



Federal Housing Finance Board

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SUBJECT: Lakeview Pedcor CIP Project

ISSUE:

Whether the Federal Home Loan Bank of Indianapolis ("Indianapolis Bank") may count letters of credit issued in connection with financing the Lakeview multifamily apartment project ("Lakeview") towards the Indianapolis Bank's Community Investment Program ("CIP") outstanding advance target minimum.

CONCLUSION:

In the absence of guidance from the Federal Housing Finance Board ("Finance Board"), the Indianapolis Bank could reasonably interpret section 10 (i) of the Federal Home Loan Bank Act ("Bank Act"), 12 U.S.C. §1430(i) (Supp. IV 1992), to permit it to count the letters of credit issued in connection with financing Lakeview towards the Indianapolis Bank's CIP outstanding advance target minimum.

DISCUSSION

I. BACKGROUND

The Bank Act requires each Federal Home Loan Bank ("FHLBank") to establish a CIP to provide funding for members to undertake community-oriented mortgage lending. See *id.* The Finance Board has directed the FHLBank to set individual performance targets to measure their community support performance in 1994. See Board Res. 93-110 (Dec. 15, 1993).

Community support is defined as average CIP advances. See id. Accordingly, each FHLBank has adopted a minimum target for outstanding CIP advances as a measure of its community support performance. Thus, if a FHLBank makes an advance to finance an activity that is eligible for financing under the CIP provisions of the Bank Act, the FHLBank may count the advance towards its Community Support performance target for 1994.

Pedcor Investments ("Pedcor"), a limited partnership, has requested the Indianapolis Bank to provide letters of credit to its members to facilitate the issuance of \$5,600,000 of tax-exempt bonds by the city of Franklin, Indiana. The proceeds of the bond issuance will provide permanent financing for Lakeview, a 1600-unit multifamily housing project owned by Pedcor. The counsel for Pedcor, through the Indianapolis Bank, has requested a legal analysis from the General Counsel of the Finance Board on whether Lakeview qualifies for financing under the Indianapolis Bank's CIP. Following are the facts pertinent to Lakeview's eligibility for financing under the CIP.

Lakeview is now completely built and fully operating. It is located on what used to be farm land just beyond the suburban fringe of Franklin, Indiana, and there is no adjacent residential or commercial development. Lakeview has created four to five full-time equivalent jobs and an estimated \$340,000 of local spending activity for property management, lawn care, painting, and other maintenance activities.

Since Lakeview will be financed by a combination of the proceeds of the tax-exempt bond issuance and the equity generated through federal low-income housing tax credits, Lakeview will be subject to the requirement that 40 percent of the project's units be affordable and set aside for tenants with income of 60 percent or less of the area median income for at least 15 years. See 42 U.S.C. § 142(d). There are no income or rent restrictions on the remaining 60 percent of the project's units. However, Pedcor is willing to commit by deed restriction to maintain at least 75 percent of Lakeview's units for families with incomes at or below 115 percent of the area median income.

As of December 1993, Lakeview was 95 percent occupied, and 88 percent of the units were occupied by families with incomes at or below 115 percent of the area median income. The remainder of the units, were occupied by families with incomes exceeding 115 percent of the area median,

II. ANALYSIS

In order for the letters of credit issued by the Indianapolis Bank to count towards its CIP outstanding advance target minimum, the letters of credit must be issued for one or more of the purposes set forth in section 10(i)(2)(A) through (D) of the Bank Act.

- (A) to finance home purchases by families whom income does not exceed 115 percent of the median income for
- (B) to finance the purchase or rehabilitation of housing for occupancy by families whom income does not exceed 115 percent of, the median income for the areas
- (C) to finance commercial and economic development activities that benefit low- and moderate-income families or activities that are located low- and moderate-income neighborhoods; and
- (D) to finance projects that further a combination of purposes described in paragraphs (A) through (C).

Id. § 1430(i)(2)(A)-(D).

The Indianapolis Bank and Pedcor argue that financing the Lakeview project meets the criteria in sections 10(i)(2)(B) and 10(i)(2)(D). See id. § 1430(i)(2)(B), (D).

