

**TESTIMONY OF CHRIS B. FOSTER ON HUD'S MARK TO  
MARKET PROGRAM RENEWAL, BEFORE THE SENATE  
SUBCOMMITTEE ON HOUSING AND TRANSPORTATION**

**June 14, 2006**

Mr. Chairman and Members of the Subcommittee, I appreciate the opportunity to testify on legislation to extend HUD's mark-to-market restructuring program from its current expiration date of October 1, 2006. My name is Chris Foster and I am President of Hampstead Partners. I am testifying today on behalf of the National Leased Housing Association, a trade association located in Washington, D.C., which for over 35 years has represented owners, managers, investors, lenders and public agencies involved in developing and preserving affordable multifamily housing primarily assisted under housing programs administered by HUD.

We strongly support the extension of the mark-to market program. It is a valuable tool that has resulted in the preservation of over 200,000 affordable rental apartments as well as resulted in significant savings to the Federal Government. The Mark to Market (M2M) program applies to properties, insured by the Federal Housing Administration (FHA) with project-based assistance primarily under section 8 of the United States Housing Act of 1937 and with rents in excess of rents for comparable unassisted units in the area. When the first wave of 20-year section 8 contracts approached expiration in the mid 1990s, Congress was reluctant to authorize renewal of the contracts at above-market rents. Many of these projects could not operate and meet mortgage payments at market rents. A large number of these projects were financed with HUD-insured mortgages. This universe of projects lent themselves to a solution with a positive budget impact, restructuring of the HUD-insured mortgage by a full or partial payment of insurance

claims, thereby lowering debt-service to a level that was sustainable at market rents. In addition, needed rehabilitation and the replenishment of reserves is generally accomplished under the program, at no cost to HUD, through further reductions in existing debt to permit new debt to be increased to cover these costs. Owners of projects that have been restructured must execute use agreements to accept section 8 renewal offers and to keep rents affordable, with or without the availability of section 8 assistance, for 30 years.

We understand that in the coming years a significant number of section 8 contracts will be eligible for initial renewal and that many are attached to projects with HUD-insured mortgages. Because rent adjustments on initial section 8 contracts are dependent on whether rents are above or below market, HUD has information available as to approximately how many of these projects may have above-market rents. In addition, other projects that previously renewed their contracts under other authorities because their rents were below market may have experienced a change in market conditions that results in their rents being above market. They are then also eligible to participate in the M2M program. The National Housing Trust estimates nearly 1000 properties will be eligible the M2M program in the next five years.

The same factors that moved Congress to enact the mark-to-market program in 1997 and to extend it in 2001 exist today and warrant a further extension. We urge Congress to authorize a five-year extension of HUD's restructuring authority and have attached for the record an industry letter signed by 15 national housing organizations that endorse such an extension.

The bill proposes two changes to the Mark to Market program that we strongly support. First the bill increases from five percent to nine percent the total number of units that can have exception rents in excess of 120 percent of the fair market rent for the area. Exception rents are budget-based rents that exceed market rent and are used when no amount of debt restructuring can yield viable rents that are below market. The five percent limit was basically an educated guess when it was enacted in 1997 and HUD's experience with that limit over the years should be acknowledged. The second change extends the period during which a nonprofit purchaser of a mark-to-market project can obtain relief from a second mortgage on the project. Such a change is necessary to recognize the reality of real estate acquisition timeframes and will encourage major recapitalization of the properties.

We recommend adding a provision to the bill to give owners of properties that have undergone debt restructuring the right to request and receive budget-based rent increases. Such rent adjustments are authorized in the mark to market regulations but discretionary with HUD and HUD has determined not to entertain any request for budget-based rent adjustments, relying instead solely on an annual OCAF adjustment. Over the 30-year life of the program, situations may arise where an OCAF adjustment is insufficient to meet rising operating costs, particularly for those properties that were underwritten before March of 2002 when HUD amended its underwriting criteria to allow a sufficient cushion for operating cost increases. In order to maintain project viability, owners should have the option of a budget-based review of rents in those circumstances.

Further, there also may be situations that will require additional restructuring of such projects.

The bill also makes one change to the authorizing statute that moves the program into new areas and which we cannot fully endorse at this time. The bill as drafted would give HUD the *unilateral* authority to require section 8 projects with HUD-insured loans, but with below-market rents, to participate in the M2M program or lose their section 8 assistance. This is a major departure from the current program and we are not aware of any compelling evidence to justify such a change. Any proposal that makes a fundamental change to current law and practice should not be included as an amendment to an extension bill and should be thoroughly vetted as part of a separate legislative initiative. For nearly nine years we have had stable and predictable rules for section 8 renewals that work well. An extension of the mark-to market program beyond its original scope and which call for unilateral participation in M2M can cause confusion and is overreaching, potentially leading to an increased number of owners opting out of the section 8 program. Properties with rents below comparable market rents have options to address rehabilitation needs and we prefer the use of existing tools rather than change the framework of the current mark to market program. In fact, we encourage the Department to review its existing tools and assign non-M2M preservation transactions (property disposition, 236 decouplings, loan work-outs, etc) to the Office of Affordable Housing Preservation (OAHP) which now administers the Mark to Market program. Due to its responsibilities related to mortgage restructuring, the OAHP office is staffed by

sophisticated real estate professionals who understand the intricacies of preservation restructurings and would be well suited to process other complex transactions.

Thank you for your time and consideration. I will be glad to answer any questions.