MORTGAGE BANKERS ASSOCIATION

March 17, 2016

Alfred M. Pollard
General Counsel
Federal Housing Finance Agency
400 7th Street, SW
Washington, D.C. 20024

Subject: Comments on Duty to Serve Proposed Rule - RIN 2590-AA27

Dear Mr. Pollard:

The Mortgage Bankers Association (MBA)[1] thanks the Federal Housing Finance Agency (FHFA) for the opportunity to comment on the proposed rule (the Proposal) to implement the Duty to Serve requirements imposed on Fannie Mae and Freddie Mac (the GSEs) by the Housing and Economic Recovery Act of 2008 (HERA).[2] FHFA previously issued a proposed rule for notice and comment in 2010, the responses to which have helped inform the current Proposal.

Duty to Serve is an important element of the GSEs' role in the market. At the start of the financial crisis, Congress recognized the need to strengthen the powers of the GSEs' regulator, underscoring the expectation that they provide liquidity and stability to the national housing market in a safe and sound manner. Congress also took the opportunity to add a Duty to Serve underserved markets to the GSEs' Affordable Housing Goals and Affordable Housing Trust Fund obligation, reinforcing that the GSEs have an obligation to ensure liquidity in the financing of affordable housing for very low-, low-, and moderate-income families. MBA supports the GSEs' Duty to Serve mandate and believes the Proposal represents notable progress toward serving underserved markets.

More specifically, MBA believes the GSEs' role as secondary market investors can be amplified under this Proposal through the explicit encouragement of the GSEs ability to leverage their secondary market role in the assessment of new product opportunities. This can be achieved through either the expansion or increase in the relative weight and

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[1] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 280,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,200 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, REITs, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mortgagebankers.org.

[2] *See* HERA § 1129.

scope of new product development and the facilitation of shared market knowledge by the GSEs with the broader industry.

To ensure inital implementation is successful, MBA recommends FHFA direct the GSEs to incorporate products and programs previously or currently under development, maintain flexibility in grading the GSEs progress, and ensure plans are drafted in a way that can be easily and accurately communicated through the GSEs' Guide framework. MBA believes successful implementation will provide an opportunity to demonstrate how the GSEs can serve underserved markets through viable and measurable activities.

BACKGROUND

The Duty to Serve was enacted as part of HERA in an effort to explicitly define the GSEs' expected role in facilitating a broad, liquid, and stable national housing market accessible to all credit-worthy borrowers. However, HERA does not expand FHFA's authority with regard to underserved markets nor does it allow for numerical targets, which are elements of the GSEs' Affordable Housing Goals. The absence of numerical goals, while affording qualitative flexiblity in determining how best to fulfill the Duty to Serve, have made it more difficult for FHFA to implement and measure progress. Given these considerations, MBA applauds FHFA for remaining faithful to the statute and offering a reasonable framework for accountability through its Proposal.

The statute requires the GSEs to "provide leadership to the market in developing loan products and flexible underwriting guidelines"[3] that serve target markets.[4] The Proposal would implement this mandate by requiring the GSEs to establish three-year Underserved Market Plans to detail how they intend to serve very low-, low-, and moderate income borrowers in these target markets.[5] Consistent with Section 1129 of HERA, the target markets are: Manufactured Housing, Affordable Housing Preservation, and Rural Areas.

Under the Proposal, the GSEs would be able to serve these markets through approved activities identified in their Underserved Market Plans. Activities specifically identified in HERA or in the Proposal are designated as Core Activities. All other activities identified in a Plan are designated as Additional Activities. While the GSEs will not be required to undertake all Core Activities, these Activities must be addressed in their Underserved Market Plans to explain how a Core Activity will be undertaken or why it will not be undertaken. Extra credit will be granted for any Activity that facilitates affordable

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[3] We applaud FHFA's inclusion of the requirement that the GSEs "conclude assessment of leveraging alternate or updated credit scores for underwriting … and, as appropriate, plan for implementation" in its 2016 Scorecard. We believe that providing mortgage underwriters the flexibility to use newer and more inclusive credit scoring models than those currently required by the GSEs would advance the goals of the GSEs statutory Duty to Serve. This will provide increased access to mortgage credit for many potential mortgage applicants who are currently unscoreable using the currently required scoring models.

[4] HERA § 1129 (12 U.S.C. 4565(a)). Separately, HERA requires FHFA to ensure that this mandate is met, even if it requires accepting below-market returns relative to other business activities. (§ 1102).

[5] As identified in 12 U.S.C. § 4502.

housing opportunities in “high opportunity” areas or mixed-income housing in areas with concentrated poverty (Diversity Activities).