A. Section 10(i)(2)(B).

Section 10(i)(2)(B) states that CIP funds may be used to finance "housing for occupancy by families whose income does not exceed 115 percent of the median income for the area." Id. § 1430(i)(2)(B). It is not clear from the plain meaning of section 10(i)(2)(B) whether all the units in a multifamily housing project must be occupied by families with incomes at or below 115 percent of area median income in order for the project to qualify for CIP financing under Section 10(i)(2)(B). The legislative history of the CIP provisions of the Bank Act does not classify this issue, and the Finance Board has not adopted any regulation, policy, or other guidance interpreting section 10(i)(2)(B).

Pedcor argues that since a significant percentage of the units at Lakeview are occupied by families with incomes at or below 115 percent of area median income, section 10(i)(2)(B) is satisfied. Similarly, the Indianapolis Bank argues that absent express regulatory or policy guidelines of the Finance Board,

the statute allow for a de minimis exception to section 10(i)(2)(B) such that up to 15 percent of the units could be occupied by families with incomes in excess of 115 percent of the area median, and the project would still satisfy section 10(i)(2)(B).

An argument can be made that the word "housing" in section 10(i)(2)(B) refers to the entire housing project. Therefore, if a large majority of the units in a project are designated for occupancy by families in the targeted 115 percent income group, then the entire project qualifies as "housing for occupancy by families whose incomes do not exceed 115 percent of median income for the area." Id.

Although the Finance Board has no written policies or guidelines governing this issue, in practice, members of the Housing Finance Directorate ("HFD") staff have told members of the staffs of the FHLBank that 100 percent of a project's units must be occupied by families with incomes at or below 115 percent of the area median in order for the project to satisfy section 10(i)(2)(B). However, since HFD staff do not have independent authority to adopt interpretations of the CIP provisions on behalf of the Finance Board, HFD's oral opinions on this issue do not constitute Finance Board policy. Thus, whether a project with less than 100 percent of its units occupied by families with the targeted income may qualify for CIP financing appears to be a matter of policy that has not been addressed by the Finance Board.

In sum, the Indianapolis Bank could reasonably argue that absent interpretive guidance from the Finance Board, Lakeview qualifies under section 10(i)(2)(B) as "housing for occupancy by families whose incomes do not exceed 115 percent of median income for the area." Id.

B. Section 10(i)(2)(D)

The Indianapolis Bank further argues that even if section 10(i)(2)(B) does not allow for a de minimis percentage of units to be occupied by families with incomes exceeding 115 percent of the area median, Lakeview nonetheless qualifies for CIP financing, because section 10(i)(2)(D) allows a project to qualify if, in combination, the project is occupied by some families with incomes at or below 115 percent of the area median and the project qualifies as a commercial or economic development activity under section 10(i)(2)(C).¹

1. Pedcor argues that Lakeview also would qualify under section 10(i)(2)(C) as an "economic development activity" without reliance on the fact that Lakeview is occupied by families with the targeted income. However, an argument can be made that if a multifamily project may be considered an

1. Commercial and Economic Development Activities"

The Bank Act does not define economic development activity,' and the plain meaning of the term does not suggest a clear and unambiguous interpretation. Further, the Finance Board has not adopted an interpretation of this term. Pedcor notes that the city of Franklin has designated Lakeview an economic development facility and the state of Indiana has concurred by allocating a portion of its tax-exempt bond volume cap to the financing of Lakeview. However, since the Finance Board is charged with interpreting the meaning of the term economic development activity" as it appears in the Bank Act, the city of Franklin's characterization of Lakeview as an economic development facility is supportive but not dispositive on this issue.

The legislative history of the CIP provisions suggests that in the context of section 10 (i)(2)(B), commercial and economic development activities" includes, but is not limited to, activities that result in employment of low-income people in low- and moderate-income neighborhoods. See Joint Explanatory Statement of the Committee of Conference ("FIRREA Conference Report), H.R. Conf. Rep. No. 222, 101st Cong., 1st Sess., 430 (1989).

Pedcor argues that Lakeview is an economic development activity because the project creates four or five full-time equivalent jobs and \$340,000 in local spending activities. In addition, as discussed below, Pedcor argues that Lakeview is a low- and moderate-income neighborhood. Therefore, according to Pedcor, Lakeview creates jobs for low-income people in a low- and moderate-income neighborhood, consistent with the purpose set forth in the FIRREA Conference Report. See *id.* Since the Finance Board has not adopted minimum standards governing what constitutes economic development activity," it is not clear whether the job creation and local spending generated by

(Footnote 1 continued from previous page)
economic development activity" under section 10(i)(2)(C) solely on the ground that it creates jobs and generates spending on maintenance services, which most housing development do, then even those multifamily housing projects that are not occupied by households with incomes at or below 115 percent of the area median could be eligible for CIP financing. This would tender meaningless motion 10(i)(2)(B), which specifically requires multifamily housing projects to be occupied by families with this targeted income in order for the projects to be financed under the CIP. Therefore, in order to read section 10(i)(2)(B) consistent with section 10 (i)(2)(C), a multifamily housing project should not be eligible for CIP financing solely by qualifying as an economic development activity under section 10(i)(2)(C).

