The Slow Pace of Evolution in CRA and Studying Operating Expenses, Cash Flow and Vacancy Rates

COHNREZNICK
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The Glacial Pace of "CRA Reform"

- 2009 - OCC, Federal Reserve and FDIC announce a CRA reform initiative followed by a series of public hearings in 2010
- 2010 - A CRA reform "Working Group" was formed;
- March 2013, changes were proposed to the Q&A's
- November 2013, final Q&A's were issued
- April 2014 – Large Institution CRA exam procedures changed
- July 2014 – FFIEC Webinar to explain the "new" Q&A's

The November 2013 Q&A

• The Agencies concede that CRA guidance was being inconsistently applied and that additional guidance was needed in a number of areas, including:

- When consideration should be given for community development activities that take place in a broader statewide or regional area (BSRA) that includes an institution's assessment area
- When consideration should be accorded for Investments in nationwide funds
- What the agencies meant by the term "regional area" and
- Whether the agencies viewed the practice of getting CRA "side letters" as mandatory

Community development activity in the "broader statewide or regional area"

- Community Development activities in a BSRA that includes the bank's assessment area are considered

- Community development activities that will not benefit the bank's assessment area ***may*** enhance a bank's performance evaluation if the bank is being "responsive" to the community development needs and opportunities in its assessment area(s)

  - The agencies emphasized that "Responsiveness" was a concept reflected throughout the CRA regulations
  - But did not provide a definition for the term

FFIEC Webinar on the New Q&A's

- Last July the agencies conducted a webinar to explain the new guidance …… which virtually no one seems to have seen. I would strongly encourage you to have someone in your organization listen to the webinar, the link for which is shown below
- https://consumercomplianceoutlook.org/outlook-live/2014/interagency-questions-answers-regarding-community-reinvestment/[consumercomplianceoutlook.org]
- The next couple of slides are screenshots taken from that presentation

How is Responsiveness Measured?

- In assessing whether a bank is being responsive to the community development needs of its assessment area, examiners ***will:***

- Include activities that directly benefit the assessment area,

- Include activities with a purpose, mandate, or function that includes serving that assessment area(s), ***even if*** the specific activity does not benefit that area or areas, and

- Consider the bank's "performance context" during the period under review – its profitability, whether qualified investments were available, the competition for those investments, etc

How community development activities in the BSRA are determined

Always considered

Direct benefit to AA(s)

- OR -

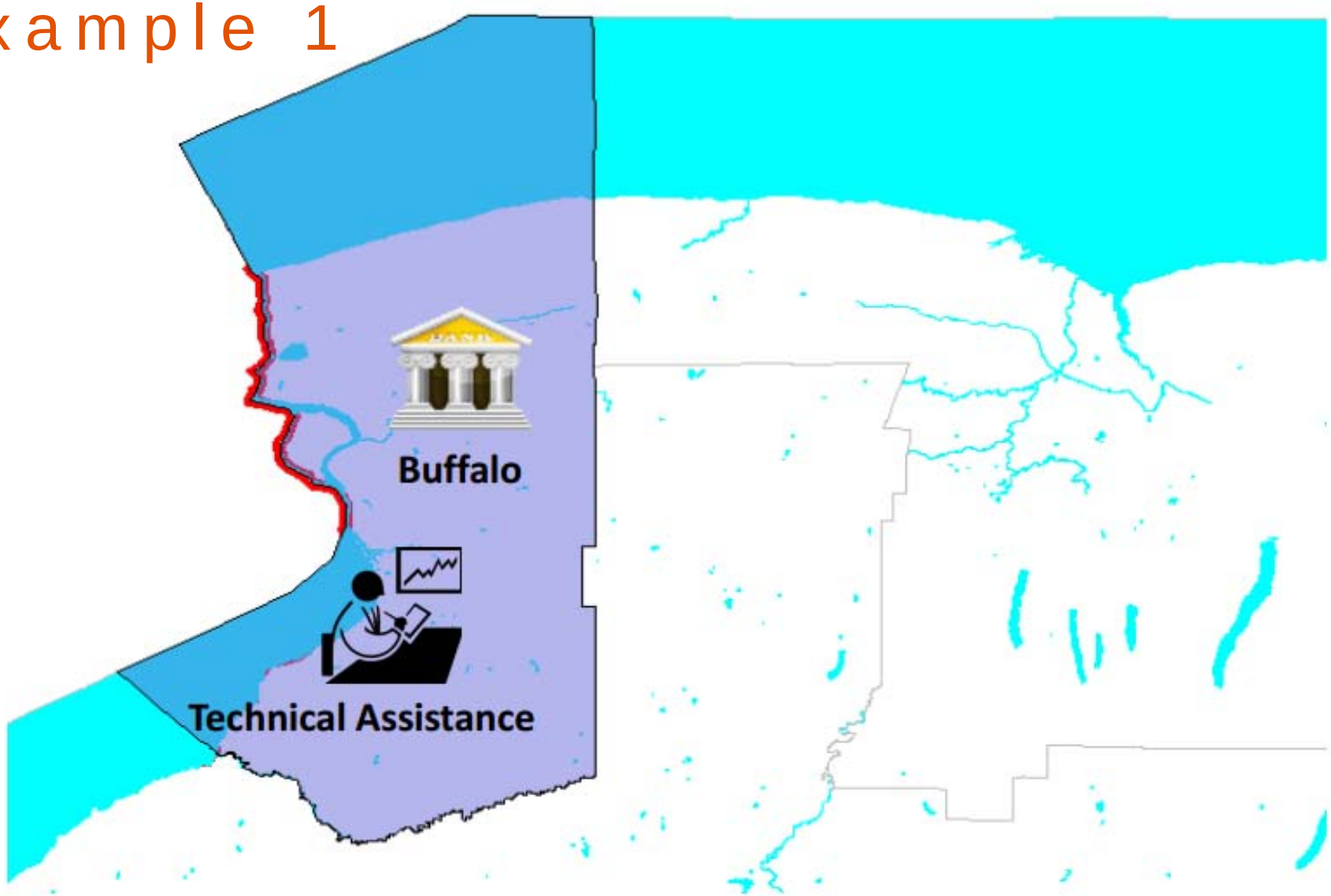
Purpose, mandate, or function to serve the AA(s)

