MORTGAGE BANKERS ASSOCIATION

June 4, 2018

Alfred M. Pollard
General Counsel
Federal Housing Finance Agency
400 7th Street, SW
Washington, DC 20219

RE: Regulatory Review [No. 2018-N-03]

Dear Mr. Pollard:

The Mortgage Bankers Association (MBA)[1] thanks the Federal Housing Finance Agency (FHFA) for the opportunity to comment on existing regulations that guide its oversight of Fannie Mae and Freddie Mac (the Government-Sponsored Enterprises, or Enterprises) and the Federal Home Loan Banks (FHLBs). We believe the regulatory review being conducted by FHFA[2] provides an important opportunity for the public to offer input on this oversight process. Periodic reviews of existing regulations represent a form of good governance, particularly as they relate to institutions or markets that are subject to frequent change.

Below, we offer our comments and recommendations on regulations pertaining to both the Enterprises and the FHLBs.

[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, DC, the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership; and to 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 2,300 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 website: www.mba.org.

[2] 83 FR 14605, "Notice of Regulatory Review," April 5, 2018. Available at: https://www.federalregister.gov/documents/2018/04/05/2018-06918/notice-of-regulatory-review.

Regulations Pertaining to the Enterprises

Standards for the Development and Approval of Enterprise Products

Despite their ongoing conservatorships, the Enterprises have continued to innovate by developing new activities and new products that serve a number of varying functions in the mortgage market. MBA strongly believes in the need for responsible innovation, as well as targeted competition between the Enterprises, which together can contribute to better customer service or secondary market executions for lenders. These outcomes should lead to more robust markets that facilitate access to credit for a broader array of borrowers.

It is important to note the unique and sizable impact that the Enterprises have in the mortgage market, as well as the fact that they remain backed by U.S. taxpayer funds. As a result, many new activities and new products of the Enterprises are likely to raise significant questions regarding their contribution to the public interest. We therefore have become concerned in recent years with a lack of transparency in the FHFA approval process for new activities and new products.

For example, little or no public information has been released regarding the design of many new activities and new products. Similarly, there is little transparency with respect to the specific factors evaluated by FHFA in its reviews. This process has made it far more difficult for policymakers, market participants, and other stakeholders to understand whether certain offerings are serving the public interest. The lack of transparency also contributes to the concern that new activities or new products could at times be structured in ways that confer competitive advantages on certain market participants. An important recent example is the use of a single vendor for various aspects of a major Enterprise technology project, thereby forcing many lenders to choose whether to retain their existing vendors or switch to the lone "approved" vendor.

To restore confidence that the Enterprises are innovating in ways that promote efficiency, enhanced competition, and robust markets, MBA recommends a number of revisions to the regulations contained in 12 CFR Part 1253.

First, FHFA could improve transparency regarding new activities by revising 12 CFR § 1253.3 to require public disclosure of any Notice of New Activity—even if such activity is not deemed to be a new product and receives a non-objection from FHFA.

Second, FHFA could explicitly specify the factors it will consider when determining whether a new activity constitutes a new product that is subject to public notice and comment. When FHFA exercises its authority pursuant to 12 CFR § 1253.3 to determine that a new activity is or is not a new product, it relies on factors that are not

well defined in the existing regulations. For example, the definition of a "new product" in 12 CFR § 1253.2 features a number of activities that are specifically deemed to *not* constitute new products, but the only affirmative characteristic of a new product is that the FHFA director determines that it "merits public notice and comment on matters of compliance with the applicable authorizing statute, safety and soundness, or public interest."

And while the Notice of New Activity provides some indication of the information used by FHFA in making its determination, it does not provide clear explanations as to how FHFA analyzes this information or what metrics are used. To improve transparency in FHFA's determination as to whether a new activity constitutes a new product (and therefore requires public notice and comment), we recommend that FHFA specify the applicable factors under 12 CFR § 1253.3. With respect to the FHFA determination related to the public interest, this clarification should incorporate the factors specified under 12 CFR § 1253.4(b)(3).

In addition, we recommend that FHFA modify the manner in which it addresses new activities denominated as "pilots." For example, in many cases an Enterprise submits a Notice of New Activity pursuant to 12 CFR § 1253.3, and that new activity is intended to be limited such that it is only available to a subset of lenders for an initial period of time, subject to further evaluation by the Enterprise and FHFA (commonly known as a "pilot"). Despite the limitations conferred by pilot status, such activities by an Enterprise could have widespread and lasting effects on markets and competition, which may or may not be in the public interest.

