



Policy Insight

Expanding Affordable Housing Options: An Overview of Duty to Serve

By Michael Eggleston and Faith Weekly

Key Takeaways

- Over 39 million U.S. households pay more than 30 percent of their income on housing, disproportionately affecting households with low income.
- The Duty to Serve Program (DTS), a component of the Housing and Economic Recovery Act of 2008, requires that Fannie Mae and Freddie Mac increase housing options for people with very low, low and moderate income.
- DTS began implementation in January 2018 and is focused on three markets: manufactured housing, rural housing and affordable housing preservation.

Background

Many factors have been attributed to a lack of housing affordability—stagnant wages, increasing housing costs, the conversion of previously affordable rental units to market rate, reduced demand for low-income housing tax credits (LIHTC) as a result of tax reform, and the tightening of mortgage credit after the Great Recession. An estimated 39 million U.S. households are housing cost-burdened, disproportionately affecting households with low income.¹ The Census Bureau defines housing cost-burdened families as those who pay more than 30 percent of their income for housing. According to the St. Louis Fed's Community Development Outlook Survey in 2016 and 2017, the issue having the greatest negative impact on people living in low- and moderate-income (LMI) communities (other than generational poverty) is the availability of affordable housing. This Policy Insight provides an overview of the Duty to Serve Program (DTS), which began implementation in January 2018.

DTS is an effort by Congress to ensure the government-sponsored enterprises (GSEs)² Fannie Mae and Freddie Mac expand housing options for buyers and renters with low income. Established as the Federal National Mortgage Association (FNMA) by Congress in 1938 as part of Franklin Roosevelt's New Deal during the Great Depression, Fannie Mae's initial purpose was to help improve access to mortgage credit (Freddie Mac—the Federal Home Loan Mortgage Corp. or FHLMC—was established in 1970 for the same purpose). The GSEs do not make loans to individual borrowers; rather they operate in the secondary market, purchasing mortgages originated by financial institutions. The increased liquidity in the housing mortgage market provided by the GSEs intends to ensure that individuals and families who buy homes and investors who purchase apartment buildings and other multifamily dwellings have a continuous, stable supply of mortgage money.

In 2008, Congress passed the Housing and Economic Recovery Act (HERA), part of which amended the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 to impose certain new requirements on the GSEs. The statute stipulated that the Federal Housing Finance Agency (FHFA) shall oversee the GSEs’ efforts in developing loan products and flexible underwriting guidelines to facilitate a secondary market for mortgages for very low-, low- and moderate-income families with respect to three underserved markets—manufactured housing, affordable housing preservation and rural housing. In particular, HERA required the FHFA director to establish, effective for 2010 and thereafter, a manner for evaluating whether, and the extent to which, the GSEs have complied with their duty to serve these underserved markets and for rating the extent of such compliance.

Based on HERA requirements, FHFA went through a full rule-making process for DTS in 2009. However, FHFA did not issue a final rule on the program until December 2016, partly due to a new rule proposed for DTS in December 2015. Throughout 2017, the GSEs proposed their plans for how they would meet their requirements under the program, solicited public feedback and then finalized their plans. FHFA approved both plans in December 2017 and program implementation commenced on January 1, 2018. Figure 1 provides a timeline of DTS from implementation through FHFA’s submission of its first annual report on the program.

Figure 1. Timeline for execution of GSE plans for implementation of Duty to Serve.



HERA stipulated the three markets that make up DTS—manufactured housing, affordable housing preservation and rural housing (Table 1).