Lakeview qualifies as economic development activity" under section 10(i)(2)(C).

2. "Benefits Low- And Moderate-Income Families

Assuming the Lakeview may be considered an economic development activity, Pedcor argues that Lakeview benefits the low- and moderate-income families, as required by section 10(i)(2)(C), because it provides housing for occupancy by low- and moderate-income families and potentially benefits low-income people who may be employed as a result of the four to five new jobs and the local spending activity created by Lakeview. See *id.* § 1430(i)(2)(C). Pedcor's counsel believes that the people who fill the four to five jobs created at Lakeview will be low-income people because the salaries for the jobs are relatively low. However, there are no plans to ensure that low-income people are employed in these jobs. Nonetheless, absent regulatory or policy guidance to the contrary, the Indianapolis Bank could reasonably argue that Lakeview benefits low- and moderate-income families within the meaning of section 10(i)(2)(C). See *id.*

3. "Located In A Low And Moderate-Income

In addition, Pedcor argues that Lakeview is an economic development activity that is located in a low- and moderate-income neighborhood, as required by section 10(i)(2)(C). The Bank Act defines "low- and moderate-income neighborhood" as any neighborhood in which 51 percent or more of the households are low- Of moderate-income households. See *id.* § 1430(j)(13)(D). Pedcor argues that Lakeview is a self-contained neighborhood and that more than 51 percent of families who live there are low- and moderate-income

The Bank Act does not define "neighborhood," and the Finance Board has not adopted an interpretation of this term. The Finance Board, however, has issued a proposed rule containing a definition of "neighborhood" for purposes of the Affordable Housing Program ("AHP"). See 59 Fed. Reg. 1323 Jan. 10, 1994). Under the proposed AHP regulation, the definition of neighborhood includes a geographic location designated in comprehensive plans, ordinances, or other local documents as a neighborhood, village, or similar geographical designation that is within the boundary but does not encompass the entire area of a unit of general local government for which income information is available to determine the percentage of households with incomes satisfying the requirements for the AHP. See *id.* at 1349.

According to Pedcor's counsel, the city of Franklin passed an ordinance designating Lakeview as an economic development facility, but not as any kind of geographic location.

Therefore, Lakeview does not qualify as a neighborhood under the definition in the proposed AHP regulation. Nonetheless, since the statute is unclear as to what qualifies as a "neighborhood," and the Finance Board has not yet adopted an official interpretation of neighborhood," there is nothing in the statute or the Finance Board's current regulations or policies that prohibits the Indianapolis Bank from determining that Lakeview's physical characteristics make it a neighborhood, as long as there is a reasonable basis for such a determination.

At present, 74 percent of the Lakeview units are occupied by families with incomes at or below 80 percent of the area median. Therefore, if Lakeview were to be considered a neighborhood, it would qualify as a low- and moderate-income neighborhood under the Bank Act.

In sum, the Indianapolis Bank could reasonably argue that Lakeview satisfies section 10(i) (2)(D), which provides for CIP financing of projects that satisfy a combination of the purposes set forth in section 10(i)(2)(B) and section 10(i)(2)(C).

It is not clear whether section 10(i)(2)(B) of the Bank Act requires 100 percent of the units in a multi family housing project to be occupied by families with incomes at or below 115 percent of the area median in order for the project to qualify for CIP financing. Further, the Finance Board has not adopted any standards governing what constitutes an "economic development activity" under section 10(i) (2)(C). Absent clear regulatory or policy guidance from the Finance Board, the Indianapolis Bank in establishing the parameters for its CIP could reasonably argue that Lakeview qualifies for CIP financing under section 10(i)(2)(B) and section 10(i)(2)(D). Therefore, the Indianapolis Bank could reasonably interpret section 10 i) of the Bank Act to permit it to count the letters of credit issued in connection with financing Lakeview towards the Indianapolis Bank's community support performance target.