Public Comment on the Fannie Mae Underserved Market Plan
Notes from a meeting held on June 29, 2017, Nashville, TN

Introduction

A public meeting was held at the Metropolitan Development and Housing Authority headquarters in Nashville, Tennessee on June 29, 2017, co-convened by the Lincoln Institute of Land Policy, and the Grounded Solutions Network. Approximately 35 participants, including representatives from both Government-sponsored Enterprises (GSEs: Fannie Mae and Freddie Mac), reviewed the Underserved Market Plans (UMPs) of the GSEs to meet their Duty to Serve (DTS) obligations.

The main goal of the meeting was to review the plans with specific reference to three housing submarkets: manufactured housing; preservation of affordable rental housing; and preservation of affordable homeownership. Meeting participants discussed the challenges presented in each submarket, each of the GSEs' proposed plans to improve financing services in each submarket, and whether they considered the proposed plans satisfactory for serving the submarkets. The discussion was based on participants' assessments of the ability of the GSEs to serve the submarkets while meeting their obligations to maintain safety and soundness.

The discussion of the Fannie Mae UMP generated the commentary that follows. Participants at the meeting who agreed with the commentary and signed on to these comments are listed at the end of this report.

Overview

Participants were impressed with the broad reach of Fannie Mae's plan across many statutory and regulatory activities in each of the three submarkets. In addition, meeting participants felt that the plans are achievable. However, participants felt that the plans were achievable because they lacked ambition and specificity. Participants found Fannie Mae's analysis of the underserved markets acceptable, but they were disappointed with the lack of identification of possible partners in each market and with the slow pace of the proposed implementation of the UMP.

Importantly, participants felt that the UMP tends to ignore the depth and breadth of the affordable housing field. In their view, participants felt that the field is full of well-established counterparties who could partner with Fannie Mae to expand its service in these submarkets, while at the same time helping to manage and reduce risk. These counterparties include: national, state, and local networks of practitioners; state housing finance agencies; and mission-driven lenders such as CDFIs and Credit Unions. In addition, many of these counterparties have innovated and tested lending products and processes that are ready for scaled investment from the GSEs. However, the UMP calls for years to study the markets and/or to design more effective lending products to serve the markets, as if deeper market knowledge or effective lending products do not already exist. Many participants felt that Fannie Mae was "padding the calendar" to manage expectations for its implementation of the plan. Participants felt that more aggressive implementation is warranted, particularly because of the urgent needs for financing services in the submarkets.

Finally, participants felt that the UMP fell short on one very important matter—the extent to which Fannie Mae could play the role of "market-maker," a role it has played in the past. For example, Fannie Mae helped to standardized the mortgage underwriting process and essentially invented the "vanilla" mortgage when it began securitizing mortgages in the early 1970s. This introduced efficiencies in the markets that made it possible to offer mortgages at more attractive rates for borrowers, but also laid the groundwork for evolution to desktop underwriting. Providers of lending capital can drive quality into underserved submarkets by establishing and enforcing new standards that require borrowers to conform to access capital on desirable terms. If Fannie Mae worked with counterparties in the field to achieve a nuanced understanding of the three submarkets, it could drive the submarkets to overcome the specific dysfunctions that made them hard to serve in the first place.

If Fannie Mae were to play the role of market-maker, it is essential that it maintain an investment portfolio. There is scant reference to maintaining or expanding Fannie Mae's existing portfolio in the UMP. Without a portfolio from which to pilot new products and approaches to serve these submarkets, Fannie Mae's efforts will be narrowed to efforts that can attract secondary capital. Until a track record is established for new products and approaches the secondary market will likely over-price capital and constrain its flow, further limiting the information that might be gleaned through disciplined portfolio lending. Participants urge the FHFA to permit both GSEs to maintain a prudently managed portfolio to cultivate high-quality lending in these submarkets.

In the following pages, more specific comments about the Fannie Mae UMP are presented by submarket.