Approval of the Underserved Market Plans would be exercised by FHFA after a period of public review and the issuance of a “non-objection” to the Plan by FHFA. Following approval, FHFA would continue to monitor and review GSE progress and score performance.

Due to the significant differences in the way the Proposal suggests fulfilling the Duty to Serve through single-family and multifamily activities, our comments will address each separately.

SINGLE-FAMILY COMMENTS

MBA supports FHFA’s Proposal as a positive step toward improving the availability of mortgage credit in underserved markets. The Proposal strikes a balance consistent with the statutory mandate; while strongly encouraging the GSEs to undertake activities identified by Congress and FHFA as fulfilling the spirit of the Duty to Serve mandate, it recognizes that some programs may not be workable at times. Most encouragingly, the Proposal allows the GSEs the freedom to develop Additional Activities, leveraging the enterprises’ substantial role in the market to aid or spur the innovation of new products and services.

MBA believes the GSEs’ role as secondary market investors can be maximized under the Proposal by further emphasizing their research and development capabilities and robust data libraries to spur innovation by lenders. Under the Proposal the GSEs may propose or develop new products or activities to FHFA for consideration to receive Duty to Serve credit. This option is an important component of the Proposal that allows the GSEs to increase their impact in the three underserved markets. As the dominant investors in single-family mortgages, the GSEs have unique insight into the market dynamics and technical factors that would aid lenders and others[6] in developing successful products that serve the target markets. To advance these opportunities, FHFA should consider expanding the scope or increasing the relative weight of this Activity. FHFA should also explicitly encourage the GSEs to leverage their secondary market role to share historical data and analysis with the primary market, engage with lenders to assess new product opportunities, and conduct related research for underserved markets.

Utilizing the GSEs to aid and facilitate primary market research and development not only leverages the enterprises’ role as core secondary market participants, but provides a ready outlet once viable products are identified and rolled-out by lenders. Through this collaborative process, the market for successful products can gain liquidity more quickly due to a mutual understanding of the details and structure. In this way, the Proposal will best accomplish the balance required of FHFA in enforcing the Duty to Serve mandate while also responsibly managing the GSEs’ resources under conservatorship. This

[6] Including, for instance, non-profits or state housing finance agencies.

approach would also minimize reliance on the nuances of the scoring methodology during the initial years of implementing the final rule.

As the GSEs learn and develop new approaches and practices, MBA asks that FHFA consider awarding Duty to Serve credit for activities that foster the sharing of market knowledge with the broader industry. Under the Outreach Assessment Factor, Duty to Serve credit could be awarded for engagement with lenders on new approaches or for the facilitatation of partnerships between lenders and other market participants such as affordable housing developers. Emphasizing these activities will further encourage the GSEs to share market knowledge with lenders to encourage new approaches and practices that can expand mortgage credit in target markets.

FHFA Should Give Consideration to Issues of Implementation

FHFA should take care to ensure that it gives due consideration to implementation issues as it evaluates the various comments it will receive from stakeholders. In this vein, MBA highlights the following issues.

First, MBA strongly recommends that FHFA direct the GSEs to incorporate any programs or products that have been or are currently under development that would further the GSEs' Duty to Serve mission in their first Underserved Market Plan. The initial years of any program are necessarily subject to a learning curve. By directing the GSEs to include current product development, FHFA will increase the likelihood of initial success by favoring the release of programs or products that are closer to market and have demonstrated sufficient viability to warrant on-going research and development efforts. This will help give the GSEs credit where due, while also ensuring that the target markets can be served as readily as possible.

Second, FHFA should be flexible in grading the GSEs' progress against an Underserved Market Plan in order to account for subtleties that may not be captured in raw purchase data. For instance, and particularly in the initial period after implementation, the GSEs may not experience significant increases in loan purchases. However, consistent with MBA's outreach recommendation above, the GSEs may have nonetheless made material progress in executing against their goal. As secondary market actors, the GSEs may not necessarily purchase every loan developed and originated as a result of their outreach to lenders and the GSEs should not be penalized for this outcome. FHFA should take care that its grading of the GSEs' progress include follow-on monitoring where success could manifest or continue after the conclusion of an Underserved Market Plan.

Finally, it is critical that FHFA ensure that the GSEs' Underserved Market Plans, especially those related to product or program development, be drafted in a way that can be easily and accurately communicated through the GSEs' Guide framework. Lenders who originate loans to sell to the GSEs as part of the Duty to Serve effort need to be able to rely on a clear, transparent product and/or program framework in order to lend with confidence. As a corrolary, FHFA should ensure that the Underserved Market Plans are developed in a way that can be readily communicated through the Guides once approved. Subsequently, it is incumbent on FHFA to develop its grading rubric in a way that incentivizes this consistency.

