion to determine, at a minimum, whether:

(A) Construction or rehabilitation of projects that are underway is making satisfactory progress towards completion, in compliance with the

commitments in the approved AHP applications, Bank policies, and the requirements of this part.

(B) Following completion of projects, satisfactory progress is being made towards occupancy of the projects by eligible households.

(C) Within a reasonable period of time after project completion, the projects meet the following requirements, at a minimum:

(1) The AHP subsidy was used for eligible purposes according to the commitments in the approved AHP applications;

(2) The household incomes and rents comply with the income targeting and rent commitments in the approved AHP applications;

(3) The projects' actual costs were reasonable in accordance with the Bank's project cost guidelines, and the AHP subsidies were necessary for the completion of the project as currently structured;

(4) The AHP-assisted units are subject to retention agreements meeting the requirements of § 951.9(a)(7) or (a)(8), as applicable; and

(5) In the case of rental projects, the services and activities committed to in the approved AHP applications have been provided in connection with the projects.

(ii) *Back-up documentation.* A Bank's written monitoring policies and procedures shall include requirements for:

(A) Bank review of back-up project documentation regarding household incomes and rents maintained by the project sponsor or owner; and

(B) Maintenance and Bank review of other project documentation in the Bank's discretion.

(2) *Long-term monitoring policies and procedures.* (i) A Bank shall adopt and implement written policies and procedures for monitoring of approved rental projects commencing in the second year after project completion to determine, at a minimum, whether during the full 15-year retention period, the household incomes, rents, and populations served comply with the income targeting, rent, and targeted population commitments, respectively, in the approved AHP applications.

(ii) *Risk factors and reliance on other monitoring.* (A) *Risk factors.* A Bank's monitoring policies and procedures shall take into account risk factors such as the amount of AHP subsidy in the project, type of project, size of project, location of project, sponsor experience, and any monitoring provided by a federal, state, or local entity as described in this paragraph (a)(2)(ii).

(B) *Reliance on other monitoring.* (1) *Tax credit monitoring.* For AHP projects that are allocated Federal Low-Income Housing Tax Credits (tax credits), a Bank may rely on the monitoring by the state-designated housing credit agency administering the tax credits of the income targeting, rent, and retention period requirements applicable under the Low-Income Housing Tax Credit Program, provided that the compliance profiles of the AHP and the Low-Income Housing Tax Credit program continue to be substantively equivalent.

(2) *Other governmental monitoring.* For AHP projects that receive funds from Federal, State, or local government entities, a Bank may rely on the monitoring by such entities of the income targeting, rent, and retention period requirements applicable under their programs, provided that:

(i) The income targeting, rent, and retention period requirements for those programs are substantively equivalent to those of the AHP;

(ii) The entity has demonstrated and continues to demonstrate its ability to monitor the project;

(3) The entity agrees to provide reports to the Bank on the project's incomes and rents for the full 15-year AHP retention period; and

(4) The Bank reviews the reports from the monitoring entity to confirm that they comply with the Bank's monitoring policies and procedures.

(C) *Risk-based sampling plan.* A Bank may use a reasonable, risk-based sampling plan to select the rental projects to be monitored and to review the back-up and any other project documentation received by the Bank. The risk-based sampling plan and its basis shall be in writing.

(iii) *Annual certifications and back-up documentation.* A Bank's written monitoring policies and procedures shall include requirements for:

(A) Bank review of annual certifications by project owners to the Bank that household incomes and rents are in compliance with the commitments in the approved AHP application and the requirements of this part;

(B) Bank review of back-up project documentation regarding household incomes and rents maintained by the project owner; and

(C) Maintenance and Bank review of other project documentation in the Banks' discretion.