To better determine whether a pilot is serving the public interest, greater transparency should be promoted through a revision to 12 CFR § 1253.3 to include a requirement that the Enterprise or FHFA disclose to the public relevant information regarding the size, scope, participants, and expected duration of the pilot. FHFA should also require the Enterprise to take measures to ensure a sufficient diversity of participants across a number of dimensions, unless there is a compelling business reason or impracticality associated with doing so. These measures should help ensure that new activities are not immune from the necessary requirements of the review process purely because they are initially structured as pilots. Similarly, we believe these measures are sufficiently targeted to help ensure that they do not reduce incentives for market participants to develop new offerings or otherwise stifle innovation.

Finally, FHFA should amend 12 CFR § 1253.3 to more explicitly require that any market data collected through pilots be made broadly available to the public. Such data can then be used to further the public interest by allowing market participants to better calibrate models, detect fraud, and spur additional innovation. Transparency in

data obtained through pilots can also serve the public interest by facilitating adoption of new offerings by a broad array of market participants.

Enterprise Multifamily Businesses and the Multifamily Market

Liquidity and stability in the multifamily rental housing market is vital across geographic regions and through all parts of the credit cycle. The Enterprises play a significant ongoing role in the multifamily sector, particularly for workforce and affordable rental housing. Both Enterprises have exceptional credit performance and deliver financing in the multifamily market through different and competing executions, while also transferring significant risk to third parties, thereby reducing taxpayer exposure. At the same time, the diversification of and competition among capital sources in the multifamily real estate market is crucial to its strength. A range of financial sectors and institutions with varying business models compete in this market in a manner that disperses risk throughout the system.

Regulations administered by FHFA affect the Enterprises' multifamily business in several ways. As is reflected in FHFA's *2017 Report to Congress*, in the exercise of its conservatorship powers under 12 CFR Part 1237, FHFA has maintained multifamily loan production caps on each Enterprise to further the strategic goal of maintaining each Enterprise's multifamily activities while not impeding the participation of private capital.[3] In addition, the duty to serve and affordable housing goals under 12 CFR Part 1282 include multifamily components. Any efforts to effect some level of reform of the Enterprises through regulatory action could similarly affect the Enterprises' multifamily business.

In light of the important role the Enterprises play in financing multifamily housing, we urge FHFA to adopt a "do no harm" approach as it engages in any activity under its current or future regulations. Such an approach recognizes the strength of the Enterprises' multifamily businesses and other capital sources in this market, as well as the need to avoid the potential for market disruption that could adversely affect the rental market in a disproportionate manner.

Public Access to Historical Data

MBA also appreciates FHFA's continued work to develop a proposed rule on public-use databases and public information provided by the Enterprises. The regulations contained in 24 CFR § 81.72, which are administered by FHFA despite being adopted by the U.S. Department of Housing and Urban Development, require the

[3] FHFA, "2017 Report to Congress," p. 40, May 23, 2018. Available at: https://www.fhfa.gov/AboutUs/Reports/ReportDocuments/FHFA_2017_Report-to-Congress.pdf.

ongoing maintenance of a public-use database. This database must include mortgage data collected under subsection 309(m) of the Fannie Mae Charter Act or subsection 307(e) of the Freddie Mac Act, as well as information submitted through the Enterprises' Annual Housing Activities Reports.

MBA will withhold its specific comments on this process until FHFA publishes its notice of proposed rulemaking. More broadly, however, MBA encourages FHFA to ensure any database developed in accordance with these regulations is truly accessible to the public at a reasonable cost. Such a database should also include more granular loan-level information from the Enterprises than those data elements currently listed in the Enterprises' charter acts (and which are cross-referenced in the regulations contained in 24 CFR § 81.72). Additional data that would be useful for public analysis includes credit scores and debt-to-income ratios for single-family loans.

Regulations Pertaining to the Federal Home Loan Banks

Membership Eligibility of Captive Insurance Companies

The FHLBs serve a critical mission by providing stable, reliable liquidity to their member institutions, which in turn allows those member institutions to support affordable housing and community investments. The FHLB membership eligibility requirements reflect the desire to limit the scope of institutions that can take part in the System to those institutions with business models that align with the FHLBs' mission. Under 12 CFR § 1263.6(a), a variety of financial institutions are granted eligibility for membership in a FHLB, provided that they "make[s] long-term home mortgage loans" and have a "home financing policy … consistent with sound and economical home financing," among other conditions.

Further, under 12 CFR § 1263.6(c), institutions that are not insured depository institutions also "must have mortgage-related assets that reflect a commitment to housing finance." These eligibility conditions are appropriate to ensure that the benefits of FHLB membership are not conferred on institutions that do not help serve the public policy objectives that led to the creation of the FHLBs.