1. **Manufactured Housing**

Overall, it is notable that the proposed targets in the UMP, while important, would barely improve the market for manufactured housing finance during the three years of the plans. This is disappointing. Participants felt that Fannie Mae can do better, and by doing better, help the submarket to overcome its dysfunction. By entering the market with sufficient liquidity, Fannie Mae can drive quality into the market—more efficient transactions will offer less expensive mortgage debt. Standardized and streamlined underwriting processes would drive out lower quality lending that harms the image of the market, for example, chattel loans made to purchase poorly sited housing.

The basic dysfunction in the market is an artifact of market players' and policymakers' lack of product understanding—this includes lending products, but also the quality of unit construction, siting standards, and other amenities. The resulting poor image of the housing stock constrains the flow of capital into the sector, which leads to discrimination in zoning, lower unit values, and a higher severity of losses when loans go bad. By providing capital on the right terms, with the right standards imposed for manufacture, pricing, and siting of the homes, the GSEs can lead real change in the submarket that has the potential to correct the dysfunctions listed above and drive market convergence for manufactured housing and site-built housing without sacrificing the enhanced affordability of manufactured housing.

Fannie Mae has excellent and useful data in its plan including discussion of the structural challenges currently imbedded in the manufactured housing finance market. Notably, the UMP recognizes the fundamental need for coordinated outreach and basic research, research that is taken for granted in other housing sectors. For example, public loan performance research is largely nonexistent, with the notable exemptions of CFED's 2013 study on manufactured home mortgages, and the lending record of the New Hampshire Community Loan Fund's manufactured housing mortgage program. It is important to note that even less is known about the performance of chattel lending products.

Participants appreciate Fannie Mae's commitment to extensive research and outreach. Fannie Mae's recognition of the need to make fundamental changes to its guidance and program standards is also important. Specific additions that participants would like to see in Fannie Mae's program standards: for all loan products, and those designed to serve the affordable market, such as HomeReady, there should equal treatment of gifts and grants for downpayments, subordinated financing such as Community Seconds for a combined loan to value (CLTV) of 105%, lower MI coverage, loan-to-value ratios, construction conversion with a single close and no discrimination against single-section homes, including the restriction of single-section homes to Planned unit Developments or PUDs. Essentially, participants hope that lending in the manufactured housing sector can converge to equivalence with lending in the site-built market.

To adequately serve the MH market, Fannie Mae must develop flexible processes to underwrite loans, and provide timely feedback to lenders regarding variances, to increase RE purchases. A meaningful part of the UMP, is Fannie Mae's commitment to reinstate MH Select, with an intention to purchase 250-750 loans in each of plan years 2 and 3. Fannie also notes that existing RE products will generate between 500 and 2500 new MH loan purchases. These target numbers lack ambition and will have little impact on the MH market. Participants think that Fannie Mae can exceed these modest targets responsibly by focusing on the use of variances and other tools in select states, especially those with established state housing finance agency programs already in place. Some of these were cited in the 2013 CFED study. Since then, new HFA products have been launched or are in development that are already suitable for GSE purchase.

Participants greatly appreciate Fannie Mae's commitment, with FHFA approval, to roll out a chattel pilot to facilitate the purchase of 350-425 MH loans in each of plan years 2 and 3. It is hoped that Fannie Mae could drive higher quality into chattel lending by offering liquidity on the right terms. Given the huge share of MH lending done through chattel, no effort to serve the manufactured home loan market can succeed without a chattel program. Fannie Mae should commit to its chattel program but provide liquidity only for high quality loans; including good loan terms for borrowers and land lease protections for tenants. As many state HFAs currently do not make or purchase chattel loans because they do not approve of the terms or protections for homeowners, Fannie Mae might work with them to establish the right guidelines to give these important counterparties comfort in participating in this lending. This suggests that the right path will be driving the chattel market to converge with the real estate mortgage market regarding loan terms and protections. Given Fannie Mae's appetite for data, we wonder whether the number of loans will be sufficient to generate enough information to understand the fundamentals of the chattel market. This underscores Fannie Mae's point that the lack of industry data hamstrings the pilot proposal. But the pilot itself will only demonstrate the viability of lending in this market if sufficient numbers of loans are purchased.

a. <u>Manufactured Housing Communities</u>

While participants appreciate Fannie's commitment to research and outreach, they expressed disappointment with its limited involvement in mission-driven Manufactured Housing Communities (MHCs). With an estimated 45,000 MHCs in the country, Fannie Mae's commitment to purchase non-profit MHC community loans for communities with w/ 200-300 units in plan years 2 and 3 will have some value, but it won't move the market. Similarly, Fannie Mae's plan to enter the Resident-Owned Community (ROC) market in year 2 by purchasing 5 ROC loans and seven loans in in year 3 is important but not sufficient to catalyze this very effective means for preserving affordable housing. It is important to note here that the lending records in the MHC space of ROC USA and the New Hampshire Community Loan Fund are pristine, so expanding this lending should not be overwrought with fear of risk.