May be considered

If the bank has been responsive to the needs and opportunities in its AA(s) –

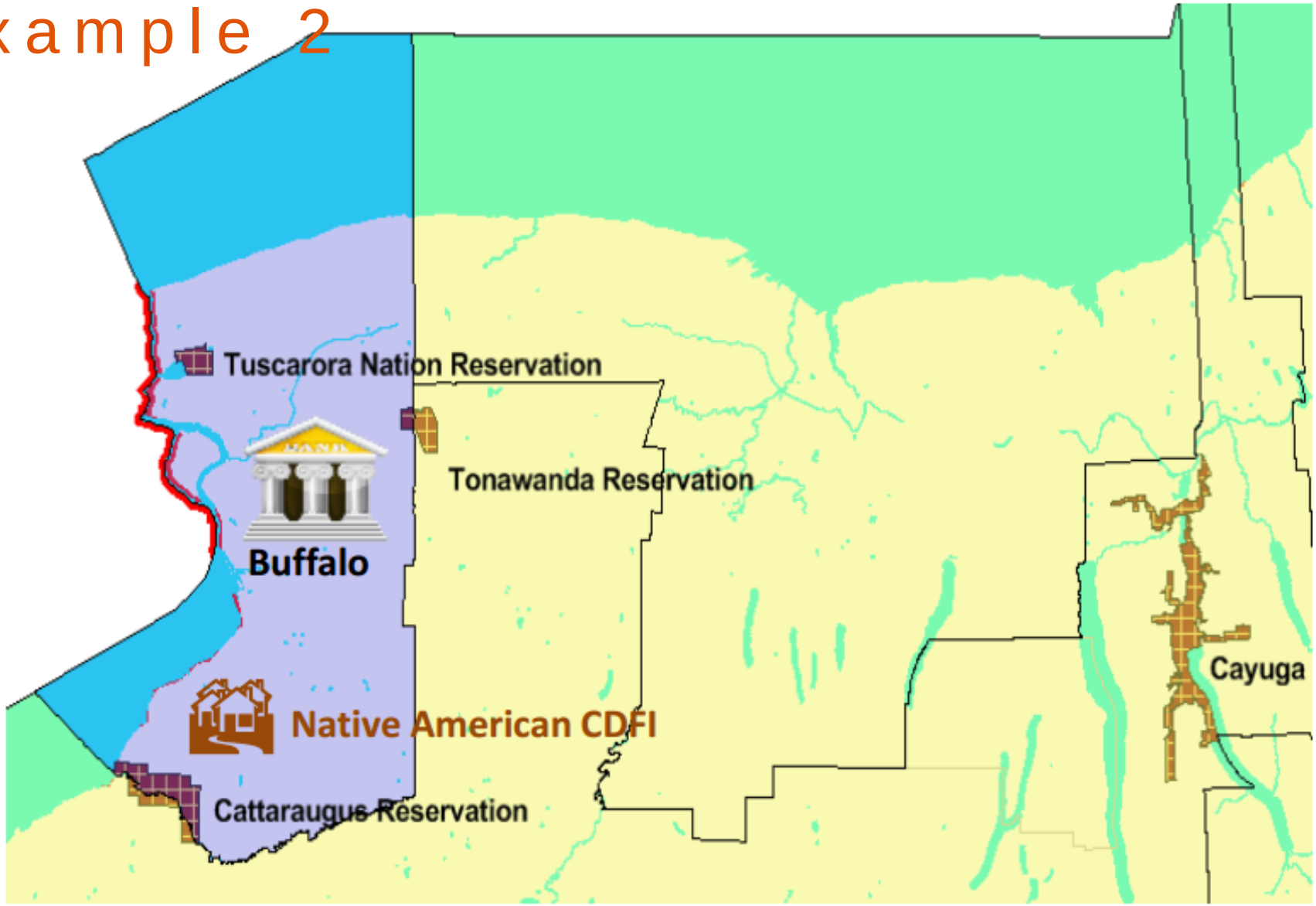
Activities that do not serve and will not benefit the AA(s)

