November 2, 2018

Mr. David R. Bean
Director of Research and Technical Activities
Governmental Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, Connecticut 06856

RE: Project No. 26-6

Dear Mr. Bean,

On behalf of the state Housing Finance Agencies (HFAs) it represents, the National Council of State Housing Agencies (NCSHA)\(^1\) appreciates the opportunity to respond to the Governmental Accounting Standards Board’s (GASB) July 30 Exposure Draft outlining proposed standards for the proper disclosure of conduit debt obligations (CDOs) in municipal issuers’ financial disclosures. We thank GASB for addressing the lack of clarity on this issue and working to develop a single definition of conduit debt obligation for federal accounting and financial reporting requirements and common procedures for reporting CDOs. We especially appreciate that GASB engaged with state HFAs and other industry stakeholders throughout the process.

The Exposure Draft’s proposed definition of “conduit debt obligation” is generally clear, accurately describes the characteristics of CDOs, and can easily be applied. NCSHA is particularly pleased that GASB has recognized that many CDOs do not place any real liability or exposure on the bond’s issuer because the debt payments on the bond are solely the responsibly of the-third party obligor that received the funds from the bond sale or placement. The Exposure Draft also does a good job differentiating between those CDOs for which issuers do face potential exposure and those for which they do not. In addition, we feel as if the Exposure Draft establishes a clear procedure for HFAs and other issuers to follow when reporting on CDOs in their financial statements.

However, we are concerned that the Exposure Draft would require HFAs and other issuers to report on all their CDO issuances in their financial disclosures, even those for which they face no exposure. This blanket requirement will increase the burden on issuers while providing little tangible benefit to investors and other market participants. In fact, such reporting could increase investor confusion by implying that CDOs for which the issuer faces no liability

\(^1\) NCSHA is a nonprofit, nonpartisan organization. None of NCSHA’s activities related to federal legislation or regulation are funded by organizations that are prohibited by law from engaging in lobbying or related activities.
could actually impact the issuer’s finances. We urge GASB to consider limiting the mandatory reporting requirement so that it applies only to CDOs for which the issuer could potentially become liable for debt payments, and allow issuers to determine for themselves whether they want to include information on other CDOs.

In addition, we also ask that GASB add language clarifying that pass-through single-family Mortgage Revenue Bonds (MRBs), do not counts as CDOs’ under the Exposure Draft. Finally, NCSHA asks that GASB clarify whether loan guarantees, in addition to bond guarantees, qualify as a limited or additional commitment under paragraph 6.

Tax-Exempt Financing is Critical to HFAs’ Affordable Housing Missions

HFAs are state-chartered housing agencies that operate in every state, the District of Columbia, New York City, Puerto Rico, and the U.S. Virgin Islands. Though they vary widely in their characteristics, including their relationship to state government, they share a common goal of providing affordable housing help to those of their constituents who need it.

The sale of tax-exempt municipal Housing Bonds is vital to HFAs’ affordable housing activities. HFAs utilize MRBs to help working families purchase their first homes. Through multifamily bonds, HFAs finance the development of affordable rental housing that would otherwise not have been built in the private market.

HFAs will often use CDOs to support their affordable multifamily programs, using multifamily bonds to secure financing that goes directly to private and/or nonprofit housing developers that they use to build or renovate affordable rental housing projects. This allows HFAs to take advantage of their partners’ expertise and capabilities to more efficiently support affordable housing development. Some HFAs issue a majority, or even all, of their multifamily bonds as CDOs. In addition, several HFAs whose missions extend beyond affordable housing also issue CDOs to support various economic development and/or healthcare projects.

