

Alfred M. Pollard, General Counsel
Attention: Comments/RIN 2590-AA26
Federal Housing Finance Agency
Fourth Floor
1700 G Street, NW
Washington DC 20552

April 12, 2010

Re: Enterprise Affordable Housing Goals; Enterprise Book Entry Procedures, (RIN) 2590-AA26

Dear Mr. Pollard:

We respectfully submit these comments on the Federal Housing Finance Agency's (FHFA) proposed rule 12 CFR Part 1282, RIN 2590-AA26, concerning the housing goals for Fannie Mae and Freddie Mac for 2010 and 2011. These comments are submitted on behalf of the Center for Responsible Lending; Consumer Federation of America; National Consumer Law Center; National Council of La Raza; and the National Fair Housing Alliance.

As national housing, civil rights, and consumer organizations we have a strong interest in promoting effective policies that help expand affordable home purchase and rental housing. The affordable housing goals for the GSEs are an important driving factor in making home mortgage credit available, especially to low income and minority households, and low income and underserved communities.

In general, we support the proposed rulemaking. The legislative changes in the goals structure enacted in the Housing and Economic Recovery Act of 2008 marked a significant restructuring of the goals, based on more than a decade of experience. We are pleased to see FHFA implementing these changes, in particular with regard to the enhanced definitions of low income and very low income; the definition of "underserved areas"; the separation of single family and multifamily goals; the counting of mortgages rather than units in the single family goals; and the separation of purchase money and refinance mortgages.

As the proposed rule elaborates, the housing market in 2010 is very different from the markets under which previous housing goals were promulgated. The collapse of the private label securities market has concentrated mortgage funding in the GSEs and in FHA. While this has significantly limited the marketing of unsafe and unsustainable loans to consumers, it also has caused nearly every part of the mortgage finance chain to tighten underwriting standards. Some of these changes were long overdue.

But it is very important not to let the misdeeds of some actors in some segments of the market overshadow the very real accomplishments of more than 30 years of experience with expanding home financing to previously underserved populations. This is especially important for minority homebuyers, who have faced historical patterns of discrimination in the terms on which loans were offered and the

manner in which they were marketed, and who became some of the hardest-hit victims of predatory and unsafe lending practices. These families also frequently have less history with homeownership and the asset building that it has long provided American families. They also have suffered from discrimination in employment, leading to much lower levels of household wealth, particularly in the African-American and Hispanic communities, than in non-minority ones. We remain concerned that this rulemaking not unduly threaten the continued ability of these borrowers to obtain credit on fair and reasonable terms either through goals that do not stretch the Enterprises or through assumptions about the market that discount or prejudice responsible, fully documented lending to low wealth families or those with non-traditional credit histories.

The proposed rule notes these changes in underwriting standards, including higher down-payment requirements, lower overall debt ratios, and higher standards for demonstrated credit payment history. We strongly support sound underwriting that results in sustainable mortgages. We also believe that many households were well served by changes in underwriting practice over the last 20 years that lowered required down payments and adopted alternative forms of demonstrating creditworthiness. These changes were driven in part by earlier promulgations of housing goals for the GSEs.

While some practices, like piggy-back second liens, qualifying borrowers using low, teaser rates rather than the full reset value of adjustable rate mortgages, and interest-only features clearly exacerbated both the rapid rise in house prices and the high failure rates in mortgages in the earlier part of this decade, there is compelling evidence that fully documented, fully amortizing loans with low down payments and without such risky features as pre-payment penalties and yield spread premiums, made to borrowers with reasonable but not spotless credit, histories performed very well even through the crisis.¹

It is important for FHFA to set the housing goals at levels that are realistic and prudent. But FHFA could provide much more clarity about the performance of a range of products that were offered in the past by the Enterprises with particular focus on goals-qualifying households through the wealth of data to which it now has access. The proposed rule notes that the Enterprises purchased private label subprime and Alt-A securities “...in response to declining market share and in pursuit of higher profits...for the yield and, in certain instances, to satisfy specific housing goals and subgoals.” It further notes that “The results of providing large-scale funding for such loans were adverse to borrowers who entered into mortgages that did not sustain homeownership and for the Enterprises themselves.”