Example 1



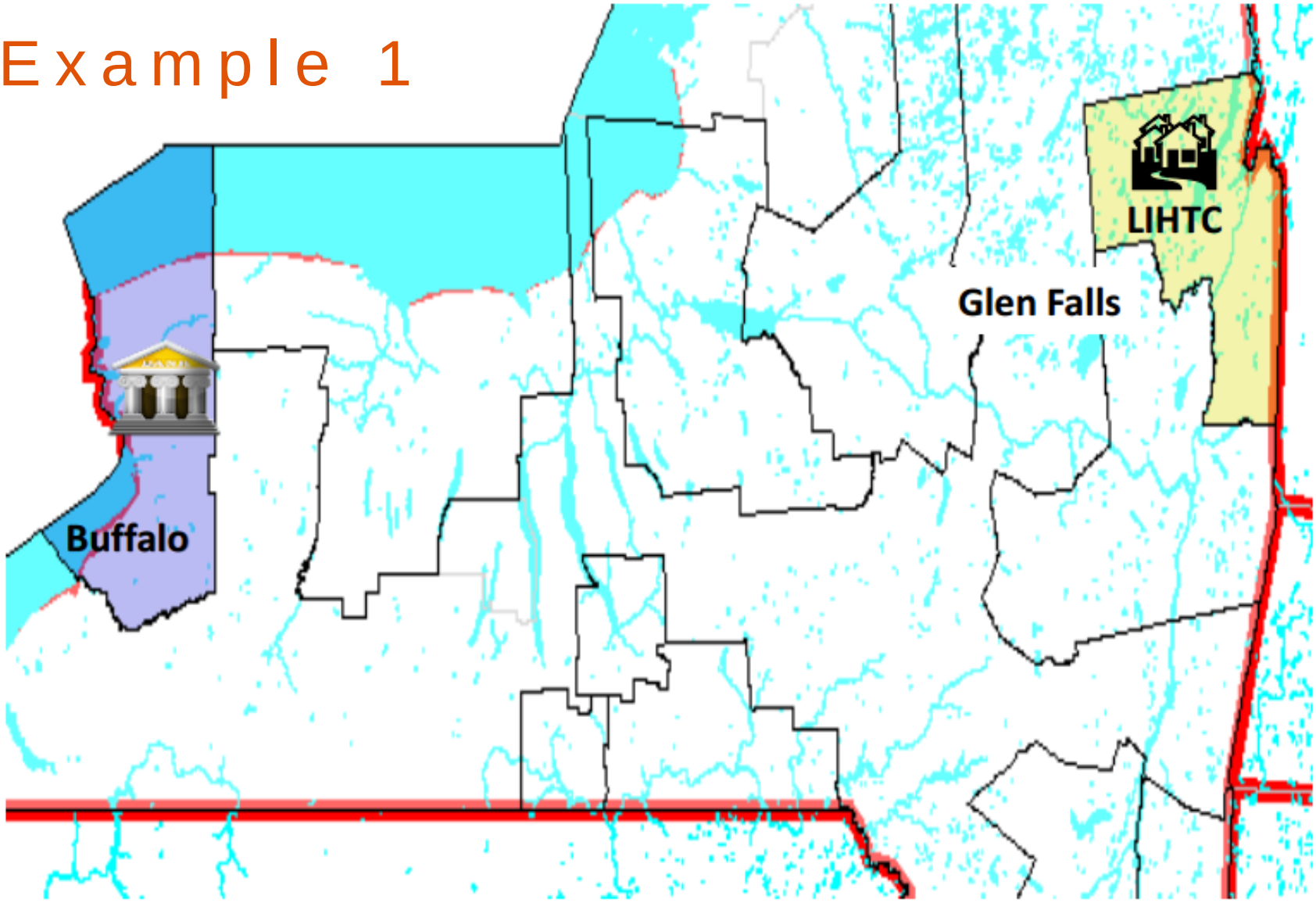
Example 1: The bank has defined the Buffalo metropolitan statistical area (MSA) as its AA, and bank offers technical assistance in its AA.