MULTIFAMILY COMMENTS

Introduction

MBA advocates for public policy that supports and maintains a broad range of capital sources in the multifamily housing finance market, including private capital and government-sponsored sources. The diversification of debt capital sources in multifamily finance is robust. We encourage FHFA to continue to support GSE multifamily activities that strengthen liquidity, stability and affordability in the multifamily rental markets, while refraining from intervention that would be harmful to the competitive landscape and compromise the safe and sound operations of the GSEs' multifamily businesses. As FHFA is aware, the multifamily businesses of Fannie Mae and Freddie Mac already incorporate significant private capital through risk-sharing and risk transfer mechanisms. Any Duty to Serve mandates should take into account the risk taken by the government and private sector GSE partners.

While we appreciate the focus on the preservation of affordable housing, manufactured housing communities and rural markets in the HERA statute, we underscore that multifamily housing, by its very nature, tends to be affordable, and that investment in a range of multifamily housing that rents at different levels in the market, including "workforce" housing, is fundamentally important to families of modest incomes.

Multifamily Finance Market Should Maintain Diversity of Capital Sources

MBA believes that FHFA should be sensitive to the role of the GSEs as it might impact the role of other capital sources. For example, with regard to the refinancing of properties with existing Federal Housing Administration multifamily loans, MBA concurs with FHFA's statement in the proposed rule, "There is no obvious role for the Enterprises to support projects funded under the Section 221(d)(4) program other than to refinance the original loans and remove the properties from the FHA insurance program." [7] Otherwise, there could be longer-term unintended consequences on, for example, smaller regional markets and the lenders that operate in those markets.[8] Currently, with the GSEs in conservatorship, the objective should be to ensure that these markets continue to be served but not by simply replacing one capital source with another. Also, we question whether replacing one capital source with another government guaranteed capital source would fulfill the Duty to Serve mission.

FHFA Questions regarding Low-Income Housing Tax Credit Equity Investments

Fannie Mae and Freddie Mac were leaders in LIHTC equity investments and helped create a tremendous supply of affordable housing. Both GSEs invested in LIHTC funds through LIHTC partnerships and Fannie Mae also made direct investments in LIHTC properties. As a result of the economic crisis and in accordance with FHFA direction,

[7] Duty to Serve proposed rule, Federal Register /Vol. 80, No. 243 / Friday, December 18, 2015 / Proposed Rules, p. 79197.
[8] Responsive to questions 27-40 in the Duty to Serve proposed rule.

the GSEs wrote down their tax credit investments in 2009.[9] Now, absent FHFA approval, neither GSE currently provides new equity investments in LIHTC funds or properties.[10] However, both GSEs provide important and strong secondary market support for their lenders that provide access to debt for affordable housing on multifamily properties that have LIHTCs. MBA believes that the GSEs should continue to focus on their traditional role in providing access to credit. The questions posed in the Duty to Serve proposed rule, however, also inquire whether the GSEs should return to participating on both the debt and equity side in the LIHTC market.

Due to the substantial disruption in the LIHTC markets when the GSEs exited, in part due to their significant market share, MBA recommends that FHFA approach potential LIHTC equity investments by GSEs with caution. Currently, there is robust investor interest in LIHTC properties which has caused the pricing of tax credits to soar to high levels. If FHFA were to consider allowing the GSEs to return to making equity LIHTC investments, MBA recommends that such activity be permitted in targeted markets only, such as rural markets that are demonstrably underserved and only for a modest portion of the market. This would address the concern that the GSEs' equity LIHTC activity should not ratchet up to their former significant investment levels. Should the GSEs' financial interests in using the federal income tax benefit of LIHTC investments alter, or, the GSEs have organizational changes that impact their ability to invest in LIHTCs, any substantial participation by the GSEs in future LIHTC markets should be reviewed and reconsidered. Also, an equity volume limit, for example, could be appropriate to prevent over investment in markets (such as New York in general) where there are ready and available equity investors, while allowing for the positive, consistent GSE support of the LIHTC market analogous to the GSEs' liquidity mission. [11]

<u>Public Housing Preservation</u>

One of the most critical national affordable housing preservation needs is for capital improvements to public housing. There is an inventory of over 1.1 million units of federally subsidized public housing that provides housing to very low income households yet is under-capitalized. It represents a national resource that should be sustained where possible because the replacement cost of new construction is so great and many units are lost annually to disrepair and obsolescence. Funds for capital improvement needs have been inadequate and HUD has estimated the backlog at $26 billion.[12] An existing innovative program to support preservation of existing public housing stock is HUD's Rental Assistance Demonstration (RAD) program.