We strongly agree that the proliferation of unregulated, poorly structured and poorly understood private label securities was a key driver in the inflation and subsequent collapse of house prices. Many households were provided unsafe and unsustainable mortgage products as a result. But the proposed rule unfortunately lacks any analysis of the results of more prudent lending that emphasized lower down payments and nontraditional measurement of credit histories that were the cornerstones of much

¹ *Risky Borrowers or Risky Mortgages: Disaggregating Effects Using Propensity Score Models*, Working Paper, Center for Community Capital, November, 2009

of the experimentation driven by the Enterprises' goals in earlier years. For instance, HUD's analysis of the GSEs' housing goals performance 2004-2005 documents that more than 90 percent of Fannie Mae's goals qualifying single family purchase money units in those years were financed using "traditional" mortgage originators and products.²

We urge FHFA to undertake and publish research on the performance of loans that were financed by the Enterprises during the 1993-2006 period that met the housing goals. In particular, we urge FHFA to focus on products developed by the Enterprises, primary market lenders and other intermediaries such as CDFIs and credit unions to reach low-wealth and low income borrowers. This information is critically needed as stability returns to the mortgage finance system and the Enterprises once again will be expected to shoulder their fair share of financing for previously underserved populations.

Likewise, the availability and cost of rental housing remains a serious concern in the communities we represent. Despite the glut of foreclosed homes and weakness broadly in the rental housing market, affordable rental homes for very low, low and moderate income families remain in extremely short supply. Mortgage credit is not the only variable affecting this situation. The lack of subsidies – through Section 8 Vouchers, or Low Income Housing Tax Credits, or mortgage revenue bonds – has meant that fewer affordable units are being created or preserved. Nevertheless, assuring the availability of long-term affordable mortgage financing for rental homes remains a very high priority. This proposed rule is an important contribution to assuring that continued funding.

The proposed rule poses a series of specific questions about the structure and execution of the goals process. This comment letter will address a major issue that should be added to the proposed goals process and then addresses the specific items in the order in which they appear in the proposed rule.

Affirmatively Furthering Fair Housing

Section 808(d) of the Fair Housing Act states that "All executive departments and agencies shall administer their programs and activities relating to housing and urban development (including any Federal agency having regulatory or supervisory authority over financial institutions) in a manner affirmatively to further the purposes of this subchapter and shall cooperate with the Secretary [of Housing and Urban Development] to further such purposes." The Fair Housing Act was passed in 1968 to eliminate segregation and housing discrimination, both of which have resulted to a certain extent from past laws and government policies. Overcoming these problems requires comprehensive and coordinated government action,³ which is why the Fair Housing Act requires all federal programs and

² HUD Working Paper HF-018, *The GSEs' Funding of Affordable Housing Loans, 2004-2005*. P. 12

³ James Carr and Nandinee Kutty write, "The severe level of...segregation, and isolation resulting from those policies have created a complex web of socio-economic challenges that defy piecemeal and uncoordinated intervention. These problems are growing. As these problems grow, they increasingly take on grave significance for the nation beyond the sole issue of social justice." *Segregation: The Rising Costs for America*, edited by James Carr and Nandinee Kutty. New York: Routeledge, 2008, 2-3.

agencies, and in particular regulatory agencies, to “affirmatively further fair housing,” and work to overcome segregation and discrimination. Thus, FHFA must insure that the entities it oversees, namely the Enterprises, carry out their programs in a manner that affirmatively furthers fair housing. It is imperative that the process establishing the goals include a review and consideration of their likely impact on fair housing outcomes, particularly any discriminatory or disparate impact on protected classes under the Fair Housing Act. Moreover, the goals must be evaluated to insure that they will further the purpose of the Fair Housing Act to both eliminate illegal housing and lending discrimination and to promote stable and diverse communities. Finally, evaluation of the fair housing implications of the Enterprises activities must be included in the overall review of their performance against the housing goals.

