



## Research

# The Housing Trust Fund and Capital Magnet Fund: A Primer

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The Federal Housing Finance Agency (FHFA), regulator and conservator of government-sponsored enterprises (GSEs) Fannie Mae and Freddie Mac, announced in December 2014 it would allow the GSEs to pay into the Housing Trust Fund and Capital Magnet Fund. This paper briefly provides background on those funds and their purpose, while also outlining the policy implications of FHFA's decision.

## BACKGROUND

TABLE 1. TIMELINE OF HTF/CMF RELATED EVENTS & RULEMAKINGS

JULY 2008	HOUSING & ECONOMIC RECOVERY ACT EFFECTIVE
SEPTEMBER 2008	FANNIE MAE & FREDDIE MAC ENTER CONSERVATORSHIP UNDER FHFA
NOVEMBER 2008	FHFA SUSPENDS GSE HTF/CMF ALLOCATIONS
MARCH 2009	<a href="#">RFC</a> : DESIGN & IMPLEMENTATION OF CMF FROM TREASURY DEPT
DECEMBER 2009	<a href="#">PR</a> : HTF ALLOCATION FORMULA FROM HUD
MARCH 2010	<a href="#">NPR &amp; RFC</a> : REGULATIONS GOVERNING THE CMF FROM TREASURY DEPT
OCTOBER 2010	<a href="#">PR</a> : REGULATIONS GOVERNING THE HTF & COORDINATION WITH HOME PROGRAM FROM HUD
DECEMBER 2010	<a href="#">IFR &amp; RFC</a> : REGULATIONS GOVERNING THE CMF FROM TREASURY DEPT
JULY 2013	NLIHC ET AL FILE <a href="#">LAWSUIT</a> AGAINST FHFA TO COMPEL PAYMENTS TO HTF
SEPTEMBER 2014	NLIHC ET AL <a href="#">LAWSUIT DISMISSED</a> FOR LACK OF STANDING

DECEMBER 2014	FHFA SENDS <a href="#">LETTER</a> TO GSEs REINSTATING CONTRIBUTIONS  IFR & RFC: PROHIBITION ON PASSING ON COST OF ALLOCATIONS FROM FHFA
JANUARY 2015	IFR: REGULATIONS GOVERNING THE HTF FROM HUD
Note: Notice of Proposed Rulemaking (NPR), Proposed Rule (PR) Interim Final Rule (IFR), & Request for Comment (RFC)	

With the Housing and Economic Recovery Act of 2008 (HERA), Congress established the Housing Trust Fund (HTF) and Capital Magnet Fund (CMF), assigning a portion of revenues from Fannie Mae and Freddie Mac as the dedicated funding source. The GSEs must set aside 4.2 basis points of each dollar of unpaid principal balance of its total new business purchases (equivalent to 4.2 cents for every \$100) and then allocate those reserved funds following each fiscal year. The funding is divided with the HTF receiving 65 percent and the CMF receiving 35 percent.

In December 2014, FHFA lifted its suspension of GSE allocations, directing them to set aside funding for the HTF and CMF this year. According to the president's budget, the GSEs are projected to distribute \$120 million and \$64 million to the HTF and CMF respectively in fiscal year 2016.<sup>[1]</sup> Another estimate projects up to \$400-500 million would go to the funds based on previous GSE volumes.<sup>[2]</sup> Congress may also elect to appropriate funds in the future.

The HTF is administered by the Department of Housing and Urban Development (HUD), which developed the formula by which money will be handed out to states and state-level housing agencies to increase and maintain the supply of affordable rental housing and boost homeownership for low-income Americans. The CMF, an account within the Community Development Financial Institutions Fund overseen by the Treasury Department, similarly funds a competitive grant program wherein community development financial institutions and nonprofit housing corporations apply for funding to be used to boost affordable housing projects as part of a larger community stabilization or revitalization strategy.

## PURPOSE OF THE HTF AND IMPLEMENTATION

Attempts to establish a national housing trust fund have been made for more than 25 years, ultimately accomplished with HERA.<sup>[3][4]</sup> The program is meant to provide a stable funding source to increase the supply of affordable housing for low-income Americans. Funds from the HTF can be combined with Low Income Housing Tax Credits (LIHTC), HOME, Choice Neighborhoods funding, Rental Assistance Demonstration, and other programs to accomplish that aim. Specifically, at least 80 percent of money from the HTF must be used for rental housing; up to 10 percent of the funds can be used for homeownership programs and 10 percent to cover recipients' administrative and planning costs.

In January, HUD issued an interim final rule establishing the regulations that will govern the HTF. In determining state allocations of funds, HUD will weigh several factors:

- State's relative shortage of rental housing for extremely low-income (ELI) families<sup>[5]</sup> (weighted 50 percent)
- State's relative shortage of rental housing for very low-income (VLI) families (weighted 12.5 percent)
- State's relative number of ELI families in substandard, overcrowded or unaffordable housing (weighted 25 percent)
- State's relative number of VLI families in substandard, overcrowded or unaffordable housing (weighted

12.5 percent)

- Local construction costs
- Minimum allocation per state of \$3 million

## ***State-Level Impacts***

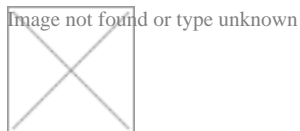
As part of its rulemaking, HUD completed a regulatory impact analysis that includes an estimate of how much money each state would receive using its allocation formula should the HTF receive either \$375 million or \$1 billion (see map below).<sup>[6]</sup> With the funding formula emphasizing affordability and existing housing stock, states with large populations and higher housing costs generally receive more HTF funding than their share of the U.S. population.