Table 1. Duty to Serve Markets		
Type of DTS Market	Definition	Context
Manufactured Housing	“Manufactured home” means a structure, transportable in one or more sections, which, in the traveling mode, is eight body feet or more in width or 40 body feet or more in length, or, when erected on site, is 320 or more square feet, and which is built on a permanent chassis and designed to be used as a dwelling with or without a permanent foundation when connected to the required utilities, and includes the plumbing, heating, air conditioning and	There is a lack of a secondary market, particularly for manufactured housing titled as personal property. Financing tends to be more expensive for manufactured housing titled as real estate. This lack of liquidity and higher pricing has inhibited the growth of manufactured housing as a viable, affordable housing option.

	electrical systems contained therein; except that such term shall include any structure that meets all the requirements of this paragraph except the size requirements and with respect to which the manufacturer voluntarily files a certification required by the Secretary and complies with the standards established under this chapter; and except that such term shall not include any self-propelled recreational vehicle.	
Affordable Housing Preservation	The final rule provides that enterprise activities eligible to be included in a plan under the affordable housing preservation market are activities that facilitate a secondary market for mortgages on residential properties for very low-, low- or moderate-income families consisting of affordable rental housing preservation and affordable homeownership preservation.	The Low Income Housing Tax Credit is the largest supply-side affordable housing subsidy in the nation.** This program, established in 1986, is structured to ensure that housing units remain affordable for 15 years, while some states and municipalities have provisions that require the units to remain affordable for a greater period of time. This has resulted in housing units that were once affordable converting to market rate.
Rural Housing	<p>“Rural area” means:</p> <ul style="list-style-type: none"> (i) A census tract outside of a metropolitan statistical area (MSA) designated by the Office of Management and Budget (OMB) (ii) A census tract in an MSA as designated by OMB that is outside of the MSA’s urbanized areas as designated by USDA’s Rural-Urban Commuting Area (RUCA) Code #1, and outside of tracts with a housing density of over 64 housing units per square mile for UDSA’s RUCA Code #2.* 	The GSEs’ business model is designed to develop products and purchase loans at large economies of scale. They have been less involved in rural communities, where there are fewer people and, thus, it may be more difficult to achieve scale.

* To download the census tracts eligible in rural areas, visit the [FHFA Duty to Serve data webpage](#).

** Federal Reserve Bank of Atlanta (2017). “Financing Affordable Housing with the LIHTC.” Retrieved from <https://www.frbatlanta.org/community-development/publications/partners-update/2017/02/170425-financing-affordable-housing-with-the-lihtc.aspx>

There are activities stipulated through statute (HERA) and through regulation that the GSEs must consider as part of DTS—at least four regulatory activities for the manufactured housing market, seven statutory or regulatory activities for the affordable housing preservation market, and four regulatory activities for the rural housing market (Table 2).

Table 2. Duty to Serve Activities			
Activities	Manufactured Housing	Affordable Housing Preservation	Rural Housing
Statutory Activities	None	1. Housing Choice Voucher Program (Section 8)	None

		<ol style="list-style-type: none"> 2. Preservation Program (Section 236) 3. Mortgage Insurance for Rental and Cooperative Housing (Section 221(d)(4)) 4. Supportive Housing for the Elderly Program (Section 202) 5. Supportive Housing for Persons with Disabilities (Section 811) 6. Homelessness Assistance 7. Rural Rental Housing Loans (Section 515) 8. Low Income Housing Tax Credit Debt 9. Comparable state and local programs 	
Regulatory Activities	<ol style="list-style-type: none"> 1. Manufactured homes titled as real estate 2. Manufactured homes titled as personal property 3. Manufactured housing communities owned by government instrumentalities, nonprofits or residents 4. Manufactured housing communities with specified tenant pad lease protections 	<ol style="list-style-type: none"> 1. Small multifamily rental properties financing 2. Multifamily energy- or water-efficiency improvements financing 3. Single-family energy- or water-efficiency improvements financing 4. Affordable homeownership preservation 5. HUD's Choice Neighborhoods Initiative 6. HUDS's Rental Assistance Demonstration 7. Purchase and rehabilitation financing of distressed properties 	<ol style="list-style-type: none"> 1. Housing in high-needs rural regions 2. Housing for high-needs rural populations 3. Rural small financial institution financing of rural housing 4. Rural small multifamily rental properties
Extra Credit Eligible Activities	<ol style="list-style-type: none"> 1. Manufactured homes chattel pilot initiative 2. Manufactured housing communities with tenant pad lease protections located in states without comparable consumer protections 3. Residential economic diversity 	<ol style="list-style-type: none"> 1. Residential economic diversity 	<ol style="list-style-type: none"> 1. High-needs rural populations (only very low-income families, income \leq 50 percent of area median income) 2. Residential economic diversity
Additional Activities	The GSEs may propose additional activities for each underserved market		