Example 2



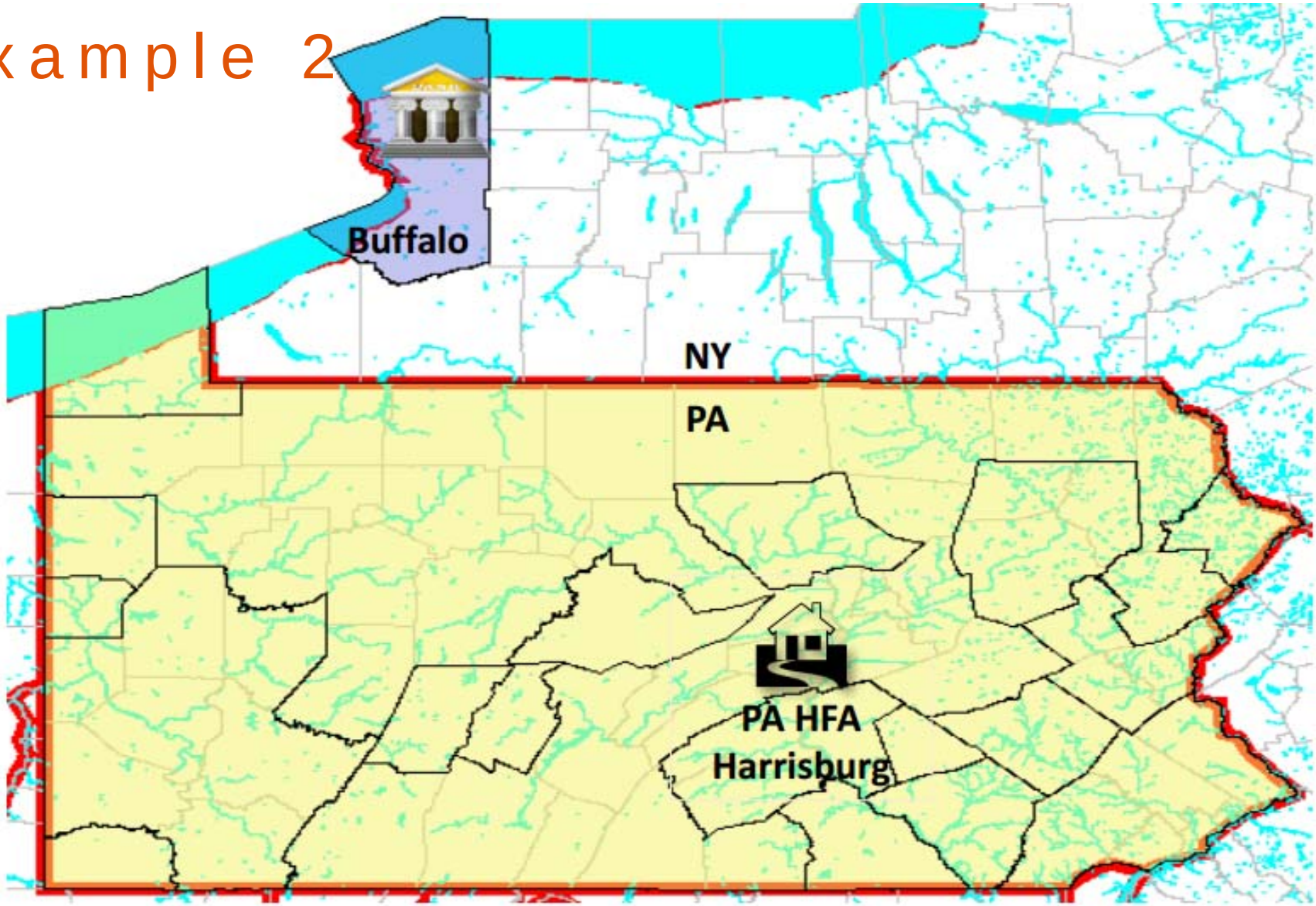
Example 2: The bank makes an investment in a Native American CDFI. The CDFI serves Indian territory within the bank's AA and home state.