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[9] P. 33, GAO Report, September 2012 "Mortgage Financing - Fannie Mae and Freddie Mac's Multifamily Housing Activities Have Increased" stated "In February 2010, FHFA determined that the sale of any LIHTC investments made by the enterprises would require the consent of Treasury under the terms of the preferred stock purchase agreements. After FHFA consulted with Treasury, it decided that the enterprises could not sell or transfer the assets and required them to write down the value of the LIHTC investments to zero, causing substantial losses for the enterprises. ."

[10] The GSEs continued to make contractual equity contributions on legacy LIHTC investments originated before FHFA conservatorship.

[11] Responsive to questions 41-45 in the Duty to Serve proposed rule.

[12] P. 41, HUD report "Capital Needs in the Public Housing Program" http://portal.hud.gov/hudportal/documents/huddoc?id=PH_Capital_Needs.pdf

Through the Duty to Serve rulemaking, FHFA could direct the GSEs to explore structures that might create new models for investment in preserving public housing. MBA also supports Duty to Serve credit for the GSEs on research oriented towards design of a model to support preservation of public housing as well as GSE goals for the RAD program.[13]

Small Multifamily Lending

MBA's data[14] confirms that one of the largest multifamily rental segments is the small multifamily loans segment which typically serves multifamily properties in the 5 to 50 unit size and of the 40,974 multifamily loans closed in 2014, 18,840 (46 percent) were loans for $1 million or less. Often these properties provide affordable housing. Community and regional banks commonly provide loans to this market, so whether this market should warrant additional policy focus could be subject to debate. Should credit be provided for Duty to Serve activity in the small multifamily market, MBA recommends that qualified loans be on properties that serve households at 80% of AMI or less which is consistent with FHFA's 2016 Scorecard for the GSEs.[15]

Energy-Efficient Housing

Encouragement of energy efficient housing is important and appropriate for FHFA to consider for Duty to Serve credit particularly if FHFA encourages the GSEs to address the challenges of the cost of energy efficiency certifications. When juxtaposed with the need for small multifamily housing finance particularly in older properties or in more rural settings, FHFA should ask the GSEs to balance the rewards for energy efficiency and the cost of acquiring and maintaining the certification. For example, one approach would be to develop a sliding scale model of energy efficiency so that an older, smaller multifamily property adopting intermediate energy consumption improvements through loan proceeds could also be rewarded.[16]

Manufactured Housing

With regard to Duty to Serve credit for manufactured housing communities (MHC), MBA supports FHFA's proposed 150 unit number maximum because the need for financing in this market is the older or rural communities that tend to be smaller in size. FHFA could encourage the GSEs to develop prudent underwriting standards that would permit financing of qualifying 3 star properties and continue to expand their investments beyond higher-end MHCs. We believe that the GSEs could collect and analyze data on manufactured housing communities to develop investor interest and better serve this market. Attracting capital and liquidity to these submarkets and products will require performance information on the asset classes. Fannie Mae and Freddie Mac could be asked to publish performance data usable by investors to estimate risks. Ultimately this will expand the markets for these assets, improve liquidity and lower the cost to borrowers.[17]

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[13] Responsive to question 67, particularly, RAD questions on page 79205 in the Duty to Serve proposed rule.

[14] MBA's Annual Report on Multifamily Lending (2014)

[15] Responsive to questions 46-50 and page 79199 in the Duty to Serve proposed rule.

[16] Responsive to questions 51-56 in the Duty to Serve proposed rule.

[17] Responsive to questions 10-15 in the Duty to Serve proposed rule.

Research and Data
MBA recommends that FHFA expect substantial contributions by the GSEs towards creating an affordable multifamily data resource to include information on the multifamily underserved segments identified by HERA and the Duty to Serve proposed rule. Both Fannie Mae and Freddie Mac have a collection of invaluable data, much of which is publicly available and understandable to the multifamily finance industry but not necessarily readily accessible to general affordable housing advocates. Subject to proprietary considerations given the limited number of GSE approved multifamily lenders, the GSEs should collect, analyze and make available additional data so that researchers and others can help develop underwriting guidelines that can be refined to systematically enhance investor interest and serve these markets. Attracting capital and liquidity to these underserved markets and potential products will require performance information on the asset classes. Ultimately this will expand the markets for these assets, improve liquidity and lower costs to borrowers.

CONCLUSION

MBA appreciates FHFA progress in developing the Proposal. In crafting the proposed framework and issuing it for comment, FHFA has taken an important step toward increasing access to credit and mortgage liquidity for underserved markets. MBA looks forward to working together on its impelmentation.

For more information on single-family comments, please contact Dan McPheeters at dmcpheeters@mba.org or Katherine Tung at ktung@mba.org, on multifamily comments, please contact Eileen Grey at egrey@mba.org,

Sincerely,

David H. Stevens, CMB
President and Chief Executive Officer