(3) *Annual adjustment of targeting commitments.* For purposes of determining compliance with the targeting commitments in an approved AHP application for both initial and long-term monitoring purposes under a

Bank's competitive application program, such commitments shall be considered to adjust annually according to the current applicable median income data. A rental unit may continue to count toward meeting the targeting commitment of an approved AHP application as long as the rent charged to a household remains affordable, as defined in § 951.1, for the household occupying the unit.

(b) *Homeownership set-aside programs: Monitoring policies and procedures.* (1) A Bank shall adopt and implement written policies and procedures for monitoring compliance with the requirements of its homeownership set-aside programs, including monitoring to determine, at a minimum, whether:

(i) The AHP subsidy was provided to households meeting all applicable eligibility requirements in § 951.6(c)(2) and the Bank's homeownership set-aside program policies; and

(ii) All other applicable eligibility requirements in § 951.6(c) and the Bank's homeownership set-aside program policies are met, including that the AHP-assisted units are subject to retention agreements required under § 951.6(c)(5).

(2) *Sampling plan.* A Bank may use a reasonable sampling plan to select the households to be monitored, and to review the back-up and any other documentation received by the Bank. The sampling plan and its basis shall be in writing.

(3) *Member certifications and back-up documentation.* A Bank's written monitoring policies and procedures shall include requirements for:

(i) Bank review of certifications by members to the Bank, prior to disbursement of the AHP subsidy, that the subsidy will be provided in compliance with all applicable eligibility requirements in § 951.6(c);

(ii) Bank review of back-up documentation regarding household incomes maintained by the member; and

(iii) Maintenance and Bank review of other documentation in the Bank's discretion.

(c) *No delegation.* A Bank's board of directors shall not delegate to Bank officers or other Bank employees the responsibility to adopt the Bank's monitoring policies and procedures under its competitive application program and homeownership set-aside programs.

#### **§ 951.8 Remedial actions for noncompliance.**

(a) *Recovery of AHP subsidies.* A Bank shall recover the amount of any AHP

subsidies (plus interest, if appropriate) that are not used in compliance with the terms of the approved application for AHP subsidy and the requirements of this part, if the misuse is the result of the actions or omissions of the member, the project sponsor, or the project owner.

(b) *Responsible party for repayment of AHP subsidies.* Except as provided in paragraph (c) of this section:

(1) If the member causes the AHP subsidies to be misused through its actions or omissions, the member shall repay the AHP subsidies to the Bank.

(2) If the project sponsor or owner causes the AHP subsidies to be misused through its actions or omissions, the following shall apply, as determined by the Bank in its discretion:

(i) The member shall recover the AHP subsidies from the project sponsor or owner and repay them to the Bank; or

(ii) The project sponsor or owner shall repay the AHP subsidies directly to the Bank.

(c) *Recovery not required.* Recovery of the AHP subsidies is not required if:

(1) The member, project sponsor, or project owner cures the noncompliance within a reasonable period of time;

(2) The circumstances of noncompliance are eliminated through a modification of the terms of the approved application for AHP subsidy pursuant to § 951.5(f); or

(3) The member is unable to collect the AHP subsidy after making reasonable efforts to collect it.

(d) *Settlements.* A Bank may settle a claim for AHP subsidies that it has against a member, project sponsor, or project owner for less than the full amount due. If a Bank enters into such a settlement, the Finance Board may require the Bank to reimburse its AHP fund in the amount of any shortfall under paragraph (e)(2) of this section, unless:

(1) The Bank has sufficient documentation showing that the sum agreed to be repaid under the settlement is reasonably justified, based on the facts and circumstances of the noncompliance (including the degree of culpability of the non-complying parties and the extent of the Bank's recovery efforts); or

(2) The Bank obtains a determination from the Finance Board that the sum agreed to be repaid under the settlement is reasonably justified, based on the facts and circumstances of the noncompliance (including the degree of culpability of the non-complying parties and the extent of the Bank's recovery efforts).

(e) *Reimbursement of AHP fund.* (1) *By the Bank.* A Bank shall reimburse its

AHP fund in the amount of any AHP subsidies (plus interest, if appropriate) misused as a result of the actions or omissions of the Bank.

