Comments of the National Community Stabilization Trust
to the Federal Housing Finance Agency

Enterprise Equitable Housing Finance Plans Request for Input

November 25, 2021

Thank you for the opportunity to respond to the Enterprise Equitable Housing Finance Plans Request for Input.

The National Community Stabilization Trust (NCST) is a national non-profit that supports families and communities by restoring distressed single-family homes, strengthening neighborhoods, and increasing sustainable, affordable homeownership. NCST does this by facilitating sales of distressed homes to community-based partners, providing technical assistance and capital for single-family rehab, and conducting federal policy advocacy grounded in our knowledge of local housing markets. NCST's programs and policy advocacy affirmatively seek to advance racial equity by strengthening neighborhoods of color and promoting racial equity in homeownership.

NCST is strongly supportive of requiring the Enterprises to develop and implement Equitable Housing Finance Plans, and we deeply appreciate the way the Request for Input highlights FHFA's housing equity mission. We believe the Request for Input accurately focuses the Enterprises' attention on a number of today's most critical fair housing issues.

FHFA and the Enterprises have tremendous power to advance equity in housing finance. While the arguments for using FHFA's conservatorship power to advance this goal have long been compelling, the case for doing so is even stronger in light of the pandemic's disproportionate effect on households and neighborhoods of color.[1] If successful, the proposed program will be among the most important initiatives that FHFA has undertaken in its history.

In our comments, we begin by describing actions FHFA can take to enable the Enterprises to set and achieve these ambitious, equity-related goals. We then offer specific comments on a number of the objectives and goals addressed in FHFA's Request for Input (Questions 3 and 4). Next, we identify five additional areas where the Enterprises should focus in their plans (Question 5). We conclude by offering recommendations on program design elements including stakeholder engagement that are specifically informed by lessons from FHFA's Duty to Serve program (Questions 8, 9, and 12).

I. FHFA can do significantly more to enable and encourage the Enterprises to achieve their public purpose to advance equity

The program discussed in FHFA's Request for Input has the potential to meaningfully affect Fannie Mae's and Freddie Mac's progress in fulfilling their responsibility to advance equity in the housing

[1] A number of these impacts are described in Julia Gordon, David Sanchez, Lindsay Augustine, Diane Cipollone, Debby Goldberg, and Lisa Rice, "Protecting Homeownership from the Impact of COVID-19" (National Community Stabilization Trust, National Fair Housing Alliance, and National Association of Realtors), May 2021, https://www.nar.realtor/coronavirus/protecting-homeownership-from-the-impact-of-covid-19

market. However, the effectiveness of their efforts in this area depend heavily on strong follow-through from FHFA.

More specifically, to make the Equitable Housing Finance program a success, leaders of FHFA must dedicate staff to this mission and empower those staff to engage with the Enterprises in a focused way. We have seen FHFA succeed along these lines before with its Office of Fair Lending Oversight, which has been able to establish strong fair lending systems, metrics, and oversight processes. Recent fair lending data and research actions signal that FHFA is similarly investing in the Division of Research and Statistics' focus on equitable housing finance issues. FHFA should also build upon its existing Office of Housing and Community Investment by giving the Office more resources and greater jurisdiction over mission-related activities and programs.

While FHFA has recently taken a number of welcome steps to enable or encourage equitable housing finance activities, there is much work still to be done. In addition to taking affirmative steps, FHFA also needs to dismantle several policy barriers that make it harder for the Enterprises to meet the goals of these Plans. NCST and others identified some of these barriers during the Duty to Serve listening sessions, including policies regarding capital requirements, equity investments, and pilots.[2]

With respect to the capital requirement, while NCST commends FHFA for revisiting its Enterprise capital standard, analysis suggests that under the proposed revision the Enterprises will still be required to hold more capital than is necessary to insulate taxpayers from their risk.[3] Requiring more capital than is necessary will be a significant barrier to achieving FHFA's desired equity goals, perhaps more influential than almost any other factor listed below. NCST suggests FHFA view the capital rule through an equity lens to see if additional changes should be made.

Additionally, when the Enterprises were placed in conservatorship, they were required to wind down their grantmaking operations, which provided much-needed support to mission-focused housing nonprofits around the country. While that directive made sense in the context of what was happening in 2008, now that they have been in conservatorship for 13 years with no clear end in sight, it may be time to rethink whether Fannie Mae and Freddie Mac could engage in some level of philanthropic activity within careful guideposts consistent with conservatorship principles. Traditional philanthropy does not serve mortgage or housing finance organizations well, and the support from the Enterprises was tremendously useful to the field.