Benchmark vs. Market Performance

The rule proposes to establish benchmark levels of performance for the Enterprises in the single family purchase money and refinancing goal, but to measure performance against both the prospectively set benchmark and actual market performance as measured by independent market data. We agree with this approach and believe it will help FHFA more effectively match Enterprise performance to actual market conditions. When combined with the statutory requirement to consider the previous three years of Home Mortgage Disclosure Act (HMDA) data in assessing the market, this dual approach should help establish a reliable set of assumptions against which the Enterprises can operate.

The housing goals establish a minimum level of effort that the Enterprises should meet in fulfillment of their charter responsibilities. They should be regarded as a floor that will assure that these secondary market entities do not discriminate against the targeted communities through their pricing, acquisition, and securitization strategies. As such, it is important that they be set at a level that is reasonably tied to market conditions. Performance should be based on not only the benchmark number that is forecast years before actual market conditions are known, but also on those actual conditions.

FHFA now has additional authorities to enforce a “duty to serve” in a number of critical areas. This authority should augment rather than replace the housing goals requirements, with the latter forming a floor and the former offering additional incentives and mandates to address specific additional needs in the market.

Leading the Market

We strongly support the language in Section V. A(4) of the proposed rule regarding “The ability of the Enterprises to lead the industry in making mortgage credit available.” First, the rule recognizes that the Enterprises at present “have played a leading role in sustaining the mortgage market during the recent crisis.” In particular, the rule notes elsewhere that “...in 2009 they not only led the multifamily market, they effectively were the market.”

We particularly support FHFA's interpretation of Congress' direction for the Enterprises to "lead the market" as including not only the housing goals themselves but the other actions and investments the Enterprises can make to assist in identifying, establishing and expanding parts of the housing market that might be neglected or overlooked. Of course one of the areas in which we fully expect the Enterprises to be market leaders is fair housing/lending. We also agree that "leading the market" should encompass non-mortgage investments in activities such as housing counseling, mortgage modifications and loss mitigation, technology and marketing, especially in helping primary market lenders to market responsible and sustainable mortgage products to low and moderate income consumers and communities, and to people and communities of color.

With respect to loss mitigation, in the current environment of widespread foreclosures, the Enterprises could and should play a critical leadership role by requiring their servicers to adopt a set of best practices. These should include, among other things, a stop on all foreclosure actions while delinquent loans are being reviewed for various loss mitigation options, an emphasis on home-saving loss mitigation steps, and the use of principal reduction to both reduce the likelihood of redefault and increase the affordability of the mortgage payment for the borrower.

Sustainable Mortgages

FHFA seeks comment in Section V. A(6) on defining "sustainable mortgage products" for purposes of determining eligibility for housing goals credit, and specifically on possible alternative means of doing so. One alternative discussed would use historical data on cumulative default rates, and Enterprise models of future performance, to determine sustainability.

In theory, historical and modeled data on the likely performance of loans with particular features could provide a useful and easily measured benchmark for establishing whether or not a loan is sustainable. However, such an approach would only be useful to the extent the models are reliable and reflect likely market conditions over some length of time. As recent history has shown, some mortgages might have performed and modeled very well in market conditions that prevailed from 1994-2004, but newer mortgages made on the same terms might have fared much more poorly in the weakened economic and house price environment of later years. Similarly, loans made today in a deflated housing market might prove to perform significantly better than models based on the worst years of the housing recession would indicate.

Historically, employment rates and the direction and magnitude of house price increases are likely to have a significant impact on loan performance regardless of features and modeled outcomes. These are notoriously hard to predict, contributing to our discomfort with using modeled CDR's as a means of determining sustainability.