(2) *By Finance Board order.* The Finance Board may order a Bank to reimburse its AHP fund in an appropriate amount upon determining that:

(i) The Bank has failed to reimburse its AHP fund as required under paragraph (e)(1) of this section; or

(ii) The Bank has failed to recover AHP subsidy from a member, project sponsor, or project owner pursuant to the requirements of paragraph (a) of this section, and has not shown that such failure is reasonably justified, considering factors such as the extent of the Bank's recovery efforts.

(f) *Use of repaid AHP subsidies.* (1) *Use of repaid AHP subsidies in other AHP-eligible projects.* Except as provided in paragraph (f)(2) of this section, amounts of AHP subsidy, including any interest, repaid to a Bank pursuant to this part shall be made available by the Bank for other AHP-eligible projects.

(2) *Re-use of repaid AHP direct subsidies in same project.* (i) *Requirements.* AHP direct subsidy, including any interest, repaid to a member or project sponsor under a homeownership set-aside program or the competitive application program, respectively, may be repaid by such parties to the Bank for subsequent disbursement to and re-use by such parties, or retained by such parties for subsequent re-use, as authorized by the Bank, in its discretion, after consultation with its Advisory Council, in its AHP implementation plan, provided all of the following requirements are satisfied:

(A) The member or the project sponsor originally provided the AHP direct subsidy as down payment, closing cost, rehabilitation, or interest rate buy down assistance to an eligible household to purchase or rehabilitate an owner-occupied unit pursuant to an approved AHP application.

(B) The AHP direct subsidy, including any interest, was repaid to the member or project sponsor as a result of a sale by the household of the unit prior to the end of the retention period to a purchaser that is not a low- or moderate-income household.

(C) The repaid AHP direct subsidy is made available by the member or project sponsor, within the period of time specified by the Bank in its AHP implementation plan, to another AHP-eligible household to purchase or rehabilitate an owner-occupied unit in

the same project in accordance with the terms of the approved AHP application.

(ii) *No delegation.* A Bank's board of directors shall not delegate to Bank officers or other Bank employees the responsibility to adopt any Bank policies on re-use of repaid AHP direct subsidies in the same project pursuant to paragraph (f)(2)(i) of this section.

(g) *Suspension and debarment.* (1) *At a Bank's initiative.* A Bank may suspend or debar a member, project sponsor, or project owner from participation in the Program if such party shows a pattern of noncompliance, or engages in a single instance of flagrant noncompliance, with the terms of an approved application for AHP subsidy or the requirements of this part.

(2) *At the Finance Board's initiative.* The Finance Board may order a Bank to suspend or debar a member, project sponsor, or project owner from participation in the Program if such party shows a pattern of noncompliance, or engages in a single instance of flagrant noncompliance, with the terms of an approved application for AHP subsidy or the requirements of this part.

(h) *Transfer of Program administration.* Without limitation on other remedies, the Finance Board, upon determining that a Bank has engaged in mismanagement of its Program, may designate another Bank to administer all or a portion of the first Bank's annual AHP contribution, for the benefit of the first Bank's members, under such terms and conditions as the Finance Board may prescribe.

(i) *Finance Board actions under this section.* Except as provided in paragraph (d)(2) of this section, actions taken by the Finance Board under this section are reviewable under § 907.9 of this chapter.

#### **§ 951.9 Agreements.**

(a) *Agreements between Banks and members.* A Bank shall have in place with each member receiving an AHP subsidized advance or AHP direct subsidy, an agreement or agreements containing, at a minimum, the following provisions, where applicable:

(1) *Notification of Program requirements and policies.* The member has been notified of the requirements of this part and all Bank policies relevant to the member's approved application for AHP subsidy.

(2) *AHP subsidy pass-through.* The member shall pass on the full amount of the AHP subsidy to the project or household, as applicable, for which the subsidy was approved.