II. Recommendations for specific plan activities (RFI Questions 3 and 4)

NCST makes the following specific suggestions regarding plan activities included in FHFA's Request for Input:

A. Automated Underwriting System (AUS) disparities

Reducing the Enterprises' Automated Underwriting System accept-rate gaps is a critical and direct way that the Enterprises can improve racial and ethnic homeownership gaps. As the Enterprises examine

[2] See "FHFA Public Listening Session: Duty to Serve Affordable Housing Preservation," https://www.fhfa.gov/Videos/Pages/Duty-to-Serve-Affordable-Housing-Preservation-FHFA-Listening-Session.aspx

[3] Donald Layton, "Newly-Proposed Changes to the GSE Capital Rule Will Eliminate Harmful Distortions," Harvard Joint Center on Housing Studies, September 21, 2021, https://www.jchs.harvard.edu/blog/newly-proposed-changes-gse-capital-rule-will-eliminate-harmful-distortions

ways to decrease these disparities, we encourage them to examine arbitrary cutoffs such as credit score floors.

Further, FHFA should test each version of the Enterprises' AUS to examine accept-rate gaps and other fair lending issues before new releases are implemented, and require the Enterprises to implement less discriminatory alternatives when issues are identified. Each Enterprise should also self-test in this regard. More broadly, fair lending testing by FHFA and self-testing should apply to all of the Enterprises' significant business activities for fair lending violations, and FHFA should release details of its fair lending examinations to the public.

We also believe the Enterprises should explore "promoting or requiring fair lending self-testing by primary lenders or other counterparties," as described in the Request for Input.

B. Racial or ethnic disparities in loan acquisition

We appreciate FHFA's inclusion of "reducing racial or ethnic disparities in the share of loans acquired by the Enterprise compared to the overall mortgage market" as a potential objective or goal. The racial and ethnic disparities in the Enterprises' market share are a clear and predictable result of the Enterprises' risk-based pricing policies. NCST believes that FHFA and the Enterprises have pursued excessive risk-based pricing in recent years, both through the setting of g-fees/LLPAs and the imposition of risk-based Private Mortgage Insurer Eligibility Requirements (PMIERs). These policies have not only driven up the cost of homeownership for borrowers, but also have directly limited the GSEs' ability to serve many borrowers of color by making GSE financing less attractive than FHA-backed mortgages.

Accordingly, NCST urges the Enterprise to propose activities focused on reducing or eliminating this risk-based pricing in their Plans, and for FHFA to work with the Enterprises to formulate and approve meaningful changes. If the Enterprises do not include such activities in their plans, FHFA must swiftly address this topic on its own as conservator. As FHFA and the Enterprises develop revised pricing policies, it will be important to be transparent with outside stakeholders and coordinate with the Federal Housing Administration about the proposed changes.

C. Servicing equity

The pandemic has had a disproportionate impact on communities of color. As a result, the number of people of color who are delinquent on their mortgages, either in or out of COVID forbearances, is similarly disproportionate. As the number of delinquencies and forbearances declines, the remaining borrowers in that status are likely to be increasingly difficult to reach or assist. If these borrowers are not assisted, loss of homeownership by people of color could exceed the gains that could be made through the other initiatives discussed in this paper.

For this reason, even as the pandemic ebbs, it is critical for FHFA and the GSEs to continue to focus on post-forbearance options for borrowers, including working to raise public awareness about the many good options offered, and on monitoring servicer performance as they manage through the post-forbearance period. FHFA also should monitor loss mitigation outcomes by race, ethnicity, language preference, and geography, and make this data public.

D. Housing supply

NCST strongly supports Enterprise activities to increase housing supply in areas with access to educational, transportation, economic, and other opportunities. To achieve this goal, the Enterprises should propose new initiatives to purchase construction-to-permanent mortgages, both for single-family and multifamily properties. Purchasing these loans on competitive terms is one clear way that the Enterprises can directly increase the supply of new homes. In addition, FHFA should allow limited equity or equity-like investments in the production of new affordable multifamily properties or the preservation of existing naturally-occurring affordable housing in these areas.

Further, if Congress passes the Neighborhood Homes Investment Act, the Enterprises should develop pilot programs to invest in NHIA tax credits and purchase home purchase mortgages supported by NHIA. NHIA is particularly important because it creates supply earmarked for owner-occupancy, which is especially critical as potential homebuyers who need mortgage financing are increasingly losing out to cash buyers.