The statute requires FHFA to annually evaluate and rate the GSEs on their DTS achievements and to report annually to Congress on FHFA's evaluations. The evaluations will consist of a three-step process: a quantitative assessment, a qualitative assessment and a potential upward adjustment based on certain eligible activities. The evaluation will result in a separate rating for each of the three underserved markets. The rating scale consists of the following:

- Fails
- Minimally Passing
- Low Satisfactory
- High Satisfactory
- Exceeds

The ratings will be made publicly available, though FHFA does not possess enforcement authority should the GSEs receive a low rating.

Key Players

In addition to homebuyers, homeowners and renters, there are many organizations and government agencies that will be directly or indirectly impacted by DTS at the local, state and federal level. Below is a list of some of the organizations and agencies that may be impacted by DTS. Please note that this is not an exhaustive list.

Federal and Quasi-Governmental Agencies

- Federal Housing Finance Agency — As the regulator for the GSEs, FHFA oversees implementation of the program and will be rating the GSEs on their performance.
- Fannie Mae and Freddie Mac — The GSEs will be responsible for increasing housing options for low- and very low-income individuals and households in the three target markets by creating products and purchasing loans on the secondary market.
- Department of Housing and Urban Development (HUD) — This federal government agency, which has field offices located throughout the U.S., oversees and funds a variety of efforts that promote affordable housing. This includes many programs, such as Section 8, that are called out in HERA, the law that created DTS.
- Department of Agriculture (USDA) — Similar to HUD, USDA has field offices throughout the U.S. It oversees and funds a variety of programs, including many that support rural housing.

State and Local Agencies

- State Housing Finance Agencies — These agencies oversee a variety of affordable housing programs, including locally administering LIHTC.
- Local Housing Authorities — These authorities administer some of the largest housing subsidy programs in the U.S., including Section 8.

Private and Nonprofit Sectors

- Banks — Banks have an obligation under the Community Reinvestment Act to meet the credit needs in LMI communities. Many have done so over the past several decades through loans and investments in affordable housing.
- Community Development Financial Institutions (CDFIs) — As mission-driven lenders, these organizations have played many roles, including lender, investor and syndicator of tax credits, all in support of affordable housing.

- Affordable Housing Developers — Developers will be impacted as the GSEs are considering re-entering the LIHTC market as investors.
- Community Development Corporations (CDCs) — These organizations have traditionally developed affordable housing as well as provided homeownership counseling. In addition to seeing more LIHTC investor demand, they may also be impacted as the GSEs look to bolster homeownership education initiatives.
- Regional and National Intermediaries — These organizations, which are often trade associations and/or CDFIs, advocate on behalf of the target markets under DTS. Examples include but are not limited to the National Low Income Housing Coalition (affordable housing preservation), Housing Assistance Council (rural housing) and ROC USA (manufactured housing).
- HUD-certified Homebuyer and Credit Counseling Agencies — Often these organizations are affiliated and/or located within a financial institution or nonprofit organization, but they may also be standalone entities.

Conclusion

Increasing access to mortgage credit and providing additional housing options for individuals and families with very low-, low- and moderate-income has the potential to increase a household's opportunity for economic mobility and resiliency, particularly at a time when so many households and families are housing cost-burdened. For the GSEs to reach their DTS targets, it will require innovative approaches, including partnering with entities that have experience in, local trust of, and insight into these three markets.

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Policy Insight is a product of the St. Louis Fed's Community Development department, sharing analysis and ideas about the issues and opportunities that impact the economic resilience and mobility of low- and moderate-income and underserved communities.

¹ www.urban.org/urban-wire/low-income-homeowners-are-burdened-housing-costs-renters

² Since Sept. 6, 2008, Fannie Mae and Freddie Mac have operated under conservatorship by the Federal Housing Finance Agency.