Example 1



Example 1: The bank makes a loan related to a LIHTC project within the state, but that will not benefit the bank's AA.

Example 2



Example 2: The bank makes a qualified investment in the Pennsylvania State Housing Finance Authority which benefits multiple communities outside of the bank's home state, but within the broader regional area.

The Economic Growth & Regulatory Paperwork Reduction Act of 1996

- Under the EGRPRA, the FFIEC must hold hearings once every ten years to identify unnecessary or unduly burdensome regulations and consider how to reduce the regulatory burden on banks
- The hearings are attended by the Comptroller of the OCC, a member of the Board of Governors of the Federal Reserve & the FDIC Commissioner
- These hearings provide AHTCC members with the opportunity to make five minute presentations on CRA matters as well as the opportunity to submit written comments

Economic Growth & Regulatory Paperwork Reduction Act

- The first hearing was in L.A. in December, a second will take place in Dallas on February 4th
- Additional hearings will be held:
  - In Boston on May 4th
  - In Chicago on October 19th
  - In Washington on December 2nd
  - I encourage the Coalition and/or its members to register and make presentations
  - More information is available at this link:
    - http://egrpra.ffiec.gov/[egrpra.ffiec.gov]

2014 Housing Credit Equity Volume by Investment Type

Top 10 Syndicators	$5,666,300,000
Remaining Syndicators	$3,545,000,000
Direct Investors	$3,286,000,000
Total	$12.497B

LIHTC Performance Metrics

- Several months ago, we published data on the performance of roughly 18,000 LIHTC projects that are still within their 15 year compliance period
- We estimate that this sub-set represents roughly 2/3 of all the "active" LIHTC projects
- The data is very positive, particularly when seen in historical perspective

GOOD…

2005

– Stabilized properties analyzed	11,239
– Physical occupancy	96.0%
– Median DCR	1.15
– Median cash flow p/u	$240
– % underperforming	34%
– Cum. foreclosure rate	0.35%

BETTER…

2010

– Stabilized properties analyzed	15,399
– Physical occupancy	96.6%
– Median DCR	1.24
– Median cash flow p/u	$419
– % underperforming	24.7%
– Cum. foreclosure rate	0.57%

BEST…

2012

– Stabilized properties analyzed	15,588
– Physical occupancy	97.0%
– Median DCR	1.30
– Median cash flow p/u	$498
– % underperforming	20.2%
– Cum. foreclosure rate	0.63%

WHY HAVE THE PERFORMANCE METRICS IMPROVED?

- Better underwriting is just part of the answer
- Low interest rates have allowed us to bail out many weak performers
- We believe that ***economic occupancy*** has increased considerably in recent years
- The demand for affordable units has resulted in lower turnover rates, and asset managers are telling us that rent collections are stronger

WHERE DO WE GO FROM HERE?

- CohnReznick is rolling out its next performance study in April and every syndicator with whom we have spoken has agreed to participate
- By adding direct investment data from the Top 5 banks, the study will include 20,000 units
- For the first time we will request and analyze
  - Both physical and economic occupancy
  - Operating expenses
  - Data on projects in areas that have experienced zero/negative growth in AMI

Operating Expense Data Request

Per Unit Operating Expenses							
Misc. Operating Expenses	Salaries & Employee Benefits	Repair and Maintenance	Management Fees	Insurance	Utilities	Property Taxes	Replacement Reserves
$500	$1,100	$1,000	$450	$350	$1,600	$900	$400

Per Unit Operating Expenses					
Salaries & Employee Benefits	N				Utilities
$1,100	$1				$1,600

CohnReznick:
Suggested expense line item inclusions:

* Employee leasing commissions and bonuses
* Office salaries
* Maintenance payroll
* Payroll taxes
* Payroll fees
* Workers compensation
* Health insurance

It's Time for the LIHTC Industry to Give up its Horse and Buggy