We urge caution in the application of such modeled performance factors. We also reiterate the value of FHFA examining and publishing information on the performance over time of specific products developed by the Enterprises and other market participants over the last two decades to provide a

context for understanding how certain features in otherwise fully documented and underwritten loans performed in a range of market conditions.

We also urge that FHFA focus on mortgage features and process attributes at least as heavily as on models of forecasted performance. We recommend that all loans with the following features be explicitly excluded:

1. low teaser rates;
2. qualifying borrowers for less than the maximum payment, using the maximum interest rate on adjustable mortgages;
3. adding unnecessary fees or restrictions like prepayment penalties and yield spread premiums;
4. reduced documentation of income;
5. interest-only;
6. any mortgage the terms of which would lead to negative amortization;
7. the presence of piggy-back second liens;
8. as well as other features that became prevalent in the later years of the housing boom.

We believe that flexible underwriting guidelines in matters like loan-to-value ratios and credit history remain critically important for the availability of mortgage credit in minority and low income communities and that the Enterprises can learn from and apply lessons learned over the last 20 years of increasingly flexible mortgage underwriting.

We encourage FHFA to consider the wealth of knowledge held by community development financial institutions. FHFA should pay attention to mortgage products and features as well as underwriting practices developed by this market segment as it may hold quite valuable information that would enhance FHFA's understanding of what promotes the origination of sustainable mortgages.

The rule also proposes to require the Enterprises to follow the Interagency Guidelines for responsible lending, in a further effort to restrict the types of mortgages that can be counted toward the housing goals, and for which the Enterprises can provide liquidity. We strongly support this related requirement, but note that the current regulatory guidance may not be sufficient, and future regulatory guidance may also not meet the necessary standards. As a consequence, we urge FHFA to monitor any changes that might be made to current regulatory guidelines and act quickly and independently to maintain high standards in the Enterprises regardless of what course of action primary market regulators might take. The history of consumer protection within the bank regulatory agencies and their willingness to step in to stop abusive practices in a timely manner is not encouraging. We do not believe FHFA should surrender its independent authority to restrict the Enterprises from engaging in abusive and unsafe lending practices.

Multifamily Subgoal for Very Low Income Families

We support the establishment of a multifamily housing subgoal for very low income families. However, we also note that increasing the Enterprises' performance in this area may be very difficult without a

significant increase in the availability of housing subsidies through which rents can be made affordable to families with incomes at or below 50 percent of the area median. There is a several-fold difference nationally between the number of renter households at this income level and the number of rental units affordable to them. Mortgage financing alone is a very weak tool through which to effect significant reductions in rent levels.

In this regard, we urge FHFA to fully count all qualifying units where the Enterprises assist in the preservation of existing units that meet the income tests,, consistent with FHFA's proposed rules on "duty to serve" requirements for the GSEs.

The proposed rule's inclusion of purchases of mortgage revenue bonds that meet certain reasonable conditions is important and helpful. These bonds are often a major source of lower-cost capital for the preservation and construction of affordable rental housing units.

Small Multifamily Units

The proposed rule seeks comment on the establishment of a subgoal for investments in low income units in small (5-50 units) properties in the future. The proposed rule notes many of the obstacles that the Enterprises historically have faced in succeeding in this market. But the vast majority of renters live in smaller properties. It is especially troubling to see Freddie Mac's "virtual exit" from this market, as described in the proposed rule. We support establishing a rule to insure that both Enterprises devote energy and resources into providing liquidity for smaller multifamily loans. We strongly endorse the proposed rule's admonition that "...FHFA expects Freddie Mac's board of directors and new senior management team to assess Freddie Mac's business model with respect to multifamily housing."