E. Formerly redlined and opportunity areas

NCST supports a strong Enterprise focus on formerly redlined areas as well as high opportunity areas. In pursuing this focus, FHFA should adopt the definitions of high opportunity areas and areas of concentrated poverty used in the Duty to Serve program for the first Equitable Housing Finance plan cycle. Over time, FHFA should conduct research comparing the current metrics to other alternatives and consider whether changes are warranted.

In addressing this critical issue, FHFA should consider why the Enterprises have not had more of an impact in this area through Duty to Serve. The lack of success may be due to the specific structure of FHFA's "Residential Economic Diversity" concept, such as the need for all qualifying activities to fit squarely within one of the three statutory Duty to Serve markets, or it may be due to other reasons. The Residential Economic Diversity activities that have been most effective are those that directly increased Enterprise purchase of RED-eligible loans through specific underwriting, pricing, or product enhancements. While the Enterprises have laid important groundwork through their research activities, it is unclear that additional publications on these topics will meaningfully impact the market.

III. Recommendations for additional plan activities (Question 5)

NCST recommends that the GSEs consider activities in the following five areas. While we believe each of these areas should be addressed in the Enterprises' initial plans (Question 5), they will also be relevant for future Enterprise plans (Question 11).

A. Distressed property and note sales practices

As post-COVID-forbearance foreclosures begin to take place, the Enterprises should reevaluate their distressed property and note sales practices.

NCST recommends eliminating or significantly restructuring the GSEs' note sales programs, which at present undermine equity and increase the racial homeownership gap. These notes are disproportionately sold to for-profit investors with no mission focus, and properties where the investor does not provide a homeownership retention option are disproportionately sold to investors rather than to homeowners. Where nonprofits are given an opportunity to participate, they are routinely outbid by a for-profit investor, and even if they are not, they are required to purchase at a price artificially elevated by the nature of the auction process. In short, note sales in today's market operate to restrict the supply of affordable homes available for owner-occupancy and change the nature of the neighborhoods where these homes are located.

If the Enterprises are going to sell notes, they should create pools of loans only offered for sale to non-profit and government entities. However, even more important than the identity of the purchaser is whether purchasers achieve outcomes that support the Enterprises' other goals – namely, supporting equity and reducing the racial homeownership gap. As such, FHFA should require all note sales to achieve certain neighborhood positive outcomes, similar to (although stronger than) the types of outcomes required for HUD's Neighborhood Stabilization Outcome pools.

B. Small balance mortgages

The lack of availability of small balance mortgages restricts the ability of low- and moderate-income families to purchase lower-value homes, which is especially ironic since these are the most affordable homes. The lack of mortgage credit in this area leaves many of these lower-priced homes vulnerable either to predatory credit arrangements such as contract for deed/land installment contract or to being acquired by cash buyers for use as rentals. The Enterprises should propose activities that would encourage the origination and servicing of small balance mortgages, including pricing or compensation incentives. They should also assess whether working with additional seller/servicers including CDFIs would enable them to create additional liquidity for these loans.

C. Tenant protection issues, including in Manufactured Housing Communities

We appreciate the Request for Input's discussion of tenant protection issues, and we believe it is appropriate for the Enterprises to prohibit source of income discrimination as a condition of providing Enterprise financing.

In addition, one overlooked opportunity is greater protections for tenants in Manufactured Housing Communities. NCST applauds Freddie Mac's recent announcement that it will only purchase loans supporting Manufactured Housing Communities that meet FHFA's tenant pad lease protections, and we encourage Fannie Mae to do the same. Further, FHFA and the GSEs should study the feasibility of strengthening the tenant pad lease protections, including restrictions on rent increases and tenant right to purchase requirements.

D. Language access

Ensuring equitable access to mortgages and information for households with Limited English Proficiency (LEP) is a critically important fair housing activity. FHFA should require the Enterprises to include in their plans the following concrete steps:

- A framework for mandatory collection, tracking, and reporting of language preference data;
- An analysis of barriers to industry use of existing translated documents and steps to encourage their use;
- A requirement that lenders provide translated documents to borrowers when they are available; and

- A requirement that servicers provide reasonable language access for the GSE-backed mortgages they service.

Additional information on these recommendations is available in the response to this RFI from the National Consumer Law Center and other signatories.

E. Appraisal and valuation equity

FHFA and the Enterprises should play an important leadership role in advancing equity in appraisals and home valuations. FHFA and the GSEs' access to the Uniform Appraisal Dataset makes them extremely well-suited to lead research efforts, and like others, we believe the Enterprises should conduct research evaluating the impact of appraisal standards and alternative valuation services on borrowers and communities of color and whether less discriminatory alternatives exist. Such research would be extremely useful for public stakeholders and for FHFA's leadership in the Interagency Task Force on Property Appraisal and Valuation Equity (PAVE).