However, we firmly believe that a rule issued by FHFA in early 2016[4] inappropriately excludes from FHLB eligibility an important subset of institutions that do further these public policy objectives: the captive insurance affiliates of mortgage real estate investment trusts (REITs). Mortgage REITs are financial institutions that invest

[4] 81 FR 3246, "Members of Federal Home Loan Banks," January 20, 2016. Available at: https://www.gpo.gov/fdsys/pkg/FR-2016-01-20/pdf/2016-00761.pdf.

almost exclusively in real estate-related assets as a condition of their business models and tax structures. In doing so, they serve as a vital source of private capital in mortgage markets, facilitating lending to a broad set of borrowers. These borrowers include those with strong credit profiles who struggle to access affordable credit because they are not able to secure loans that meet the Qualified Mortgage standard.

Prior to the issuance of this rule, a number of mortgage REITs safely and prudently maintained indirect access to FHLB advances through captive insurance affiliates that were members of a FHLB. These advances supplement mortgage REITs' other funding sources, allowing them to borrow at longer maturities and support stable housing finance through changing market dynamics, including the effects of the Federal Reserve's diminishing investment in residential mortgage-backed securities.

For the reasons noted above, MBA believes that mortgage REITs, at the very core of their operations, maintain a commitment to housing finance that warrants eligibility for FHLB membership. Their access to FHLB advances through their captive insurance affiliates allows them to further this commitment in a safe, responsible manner that diversifies the sources of private capital serving borrowers in the housing finance system.

In order to continue FHLB eligibility for those mortgage REIT affiliates that are currently transitioning out of their existing memberships, and to restore FHLB eligibility for those mortgage REIT affiliates that have already been forced to terminate their memberships, MBA recommends a series of changes to 12 CFR Part 1263. The regulations contained in 12 CFR § 1263.6(e) should be rescinded, and other conforming changes should be made throughout 12 CFR Part 1263 to reverse the effects of the portions of FHFA's 2016 rule pertaining to captive insurance companies.

These conforming changes include revision of the definition of "insurance company" in 12 CFR § 1263.1. Further, to accommodate a more seamless re-entry of those mortgage REIT affiliates that have already been forced to terminate their memberships, the five-year waiting period required under 12 CFR § 1263.30(a) should be waived for captive insurance companies that were admitted to FHLB membership on or after September 12, 2014. And finally, any regulatory changes should ensure that captive insurance companies be allowed to maintain or regain membership in the same FHLB in which they are or were a member.

Acceptance of eNotes

As mortgage lenders continue to rely upon new and evolving technology in loan origination, servicing, and secondary market functions, it is critical that relevant regulations keep pace. In particular, the growing use of electronic promissory notes (eNotes) presents a challenge for certain regulations issued prior to this technological development. FHFA should ensure that its existing regulations do not unintentionally stifle innovation by restricting the growth of eNotes. An important example is the inability of FHLB members to access advances against eNotes.

The regulations governing FHLB advances in 12 CFR Part 1266, Subpart A rely upon the definition of an "advance" specified in 12 CFR § 1266.1. This provision defines an advance as "a loan from a [Federal Home Loan] Bank that is … supported by a note or other written evidence of the borrower's obligation." Because the regulations may be read to imply the need for *written* notes, it is unclear whether eNotes are acceptable forms of documentation supporting FHLB advances to their members.

While FHFA has specifically directed the Enterprises to facilitate the use of eNotes in the market, many FHLBs continue to express concerns that FHFA does not support advances against eNotes. This inconsistency has tangible implications for the market, as it artificially favors a securitization execution relative to a portfolio execution. The failure to allow advances against eNotes also inhibits the transition to digital mortgages, as lenders often cannot afford bifurcated processes and therefore continue the use of inefficient and error-prone paper processing.

Given the increasing importance of eNotes to the mortgage industry, including the efficiencies and savings that hold the potential to lower costs for consumers, MBA believes that FHFA should clarify that eNotes represent an acceptable form of documentation for the purposes of FHLB advances. And while we believe FHFA could issue guidance through an Advisory Bulletin that would provide the necessary clarification, a change in the definition of an "advance" contained in 12 CFR § 1266.1 would also address the problem. Such a regulatory change should replace the phrase "supported by a note or other written evidence … " with "supported by a note, written or electronic, or other written or electronic evidence …."

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MBA appreciates FHFA's thorough review of its existing regulations, as well as its consideration of our comments. We believe there are numerous opportunities for FHFA to employ a more efficient regulatory approach that promotes competition in the mortgage market. In addition to the issues raised above, other areas which we believe warrant further action include more formally ensuring a level playing field for

lenders of all sizes and business models, as well as improving coordination with other regulators when implementing actions related to borrowers with limited English proficiency, including a language preference question on the Uniform Residential Loan Application.

Should you have questions or wish to discuss these comments, please contact Dan Fichtler, Director of Housing Finance Policy, at (202) 557-2780 or dfichtler@mba.org.

Sincerely,

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Senior Vice President
Public Policy and Industry Relations
Mortgage Bankers Association