Reexamine Reporting Requirements for CDOs with no Issuer Exposure

As GASB notes, CDO issuances differ in the amount of liability that issuers face or potentially face. In some cases, issuers and HFAs serve purely as conduits, with no obligation or commitment to pay off debts related to the bond issuance, even if the third-party entity that received the funding from the bond is unable to make its payments. Other CDOs include limited commitments from the issuer that it will cover debt payments on the CDO if the third-party obligor is unable to do so. The Exposure Draft would require issuers to disclose and describe all CDOs, whether or not the issuer has entered into an obligation to cover bond payments, in the Notes section at the end of financial statements. Similarly, issuers will be required to report any CDOs for which they have entered a limited commitment to cover debt payments as a potential liability if the issuer determines that it is “more likely than not” that it will have to support debt payments.
NCSHA agrees that issuers should be required to report information about CDOs for which they have made limited commitments to cover debt payments, as such arrangements represent potential liabilities that could impact issuers’ finances. However, we do not see the value in requiring that HFAs and other issuers provide information on CDOs for which they have made no commitments, and for which the obligor is wholly responsible for paying the debt off. Such CDOs have no material impact on issuers’ financial health, so whatever information provided will be of no relevance to investors and creditors. At the same time, the inclusion of such information could provide the wrong impression, suggesting to investors and others in the market that such CDOs, and the projects they fund, could have an impact on an issuer’s bottom line, despite the issuer having no exposure.

While such disclosures will be of limited value to the market, the reporting could prove burdensome to HFAs and other issuers. As mentioned above, some HFAs use CDOs to finance a large amount of their multifamily lending. Having to report on all of these CDOs, including those for which the HFA has no obligations, will substantially increase the amount of time and resources they have to devote to their financial reporting. This will use up resources that could be better used toward meeting their critical affordable housing and economic development missions.

We urge GASB to amend the proposed guidelines so that issuers must only include in their financial statement information on CDOs for which they have entered into a commitment to make debt service payments. GASB can still allow issuers to report on those CDOs for which they have not entered into a commitment if the issuer chooses to do so.

Clarify Treatment of Single-Family Pass-Through Bond Transactions

When using MRBs to finance their affordable homeownership programs, HFAs utilize a variety of different bond structures depending on market conditions and the needs of their program. One commonly used MRB structure is known as “pass-through”, whereby investors receive principal payments directly associated with a group of home purchase mortgage loans or mortgage backed securities (MBS) on a pro rata basis. Under this structure, payments for an asset (the single-family mortgage loan) held by a third-partly obligor (the borrower) go directly to the bond’s investors. Consequently, NCSHA has learned that some HFAs consider pass-through structured MRBs to be CDOs, and report them as such on their financial disclosures.

NCSHA does not believe that GASB intended to include pass-through MRBs in its definition of CDOs. CDOs generally provide financing to single entities to develop and manage large-scale assets that will fulfill a public purpose. MRBs are used to provide relatively small amounts of financing to hundreds or even thousands of low- and moderate-income borrowers to purchase a home. While helping working families purchase a home is an important public purpose, the actual properties purchased are used only for the benefit of the homebuyers.
NCSHA asks GASB to amend its proposed guidance to make it clear that pass-through MRBs do not fall under the definition of “conduit debt obligation.”

**Clarify Definition of “Guarantee” in Paragraph 6**

Paragraph 6 of the Exposure Draft provides examples of the limited or additional commitments an HFA or other issuers can make to support a bond’s debt service payments while still having the bond qualify as a CDO. One example of an additional commitment is if the issuer chooses to extend a guarantee on the bond in which it pledges to make debt service payments on the bond in the event that the third-party obligor is unable to do so.

It is unclear if this example applies only to guarantees offered on bonds, or to guarantees also provided on the loans that the bond finances. For example, state HFAs have partnered with private builders to issue conduit bonds that develop affordable multifamily housing through the Federal Housing Administration’s (FHA) FHA HFA Risk Sharing program. Under such arrangements, the proceeds from the bond sale are used to finance a multifamily mortgage that receives credit enhancement from FHA, but only for a portion of the loan. The HFA assumes the risk on the remaining portion of the loan.

We ask that GASB clarify whether such arrangements will fall under the definition of CDO.

Finally, we note that in paragraph 5 of the Exposure Draft it states that, in order for a bond issuance to be considered a CDO, the issuer’s commitments have to be limited to those discussed in paragraph 6. Then in paragraph 6 it states that additional commitments are not limited to the examples provided. NCSHA understands that it may not be possible for GASB to put together an exhaustive list of commitments that issuers can extend on a bond issuance and still have it qualify as a CDO. At the same time, we urge GASB to study this matter further and consider if there are any other examples it can list, or further guidance it can provide, so as to provide as much clarity as possible for HFAs and other issuers.

Thank you for your consideration. We would be happy to discuss these issues with you at your convenience.

Sincerely,

Garth Rieman
Director, Housing Advocacy and Strategic Initiatives