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Comments on RFI on Equitable Housing Finance Plans

Submitted to the Federal Housing Finance Agency

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In 2020, 3.06% of loans purchased by Fannie Mae were for Black borrowers and 8.03% were Hispanic borrowers. In comparison, 65.61 % were for white borrowers[1]. For Freddie Mac in 2020, 3.28% of loans purchased were to Black borrowers and 6.77% to Hispanic borrowers. Compare that to 64.62% of loans were for white borrowers[2]. This poor performance with Black and Hispanic borrowers is an ongoing problem in meeting an important market opportunity. Compare these numbers with FHA insured mortgages, where in 2020, 12.74% of FHA loans went to Black borrowers, 17.29% of loans went to Hispanic borrowers and 50.11% went to white borrowers[3].

We recognize that Fannie Mae and Freddie Mac will not accept the same levels of risk that FHA will. But there is a wide gap between the Government Sponsored Enterprises (GSE) and the FHA credit opportunity and plenty of room for Fannie Mae and Freddie Mac to do significantly better.

One fundamental area needing improvement is the GSE's lending to people with lower downpayments and lower credit scores. Black and Brown borrowers coming from lower wealth communities are not be able to save as much funds for a downpayment. Their families are typically lower wealth and have less ability to gift downpayment contributions to help with the purchase. They are also more likely to be rent burdened, paying a higher proportion of their income for rent and, as a result, having greater difficulty saving downpayment funds.

At the same time, the GSE's have maintained very high credit score averages. The average credit score in the Fannie Mae portfolio is 751[4]. For Freddie Mac, the average credit score is 759[5]. Compare that to the average credit score of Black households, which is 677 and for

[1] Annual Mortgage Report – Fannie Mae 2020
[2] Annual Mortgage Report – Freddie Mac 2020
[3] FHA Single Family Production Report
[4] First Quarter 2021 Financial Results Summary – Fannie Mae

[5] First Quarter 2021 Financial Results Summary – Freddie Mac

Hispanic households, 701. White average credit scores are 734[6]. Over 50% of white people have FICO scores above 700 compared to only 20.6% of Black people.[7] People coming from low wealth communities often have lower credit scores. What we see in housing counseling programs that do extensive reviews of credit reports for people who want to buy their first house is that low and moderate income people of color may have 1) thinner credit files where minor credit dings have outsized impact, 2) a reluctance to increase credit capacity, which means they are not aware of the counterintuitive value of having plenty of unused credit capacity to improve the credit score, 3) credit reporting errors, 4) use of subprime credit sources where timely payment is not as valuable as with prime credit sources in credit scoring, 5) some institutional players that only report late credit payment but not timely payment, 6) personal preferences to use cash over credit, and 7) recent immigrant credit histories where the country of origin credit does not routinely transfer and it takes time to understand and access the United States systems.

Fannie Mae and Freddie Mac automated underwriting programs treat lower downpayment borrowers with lower credit scores as layered risk and higher risk[8]. This disadvantages Black and Brown borrowers and helps explain why such low percentages of the Black and Brown borrowers are in the Fannie Mae and Freddie Mac portfolios.

The new Fannie Mae program to review the borrower's electronic bank activity, with the borrower's permission, is a valuable step in the right direction. More credit information for a more robust credit profile is important. However, this does not help people who pay some of their bills in person or people who operate in a cash economy.

First, to significantly increase Black and Brown portions of their portfolios, the GSE's should recognize that they need to properly service low downpayment borrowers by going lower on credit score.

Second, the GSE's should work closely with HUD approved housing counseling agencies to identify the borrowers in the 600 to 700 credit score bands that are lower risk and capable of making timely payment.

Housing counselors can develop more robust credit profiles by documenting and evaluating rent, utility, furniture, and childcare payments. Counselors can assemble letters of explanation, help people set up automatic payments, and provide financial management skills. The GSE's should accept and approve participants with lower credit scores who successfully complete housing counseling programs.

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[6] Average Credit Scores by Race
[7] Choi, Jung Hyun, Alanna McCargo, Michael Neal, Laurie Goodman, and Caitlin Young. "Explaining the Black-White Homeownership Gap." Urban Institute, October 2019. https://www.urban.org/sites/default/files/publication/101160/explaining_the_black-white_homeownership_gap_2.pdf
[8] Tom Herbert, MIT, The Unequal Costs of Black Homeownership

Third, living with parents and relatives is common in communities of color. Rent payments in these situations when properly documented should not be rejected because the relationship is not "at arm's length."

Fourth, the GSE's and Ginnie Mae should have a program to address the income volatility that impacts low and moderate income borrowers. Without increasing the cost to the borrower, Fannie and Freddie and Ginnie Mae should provide protections for people who have a temporary loss of income. As an example, MassHousing, the Massachusetts housing finance agency, has a program to provide up to 6 months of house payment for any of their borrowers who are unemployed. FHFA and Ginnie Mae can demonstrate leadership in developing a similar program which would reduce risk and help maintain longterm homeownership in Black and Brown communities.

Fifth, FHFA should restore the housing counseling data fields and language preference collection in the Uniform Residential Loan Application. The inability of the lending community to track and utilize language preference means that lenders and servicers cannot communicate with a portion of their borrowers who will not understand communications in English. This is an ongoing and unnecessary problem. Integrating the language preference data field into mortgage origination, requiring that the language preference transfers at closing with the mortgage information to the servicer, and keeping the information available if servicing is sold, will mean that the lender and servicer have the ability to communicate in language at any point in the relationship. Similarly, restoring the housing counseling data fields will allow housing counseling work to be tracked. In the future investors may evaluate counseled loans as lower risk, and servicers can refer delinquent borrowers back to the agency with which they had worked.

Sixth, FHFA and Ginnie Mae should develop a system to fund housing counseling services provided to their borrowers. Fannie Mae's $500 LLPA paid to the lender for a counseled loan rarely filters down to the housing counseling agency.

Finally, post purchase housing counseling is valuable for first time homebuyers. There needs to be adequate funding and the program should incentivize borrowers to participate. Also, servicers should refer counseled borrowers back to the housing counseling agency if the borrower has a delinquency.