(3) *Use of AHP subsidy.* (i) *Use of AHP subsidy by the member.* The

member shall use the AHP subsidy in accordance with the terms of the member's approved application for the subsidy, and the requirements of this part.

(ii) *Use of AHP subsidy by the project sponsor or owner.* The member shall have in place an agreement with each project sponsor and project owner, in which the project sponsor and project owner agree to use the AHP subsidy in accordance with the terms of the member's approved application for the subsidy, and the requirements of this part.

(4) *Repayment of AHP subsidies in case of noncompliance.* (i) *Noncompliance by the member.* The member shall repay AHP subsidies to the Bank in accordance with the requirements of § 951.8(b)(1).

(ii) *Noncompliance by a project sponsor or owner.* (A) *Agreement.* The member shall have in place an agreement with the each project sponsor and project owner, in which the project sponsor and project owner agree to repay AHP subsidies to the member or the Bank in accordance with the requirements of § 951.8(b)(2)(i) or (b)(2)(ii), respectively (as applicable).

(B) *Recovery of AHP subsidies.* The member shall recover from the project sponsor or project owner and repay to the Bank any AHP subsidy in accordance with the requirements of § 951.8(b)(2)(i) (if applicable).

(5) *Project monitoring.* (i) *Monitoring by the member.* The member shall comply with the monitoring requirements applicable to such party, as established by the Bank in its monitoring policies and procedures (and set forth in the agreement) pursuant to § 951.7.

(ii) *Agreement.* The member shall have in place an agreement with each project sponsor and project owner, in which the project sponsor and project owner agree to comply with the monitoring requirements applicable to such parties, as established by the Bank in its monitoring policies and procedures (and set forth in the agreement) pursuant to § 951.7.

(6) *Transfer of AHP obligations.* (i) *To another member.* The member shall make best efforts to transfer its obligations under the approved application for AHP subsidy to another member in the event of its loss of membership in the Bank prior to the Bank's final disbursement of AHP subsidies.

(ii) *To a nonmember.* If, after final disbursement of AHP subsidies to the member, the member undergoes an acquisition or a consolidation resulting in a successor organization that is not a



member of the Bank, the nonmember successor organization assumes the member's obligations under its approved application for AHP subsidy, and where the member received an AHP subsidized advance, the nonmember assumes such obligations until prepayment or orderly liquidation by the nonmember of the subsidized advance.

(7) *Retention agreements for owner-occupied units.* The member shall ensure that an AHP-assisted owner-occupied unit is subject to a deed restriction or other legally enforceable retention agreement or mechanism requiring that:

(i) The Bank or its designee is to be given notice of any sale or refinancing of the unit occurring prior to the end of the retention period.

(ii) In the case of a sale or refinancing of the unit prior to the end of the retention period, an amount equal to a pro rata share of the AHP subsidy that financed the purchase, construction, or rehabilitation of the unit, reduced for every year the seller owned the unit, shall be repaid to the Bank from any net gain realized upon the sale or refinancing, unless:

(A) The unit was assisted with a permanent mortgage loan funded by an AHP subsidized advance;

(B) The unit is sold to a very low-, or low- or moderate-income household; or

(C) Following a refinancing, the unit continues to be subject to a deed restriction or other legally enforceable retention agreement or mechanism described in this paragraph (a)(7).

(iii) In the case of a direct subsidy, such repayment of AHP subsidy shall be made:

(A) *To the Bank.* If the Bank has not authorized re-use of the repaid AHP subsidy or has authorized re-use of the repaid subsidy but not retention of such repaid subsidy by the member or project sponsor, pursuant to § 951.8(f)(2), or has authorized retention and re-use of such repaid subsidy by the member or project sponsor, pursuant to such section and the repaid subsidy is not re-used in accordance with the requirements of the Bank and such section.