Participants felt that Fannie Mae's proposal to support loans for MHCs with meaningful lease protections, to support 250 MHC units in year 3, is valuable but again of insufficient volume to move the market in the right direction. The proposed pilot for CDFI investment to support ROCs/Non-Profit MHCs is vital to preserve affordable homeownership. Participants believe this could help transform the MHC market into a more sustainable and responsible option, but it must be done at sufficient scale to make meaningful impact.

Fannie Mae's investment in communities comes at an important time. MHCs are under considerable pressure from other investors to close and convert to alternate land uses. The current inventory of manufactured housing in MHCs represents the largest share of unsubsidized affordable housing in the country. Without a serious commitment to preservation of this housing stock, families living in these communities will be cast into competition for a grossly inadequate affordable housing stock, or worse yet, adding their names to years-long waiting lists for housing subsidies.

2. Multifamily Preservation and Rural Markets

a. <u>Partnering with Housing Finance Agencies in Preservation Activities</u>

In Fannie Mae's plans, small financial institutions are referenced as if they are separate from other intermediaries, like State Housing Finance Agencies (HFAs). Partnering with state agencies can provide Fannie Mae important access to local market reconnaissance. For example, Minnesota Housing has a strategic priority to preserve federally assisted multifamily housing developments. In addition, the agency is the Performance-Based Contract Administrator for HUD's Section 8 portfolio for the state of Minnesota and utilizes this relationship to strategically allocate preservation resources. Minnesota Housing would be an important strategic partner for Fannie Mae in its efforts to preserve affordable housing in the state. Similarly, other state HFAs, like the Tennessee Housing Development Agency (THDA) stand ready to partner with Fannie Mae to preserve affordable housing in their states.

To facilitate preservation of affordable housing, Fannie Mae should consider developing a fully amortizing product to parallel FHA mortgage insurance products that is priced to reflect the stability of long term owners. The product should include low interest rates that are comparable to standard balloon deals, higher loan to value ratios (up to 100% in certain markets compared to standard 85%), better baseline pricing on fully amortized loans. If there were better baseline pricing on fully amortizing loans for affordable loans, state HFAs would be in a better position to follow with a second or other deferred financing.

Fannie Mae specifically addresses the statutory activity of state and local housing programs in its UMP, and expresses intentions to review at least five programs that currently do not meet the definition of a "multifamily affordable housing" transaction as defined by them. This outreach in year one of the plan is expected to result in the purchase of 10-15 loans in each of years 2 and 3. The numeric goals of partnerships and loan purchases are conservative, but given there is no precedence for this activity, the goal may be a reasonable starting place. However, participants encourage Fannie Mae to consider solutions beyond first position amortizing debt, such as a soft second or even deferred solution, recognizing that mission-driven financial transactions do not conform with standard loan products.

Developing a new offering to close capital gaps for Section 8 transactions and rental assistance demonstration (RAD) are important given tax credit pricing and federal appropriations uncertainties. These products need to have terms conducive to supporting deep subsidies, such as lower interest rates, higher loan to value ratios (up to 100%), and better baseline pricing for affordable products. Participants encourage Freddie Mac to consider solutions beyond a first amortizing mortgage, such as a soft second or even deferred activity to help to achieve deep affordability.