IV. Lessons from FHFA's Duty to Serve program (Questions 8, 9, and 12)

There are many important lessons to be learned from the Duty to Serve program as FHFA pursues development and implementation of Equitable Housing Finance Plans. A useful overview of early lessons from the program was released earlier this year by the Lincoln Institute of Land Policy.[4] Ultimately, we believe that the Duty to Serve program has achieved notable early successes, but that a complex program structure, gaps in transparency, and contradictory policy signals from FHFA have limited the program's overall effectiveness and impact. FHFA must continue to iterate and improve its program design if we expect the Enterprises to meaningfully increase liquidity in these markets.

Notably, the similarities between the Duty to Serve program and FHFA's proposal for Enterprise Equitable Housing Finance Plans are sufficiently strong that it may make sense to leverage existing Duty to Serve processes to govern the Equitable Housing Finance Plans process, so long as these Duty to Serve processes are enhanced and strengthened in the process and additional staff are dedicated to these programs. Moreover, to the extent possible, adopting common nomenclature (e.g. activities, objectives, SMART goals), methodology, and formatting across the two programs would help outside stakeholders understand and monitor the program.

We recommend that FHFA consider the following actions:

A. Ratings and public assessments

FHFA should develop a rating system that is measurable and meaningful, just as it has for the Duty to Serve program, and should make those ratings available to the public. One extremely promising element of Duty to Serve is FHFA's use of expert program staff and outside contractors to make judgments about the impact of the Enterprises activities on the underserved markets. However, more than three and a half years after the program officially launched, we still have not seen FHFA's staff-level ratings of the Enterprises' impact on the underserved markets, which limits the public's ability to understand the Enterprises' progress and impacts in these markets. Measuring impact inevitably involves some level of subjective judgment, but we encourage FHFA to be transparent about its views. In both the Duty to

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[4] Jim Gray and George W. McCarthy, "Duty to Serve: The Purpose of Fannie Mae and Freddie Mac and Early Lessons Learned in Underserved Housing Markets." (Lincoln Institute of Land Policy), April 2021.

Serve and Equitable Housing Finance programs, the ultimate goal should be to create processes where FHFA, the GSEs, and market participants share information and jointly learn how to better reach underserved markets.

B. Program transparency and reporting

We encourage FHFA to mirror the Duty to Serve program's strong emphasis on transparency, but to go even further. First, FHFA should build on the successful Duty to Serve Dashboards by spelling out key metrics that it believes indicate success in advancing equitable housing finance, and publishing analysis of Enterprise performance based on those metrics. Second, FHFA should continuously strive to provide as much loan-level data as possible to the public.

We strongly support public reporting along the lines of the Duty to Serve program, but we encourage FHFA to streamline that reporting. As FHFA creates its Equitable Housing Finance program, it should assess the possibility of creating a single reporting structure that would meet the needs of both this program and Duty to Serve.

C. Public input

FHFA's experience with Duty to Serve has also demonstrated that public input is a critical tool in encouraging the Enterprises to set and achieve meaningful goals. It is well worth the effort to accept public comments on proposed plan activities, and it would also helpful for FHFA to establish clear criteria for the approval of plans.

In addition, we are grateful for FHFA's public listening sessions, and we appreciate that FHFA has taken proactive steps to structure them productively, including by focusing them on more limited topics. However, FHFA must be realistic that quick turnaround times and lack of advance notice affect the quality of the input FHFA receives, especially from nonprofit and community organizations that lack the staffing of large trade associations.

In that vein, FHFA and the Enterprises should consider new ways of working with outside stakeholders. The Lincoln Institute of Land Policy has convened an Underserved Markets Coalition to monitor and advocate on the Enterprises Duty to Serve and Equitable Housing Finance activities. FHFA and the GSEs should work closely with this coalition.

Conclusion

Asking the Enterprises to develop Equitable Housing Finance Plans is one of the most important initiatives that FHFA has undertaken to date. The effort appropriately centers those who have for so long been left out of the benefits of homeownership for family stability, health, and prosperity. Both Fannie Mae and Freddie Mac can be doing a lot more to advance equity in our housing markets, which will not only help communities of color, but will also make the entire system stronger and more resilient. NCST is grateful to have the opportunity to comment on this critically important topic.

If you have any questions, please do not hesitate to reach out to David Sanchez, Director of Research and Development, at dsanchez@stabilizationtrust.org or 202-706-7499.