(B) *To the member or project sponsor.* To the member or project sponsor for re-use by such member or project sponsor, if the Bank has authorized retention and re-use of such subsidy by the member or project sponsor pursuant to § 951.8(f)(2).

(iv) The obligation to repay AHP subsidy to the Bank shall terminate after any foreclosure.

(8) *Retention agreements for rental projects.* The member shall ensure that an AHP-assisted rental project is subject to a deed restriction or other legally

enforceable retention agreement or mechanism requiring that:

(i) The project's rental units, or applicable portion thereof, must remain occupied by and affordable for households with incomes at or below the levels committed to be served in the approved AHP application for the duration of the retention period.

(ii) The Bank or its designee is to be given notice of any sale or refinancing of the project occurring prior to the end of the retention period.

(iii) In the case of a sale or refinancing of the project prior to the end of the retention period, the full amount of the AHP subsidy received by the owner shall be repaid to the Bank, unless:

(A) The project continues to be subject to a deed restriction or other legally enforceable retention agreement or mechanism incorporating the income-eligibility and affordability restrictions committed to in the approved AHP application for the duration of the retention period; or

(B) The households are relocated to another property that is made subject to the terms of the approved AHP application as well as a deed restriction or other legally enforceable retention agreement or mechanism incorporating the income-eligibility and affordability restrictions committed to in the approved AHP application, for the remainder of the retention period.

(iv) The income-eligibility and affordability restrictions applicable to the project shall terminate after any foreclosure.

(9) *Lending of AHP direct subsidies.* If a member or a project sponsor lends AHP direct subsidy to a project, any repayments of principal and payments of interest received by the member or the project sponsor must be paid forthwith to the Bank, unless the direct subsidy is being lent by a revolving loan fund pursuant to § 951.5(c)(13).

(10) *Special provisions where members obtain AHP subsidized advances.* (i) *Repayment schedule.* The term of an AHP subsidized advance shall be no longer than the term of the member's loan to the project funded by the advance, and at least once in every 12-month period, the member shall be scheduled to make a principal repayment to the Bank equal to the amount scheduled to be repaid to the member on its loan to the project in that period.

(ii) *Prepayment fees.* Upon a prepayment of an AHP subsidized advance, the Bank shall charge a prepayment fee only to the extent the Bank suffers an economic loss from the prepayment.

(iii) *Treatment of loan prepayment by project.* If all or a portion of the loan or loans financed by an AHP subsidized advance are prepaid by the project to the member, the member may, at its option, either:

(A) Repay to the Bank that portion of the advance used to make the loan or loans to the project, and be subject to a fee imposed by the Bank sufficient to compensate the Bank for any economic loss the Bank experiences in reinvesting the repaid amount at a rate of return below the cost of funds originally used by the Bank to calculate the interest rate subsidy incorporated in the advance.

(B) Continue to maintain the advance outstanding, subject to the Bank resetting the interest rate on that portion of the advance used to make the loan or loans to the project to a rate equal to the cost of funds originally used by the Bank to calculate the interest rate subsidy incorporated in the advance.

(b) *Agreements between Banks and project sponsors and owners.* A Bank shall have in place an agreement with each project sponsor and project owner, in which the project sponsor and project owner agree to repay AHP subsidies directly to the Bank in accordance with the requirements of § 951.8(b)(2)(ii) (if applicable).

(c) *Application to existing AHP projects.* The requirements of section 10(j) of the Act (12 U.S.C. 1430(j)) and the provisions of this part, as amended, are incorporated into all agreements between Banks, members, project sponsors, or project owners receiving AHP subsidies. To the extent the requirements of this part are amended from time to time, such agreements are deemed to incorporate the amendments to conform to any new requirements of this part. No amendment to this part shall affect the legality of actions taken prior to the effective date of such amendment.