It would be extremely helpful if Fannie Mae would help to solve the conundrum of financing mixed-income development. Although this is a frequently articulated goal in public policy, financing solutions for mixed-income housing are conspicuously absent from guidelines for developing or preserving affordable housing. For example, Fannie Mae could explicitly include "residential economic diversity" in scoring applications for multifamily preservation financing, especially related to the "rental assistance demonstration" (RAD) program. In addition, creating a mixed-income financing product that has terms, pricing, and execution that are superior to existing products would help to catalyze preservation of this important segment of the housing stock. An important component for this lending product would be providing forward commitments to give assurance to other partners that permanent financing will be accessible. As noted in other areas of this comment, it will be necessary for Freddie Mac to maintain or expand its portfolio lending to innovate in this space.

Participants were encouraged that Fannie Mae acknowledges that states and localities have different affordable housing needs and programs that are designed to meet these needs, but this results in differing standards across different organizations. Perhaps it would be better to drive standardization across states with a higher quality product as defined above.

b. Preservation of small multifamily rental projects

In the draft plan, Fannie Mae addresses the regulatory activity of financing small multifamily rental projects (5-50 units) to develop and scale an effective approach for purchasing loans from financial entities with $10 billion or less in assets. To achieve its objective, Fannie Mae will conduct outreach to identify an effective approach. This would start by partnering with existing delegated underwriting and servicing (DUS) lenders to build or enhance existing networks with a goal of purchasing at least 45 loans. Fannie Mae should not limit initial outreach to DUS lenders. Instead they should define and cultivate "Special Affordable Small Loan Lenders" from the start because it is likely that not enough DUS lenders will be available and interested in sourcing these loans to Fannie Mae.

To address preservation of USDA Rural Development Section 515 properties, which typically are smaller properties, Fannie Mae should partner with USDA, but must keep in mind that RD loans cannot be subordinate so it will require creativity to find a permanent loan solution.

c. Low Income Housing Tax Credit (LIHTC) Activities in Preservation and Rural Markets

Participants feel that it will be important for Fannie Mae to balance LIHTC activities in urban markets with activities that meet the definition of "high needs" rural areas and preservation deals in other rural areas (e.g. in low CRA demand areas). Participants encourage Fannie Mae to partner with state equity funds, such as the Minnesota Equity Fund to develop and scale up lending relationships in these areas.

In rural markets, Fannie Mae intends to acquire equity investments in LIHTC properties in areas associated with statutory or regulatory preservation activities. Research up front to identify goals and partners or best-in-class syndicators to support a year 2 goal of 5 equity investments and year 3 goal of 10 equity investments is encouraged. However, the plan should expand to include "high need rural populations," in addition to rural areas, if the intent of this objective is to serve "high need rural areas" as defined by the final rule.

In the preservation market, Fannie Mae has an objective to increase the purchases of mortgages secured by LIHTC properties, and states a goal of purchasing 40-70 loans secured by LIHTC properties. Given the three-year baseline of 56 loans, participants encourage Fannie Mae to consider a higher goal in year 1 as additional product enhancement needs are identified, even amidst market uncertainty. If the market is not able to respond, the plan could be amended in year's 2 and 3. In addition, Fannie Mae should consider room for flexibility in its standard underwriting guidelines and risk assessment.

3. Preserving Affordable Homeownership

Fannie Mae proposes generic and relatively minor outreach and marketing to identify loan product needs. However, this work has already been done and submitted in a 14-page white paper by Grounded Solutions Network (formerly National CLT Network). Participants would rather proactively recruit a select group of Fannie Mae lenders working at financial institutions with large geographic footprints to educate, train, and incentivize them to partner with shared equity programs to originate mortgages to their homebuyer and owners. In addition, broad based outreach to Fannie Mae lenders is needed, especially when future loan product changes make origination easier or provide better incentivizes.

Lenders in markets with strong shared equity homeownership programs should be identified to educate lenders and build partnerships with other shared equity homeownership programs in less developed markets. Fannie Mae should staff a "help desk" that is available for lenders and program providers, where lenders in the middle of deals can get fast answers and certainty on compliance and program providers may request help to find local Fannie Mae lenders that can be trained and supported (and hopefully, incentivized) on shared equity homeownership origination.

Fannie Mae proposes research, including economic studies and case studies, which participants believe is of low value and likely less impactful than the following research, which would greatly support the field and help Fannie Mae to meet its DTS objectives:

- ***i.*** ***Development, Updating, and Maintenance of a National Inclusionary Housing Database.*** A critical challenge in the realm of shared equity homeownership is understanding the size and scope of the market. The largest market, which is the least documented, is deed-restricted housing in inclusionary housing programs. Willing partners for Fannie Mae, including the Grounded Solutions Network, have laid a foundation upon which to build this research as a public resource.