We note also that the proposed small multifamily provision would not address the significant number of rental homes that are in single family buildings. Many renters live in such properties, some in single unit structures and many others in 2-4 unit homes. The proposed rule specifically excludes mortgages financing rental units in 1-4 unit homes from the single family goals calculations. The rule proposes that FHFA continue to monitor GSE performance in serving this market. We are concerned that this exclusion could lead to a reduction in financing, through lack of attention or through overly strict underwriting guidelines that could jeopardize the availability and affordability of such rental units for low and moderate income families. It could also reduce the wealth building impacts that ownership and rental of 1-4 unit homes can provide in minority communities. Anecdotal evidence from the Gulf Coast area suggests that many landlords, including many African-American owners, rented out homes that they had inherited or otherwise obtained, increasing their assets and income and preserving a valuable stock of affordable rental homes. FHFA should consider how to measure GSE performance in this sector going forward and report on changes in Enterprise participation in this market as they are observed.

Setting the Multifamily Goals

The proposed rule notes in Section VI(B) that reliable data for multifamily originations is “less certain” than in the single family area. This has been true for many years and has complicated efforts to calibrate the Enterprises’ housing goals in this area. We urge FHFA to collaborate with HUD to reinvigorate former data collection and publishing efforts that provided a more complete and contemporaneous picture of multifamily rental housing loan activities, and where necessary to develop new ones. Especially in light of the single family market’s collapse and the renewed focus on the importance of balanced housing policy, the lack of effective data on the multifamily mortgage market is a serious problem.

We note that the a sizeable number of occupied multifamily rental properties are facing potential difficulties in renewing expiring debt because of lower property valuations and tightened underwriting standards. Failure to meet capital requirements or more conservative underwriting tests could prevent properties from obtaining new financing. FHFA should consider counting modifications of existing loans for units that serve goals-qualifying units as mortgage purchases for purposes of the goal to encourage the Enterprises to extend and modify the terms of existing mortgages, defer payments for a limited period of time, or refinance under more favorable terms.

Manufactured Housing

The rule proposes not to permit the counting of loans extended to personal property manufactured housing loans, “pending future review.” We strongly support this exclusion.

Private Label Securities

The proposed rule describes in Section VII(E) that the rule would exclude all private label securities from counting for purposes of the affordable housing goals. We support this exclusion.

Second liens and HECMs

The proposed rule would exclude from both the numerator and denominator all Home Equity Conversion Mortgages (HECMs) and second liens, based on statutory direction to include only “conventional loans” in assessing goals performance. The rule would not prohibit the Enterprises from acquiring interests in such loans, but would not permit them to be counted for housing goals purposes.

We are concerned about the impact of the proposed decision not to count GSE-funded HECMs in light of recent developments in the reverse mortgage market. That market has shifted dramatically. We want the GSEs to be invested in the development of safe, low-cost HECMs. As has become apparent with the recent dramatic shift in the HECM market, current consumer protections for seniors who obtain HECMs are not adequate.

Where Fannie Mae had been the primary secondary market purchaser of HECMs, Ginnie Mae is now purchasing a significant majority of HECMs—approximately 70%—and these mortgages are originated as fixed rate mortgages in which the homeowners are required to take the full lump sum at closing. In comparison, only a year ago credit lines predominated with only about 50% taken as an upfront draw. The fixed rate product compares unfavorably to the traditional Fannie Mae funded HECM whose adjustable rate credit line enabled homeowners to withdraw funds as financial needs arose. The fixed rate product is both more expensive and more susceptible to abusive cross selling of unnecessary financial products. For this reason we believe it is important to encourage the origination of more flexible adjustable rate line of credit HECMs and other lower cost products through through affordable housing goals.

Reverse mortgages can be an important part of effective asset planning for seniors, when provided with adequate counseling, disclosures and other important consumer protections, although we believe FHFA, HUD and others should conduct research to ascertain the full impact of these products on older homeowners' financial well being. As the nation ages and more and more homeowners find themselves potentially house-rich and cash-poor, reverse mortgages may become a larger part of the market. We urge FHFA to reconsider and, perhaps, provide a fuller explanation of their reasoning for excluding these loans from the goals.

We appreciate the opportunity to comment on this important proposed rule.

Sincerely,

Center for Responsible Lending
Consumer Federation of America
National Consumer Law Center
National Council of La Raza
National Fair Housing Alliance