#### § 951.10 Conflicts of interest.

(a) *Bank directors and employees.* (1) Each Bank's board of directors shall adopt a written policy providing that if a Bank director or employee, or such person's family member, has a financial interest in, or is a director, officer, or employee of an organization involved in a project that is the subject of a pending or approved AHP application, the Bank director or employee shall not participate in or attempt to influence decisions by the Bank regarding the evaluation, approval, funding, monitoring, or any remedial process for such project.

(2) If a Bank director or employee, or such person's family member, has a financial interest in, or is a director,

officer, or employee of an organization involved in an AHP project such that he or she is subject to the requirements in paragraph (a)(1) of this section, such person shall not participate in or attempt to influence decisions by the Bank regarding the evaluation, approval, funding, monitoring, or any remedial process for such project.

(b) *Advisory Council members.* (1) Each Bank's board of directors shall adopt a written policy providing that if an Advisory Council member, or such person's family member, has a financial interest in, or is a director, officer, or employee of an organization involved in a project that is the subject of a pending or approved AHP application, the Advisory Council member shall not participate in or attempt to influence decisions by the Bank regarding the approval for such project.

(2) If an Advisory Council member, or such person's family member, has a financial interest in, or is a director, officer or employee of an organization involved in an AHP project such that he or she is subject to the requirements in paragraph (b)(1) of this section, such person shall not participate in or attempt to influence decisions by the Bank regarding the approval for such project.

(c) *No delegation.* A Bank's board of directors shall not delegate to Bank officers or other Bank employees the responsibility to adopt the conflict of interest policies required by this section.

#### **§ 951.11 Temporary suspension of AHP contributions.**

(a) *Request to Finance Board.* If a Bank finds that the contributions required pursuant to § 951.2 are contributing to the financial instability of the Bank, the Bank may apply in writing to the Finance Board for a temporary suspension of such contributions.

(b) *Board of Directors review.* (1) In determining the financial instability of a Bank, the Board of Directors shall consider such factors as:

- (i) Severely depressed Bank earnings;
- (ii) A substantial decline in Bank membership capital; and
- (iii) A substantial reduction in Bank advances outstanding.

(2) *Limitations on grounds for suspension.* The Board of Directors shall not suspend a Bank's annual AHP contributions if it determines that the Bank's reduction in earnings is due to:

- (i) A change in the terms of advances to members that is not justified by market conditions;
- (ii) Inordinate operating and administrative expenses; or
- (iii) Mismanagement.

#### **§ 951.12 Affordable Housing Reserve Fund.**

(a) *Deposits.* If a Bank fails to use or commit the full amount it is required to contribute to the Program in any year pursuant to § 951.2(a), 90 percent of the unused or uncommitted amount shall be deposited by the Bank in an Affordable Housing Reserve Fund established and administered by the Finance Board. The remaining 10 percent of the unused and uncommitted amount retained by the Bank should be fully used or committed

by the Bank during the following year, and any remaining portion shall be deposited in the Affordable Housing Reserve Fund.

(b) *Use or commitment of funds.* Approval of applications for AHP subsidies from members sufficient to exhaust the amount a Bank is required to contribute pursuant to § 951.2(a) shall constitute use or commitment of funds. Amounts remaining unused or uncommitted at year-end are deemed to be used or committed if, in combination with AHP subsidies that have been returned to the Bank or de-committed from canceled projects, they are insufficient to fund:

(1) The next highest scoring AHP application in the Bank's final funding period of the year for its competitive application program;

(2) Pending applications for funds under the Bank's homeownership set-aside programs; and

(3) Project modifications approved by the Bank pursuant to the requirements of this part.

(c) *Carryover of insufficient amounts.* Such insufficient amounts as described in paragraph (b) of this section shall be carried over for use or commitment in the following year in the Bank's competitive application program or homeownership set-aside programs.

Dated: December 14, 2005.

By the Board of Directors of the Federal Housing Finance Board.

**Ronald A. Rosenfeld,**  
*Chairman.*

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