With \$375 million in HTF funding, California would predictably receive the most funding, totaling \$61 million. California and New York, with higher than average housing costs, would stand to receive 16.3 percent and 9.6 percent of a \$375 million trust fund allocation despite making up only 11.9 percent and 6.2 percent of the country's population, respectively.<sup>[7]</sup> If funding to the HTF increased to \$1 billion, California would receive 18.7 percent of HTF funding and New York would receive 11 percent. Many small states such as Wyoming and Vermont would also receive an outsized share of HTF funding in regard to their share of the population due to the \$3 million minimum, though that advantage would diminish as funding to the HTF increases. In total, 21 states, the District of Columbia, and Puerto Rico would receive the minimum \$3 million allocation if the HTF receives \$375 million from the GSEs.

In its interim final rule, HUD also made a few significant changes to the regulations governing the HTF from its 2010 proposed rule. HUD reversed course on a proposal to encourage transit-oriented development. HUD will also now allow HTF funds to be used on public housing. And perhaps most notably, if less than \$1 billion is allocated to the HTF, all funds must be used for ELI housing so that funding can prioritize worst case needs.

## ***End of Suspended Assessments***

Shortly after HERA was passed in 2008, the GSEs entered into conservatorship overseen by FHFA and allocations to the HTF and CMF were suspended. FHFA Director Mel Watt reversed that decision in December 2014, sparking some controversy; in particular, many see FHFA's action conflicting with mandates under HERA. By statute, FHFA must suspend allocations under a number of scenarios<sup>[8]</sup>, shown below:



Furthermore, FHFA has broader mandates as conservator of the GSEs<sup>[9]</sup>, shown below:



In letters to Fannie Mae and Freddie Mac, FHFA Director Mel Watt reasoned that the temporary suspension was no longer justified because the allocations “would not contribute to the financial instability” of the GSEs, citing their recent dividends to the Treasury Department.<sup>[10]</sup> He argued the two other provisions allowing the

suspension of allocations were also no longer applicable because of changes to the GSE stock purchase agreement that sweep all GSE profits to the Treasury Department. Furthermore, FHFA expects the GSEs to maintain profitability in the near future and reserves the right to reverse the decision if they do not.

## CRITICISMS AND POLICY IMPLICATIONS

1. Funds are not subject to the scrutiny and approval inherent in the regular appropriations process.

Advocates of the HTF have acknowledged the importance of gaining funds necessary for its capitalization from outside the regular appropriations process. Sheila Crowley, President and CEO of the National Low Income Housing Coalition, stated at a Senate Banking Committee hearing, "...if we thought we could get the appropriated funds...to solve this problem, then we would not need to have this conversation."<sup>[11]</sup> Critics argue that this mentality undermines the integrity of the congressional appropriations process, which forces lawmakers to weigh the tradeoffs of policy priorities in distributing finite budget resources.<sup>[12]</sup> Furthermore, by relying for funding outside of the appropriations process, Congress forfeits the opportunity to scrutinize the HTF's effectiveness at meeting stated policy objectives.

2. Government support for affordable housing is redundant with appropriated funding of more than 30 programs.

The federal government supports housing in many different ways—from tax credits and deductions to the more than 30 programs in HUD. In fact, the GAO concluded that the federal government "incurred about \$170 billion in obligations for federal assistance and forgone tax revenue in fiscal year 2010" to provide housing aid to homebuyers, renters, and state and local governments.<sup>[13]</sup> A complex web of existing federal support has raised doubts about the costs, effectiveness, and efficiency by which the federal government boosts housing affordability. The HTF adds further complexity without reforming existing programs that work to accomplish similar aims, such as the HOME Investment Partnerships Program and the LIHTC.

3. FHFA's decision ignores its statutory obligations and obligations to taxpayers.

With obligations under the law to "preserve and conserve" GSE assets, suspend allocations that contribute to "financial instability," and put the GSEs in a "sound and solvent condition" or receivership, some argue that FHFA is ignoring statutory obligations.<sup>[14]</sup> Additionally, all net income from the GSEs sweeps to the Treasury Department. HTF payments reduce amounts swept to Treasury, which are meant to compensate taxpayers for the risks they take on by supporting the GSEs.<sup>[15]</sup>

4. Regardless of the decision by FHFA, the unsustainable nature of GSE conservatorship undermines the efficacy of the HTF and discourages housing finance reform.

The HTF's aim (and the reasoning behind putting it outside the regular appropriations process) was to establish a stable, permanent source of funding for affordable housing. Yet using the GSEs as the funding source stands in opposition to that aim. The GSEs' exact future is uncertain, though broad bipartisan and public support exists for their elimination.<sup>[16]</sup> Relying on the GSEs to fund federal programs additionally adds a disincentive for lawmakers to finally tackle housing finance system reform; growing the GSEs would elicit more money for the HTF and CMF despite increased risks to taxpayers.

HTF allocations are expected to proceed sometime in 2016 unless FHFA reverses its decision and suspends allocations. Congress could also act to prevent the HTF allocations from moving forward. Legislation has been introduced in the House of Representatives that would apply GSE dividends toward reducing the federal budget deficit instead of funding the HTF.<sup>[17]</sup>

[1] See <http://www.whitehouse.gov/sites/default/files/omb/budget/fy2016/assets/hud.html> & <http://www.whitehouse.gov/sites/default/files/omb/budget/fy2016/assets/tre.html>