- ***ii.*** ***Best Practices, Enabling Policies, and Innovations in Rental Housing that Provides Lasting Affordability.*** Far less is known about how to deliver permanently affordable housing in rental projects. Given the challenges described above in the discussion of "affordable housing preservation," support is needed to conduct applied research that "works the problem" of requiring permanent affordability in publicly-supported rental projects.

Fannie Mae proposes changes to loan products to support the preservation of affordable homeownership. However, participants request more specific attention to the following priority: ***removing barriers for deed-restricted programs, especially those that have restrictions that survive foreclosure.*** Specific barriers that need to be addressed include: making it clearer in the Selling Guide which sections and requirements apply to which kind of deed-restricted program; establishing automated underwriting when restrictions survive foreclosure; calculating down payment requirements based upon the affordable purchase (not the appraised value); removing reps & warranty requirements for lenders, or providing some alternative incentives; providing guidance on how to evaluate the impact of different resale restrictions on property appraisals and establishing a system to allow market-rate comparables to be used during appraisal process; removing references to requirements on shared appreciation in property value and allowing nonprofits and government shared equity housing programs to design resale formulas that work for their local markets and balance wealth building and affordability preservation; and, minimizing and clarifying organizational underwriting criteria for community land trusts and considering moving organizational underwriting in-house or to a third-party in order to minimize burdens on lenders, and to provide additional incentives for lenders to originate loans on ground-leased property.

Fannie Mae states that it has not tracked shared equity loans, and therefore, cannot establish a baseline for loan purchases. However, the UMP states that it will perform an analysis of Fannie Mae's portfolio of shared equity loans in Year 1, 2, and 3. Participants request then that Fannie Mae establish a baseline volume for loan purchases. Fannie Mae should at least double its goal for loan purchases for every year within the final UMP. Grounded Solutions Network has documented roughly 100,000 homes, which is nowhere near the entire shared equity homeownership field. There are hundreds of additional programs. Fannie Mae is proposing to purchase a mere 1% of loans for those documented units. They need to do more.

Finally, Fannie Mae plans to determine a potential role for multifamily financing in conjunction with efforts to preserve affordable homeownership. Participants feel that the goals should be more ambitious and incorporate other evaluation areas. Fannie Mae should address two different aspects of lending for limited equity cooperatives in these expanded activities: (1) improving the terms of blanket mortgages, and (2) offering a viable share loan product for buyers in limited equity housing cooperatives. In addition, Fannie Mae should conduct outreach as a Year 1 activity and then develop a "pilot" or test product variances for year 2 and 3 that will result in evaluating loan performance and permanent changes in financing products to scale up this activity.

4. Appendix: Meeting Participants

Amy Barnard, Next Step
Kay Bowers, New Level CDC
Hiram Brown, Urban Housing Solutions
Kathy Buggs, Congressman Cooper's Office

Kim Cox, Walker & Dunlop
Marshall Crawford, The Housing Fund
Jessica Deegan, Minnesota Housing Finance Agency
David “Buck” Dellinger, Metropolitan Development and Housing Agency (MDHA), Nashville
Stacey Epperson, Next Step
Clint Gwin, Pathway Lending
Jim Harbison, Metropolitan Development and Housing Agency (MDHA), Nashville
Jennifer Hopkins, New Hampshire Community Loan Fund
David Johnson, Johnson Johnson Crabtree Architects
Eddie Latimer, Affordable Housing Resources, Inc.
Morgan Mansa, Mayor's Office of Nashville
George "Mac" McCarthy, Lincoln Institute of Land Policy
Laura Mullahy, Lincoln Institute of Land Policy
Barry Noffsinger, Credit Human Federal Credit Union
Ralph Perrey, Tennessee Housing Development Agency
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Michael Wegerson, Metropolitan Development and Housing Agency (MDHA), Nashville
Betty Whittaker, Kentucky MHI
Tony Woodham, Woodbine Community Organization