September 8, 2014

Mr. Joseph Prendergast
Manager of Policy Research
Office of Policy Analysis and Research
Federal Housing Finance Agency
400 7th Street, SW
Washington, DC 20024

Re: FHFA's Request for Input on Fannie Mae and Freddie Mac Guarantee Fees and All Related Information

Dear Mr. Prendergast:

On behalf of the state Housing Finance Agencies (HFAs) it represents, the National Council of State Housing Agencies (NCSHA) appreciates the opportunity to respond to the Federal Housing Finance Agency's (FHFA) June 5 request seeking input on the guarantee fees (g-fees) that Government-Sponsored Enterprises (GSEs) Fannie Mae and Freddie Mac charge lenders in exchange for guaranteeing single-family mortgage loans.

NCSHA applauds Director Watt's decision to suspend indefinitely the g-fee adjustments that FHFA initially announced in December and to seek public input before taking any further action. In our view, the planned adjustments seemed arbitrary and could have had unintended negative consequences for the housing market, including making buying a home less affordable for many low- and moderate-income borrowers.

We strongly agree that before any changes are made to the GSEs' g-fees, further review is needed to understand the impact any such adjustments will have on the availability of mortgage credit as well as the GSEs' financial health. Because of the dominant role Fannie Mae and Freddie Mac currently play in housing finance, any adjustments made to the g-fees are likely to have substantial ripple effects across the entire housing market.

We also thank Director Watt and FHFA for renewing its focus on one of the key elements of its core mission: ensuring that the GSEs "serve as a reliable source of liquidity and funding for housing finance and community investment." This emphasis, which has key implications for the discussion about potential g-fee increases, is evident in FHFA's 2014 Strategic Plan for the Conservatorships of Fannie Mae and Freddie Mac (FHFA's 2014 Strategic Plan), as well as the 2014 Scorecard for both firms, which both recognize that "[A] healthy

housing finance market requires liquidity and access across different market segments to provide homeownership opportunities to creditworthy borrowers."

NCSHA appreciates that, as conservator of Fannie Mae and Freddie Mac, it is FHFA's duty to ensure that the g-fees Fannie Mae and Freddie Mac charge are adequate to ensure the firms' fiscal stability and protect taxpayers against potential losses. That being said, FHFA should remain mindful of other important factors when determining how to set g-fees. Specifically, FHFA should be careful not to set g-fees so high that they substantially increase homeownership costs for low- and moderate-income borrowers or jeopardize the housing market's still-fragile recovery.

We urge FHFA to use this public comment and review period as an opportunity to build on its recent efforts to promote an efficient and accessible housing market. To this end, we ask that, when considering how to structure g-fees, FHFA not just consider how to deliver substantial revenue for both Fannie Mae and Freddie Mac, but to give equal consideration to how to ensure a liquid housing finance market capable of serving all creditworthy borrowers. One specific strategy for responsibly accomplishing this balance is to continue to allow and to encourage both Fannie Mae and Freddie Mac to offer advantaged pricing on loans originated through state HFA programs.

State HFAs: A Natural Partner in Supporting Affordable Homeownership

HFAs are state-chartered housing agencies that operate in every state, the District of Columbia, New York City, Puerto Rico, and the U.S. Virgin Islands. Though they vary widely in their characteristics, including their relationship to state government, HFAs share a common mission of providing affordable housing lending help to responsible borrowers who need it. HFAs are well-known for their safe and sound lending programs, which have provided a reliable source of affordable mortgage money for working families over many decades in strong and weak economies.

HFAs have proven over many decades that affordable housing lending done right is good lending. They engage in many best practices proven to strengthen loan performance, such as pre-purchase counseling, high-touch servicing, and flexible yet prudent underwriting. HFAs have never engaged in subprime or other risky lending. Any revenue HFAs generate from their lending and other activities is reinvested by them in furtherance of their affordable housing mission.

FHFA recently recognized the key role that HFAs play in supporting responsible and affordable mortgage lending in its 2014 Strategic Plan, crediting HFAs with having "historically provided access to credit and lower down payment lending for lower- and moderate-income families" and having "proven, strong performance records." The 2014 Strategic Plan and the 2014 Scorecard suggest that both Fannie Mae and Freddie Mac increase their partnerships with

state HFAs. Similar language was recently included in FHFA's proposed Strategic Plan for 2015-2019. We are grateful to FHFA for recognizing the HFAs' history of providing access to credit to underserved families and their loans' strong performance.

Fannie Mae has already found HFAs to be a valuable strategic partner and currently offers state HFAs preferred terms through its HFA Preferred products. This initiative has been a spectacular success. In 2013 alone, 31 HFAs utilized the products to finance over 18,000 home mortgages to low- and moderate-income home buyers, and HFAs predict they will fund over 23,500 loans through this program in 2014. This program provides Fannie Mae an opportunity to responsibly support affordable homeownership while allowing HFAs to reach underserved borrowers, including those they cannot generally serve through traditional tax-exempt bonds, such as non-first-time home buyers and those homeowners who wish to refinance.

Policy Questions

Question 1: Are there factors other than those described in section III—expected losses, unexpected losses, and general and administrative expenses—that FHFA and the Enterprises should consider in setting g-fees? What goals should FHFA further in setting g-fees?

As mentioned above, NCSHA believes that FHFA should ensure that it does not set the fees in such a way so as to restrict access to affordable credit to creditworthy low- and moderate-income borrowers. This component of FHFA's mission should not be subordinated to concerns about maximizing the GSEs' revenue, but should be considered an equally important goal.

NCSHA understands that, as conservator of Fannie Mae and Freddie Mac, FHFA has a duty to ensure that Fannie Mae and Freddie Mac collect enough revenue to adequately protect themselves against potential losses from failed mortgages. However, to ensure the housing market remains liquid and resilient, it will be necessary for FHFA to consider additional factors, including the impact the fees will have on credit availability for all creditworthy borrowers and the effect such fees could have on the to-be announced (TBA) securitization market.

When weighing all of these factors, FHFA should make use of a comprehensive set of data sources that provide a holistic view of the current and projected state of the housing market for all potential buyers. In addition to looking at macro data that provides aggregate information about trends in home sales, prices, and similar data, we urge FHFA to examine specific data about various market segments, particularly first-time home buyers and lower-income borrowers. This will give FHFA a more complete sense of how its policies will impact all aspects of the market. One possibility would be for FHFA to examine data from the Home Mortgage Disclosure Act (HMDA), similar to the method the agency uses to determine the GSEs' affordable housing goals.

Question 2: Risk to the Enterprises increases if the proportion of higher-risk loans increases relative to the proportion of lower-risk loans. This change in mix can occur if lower-risk loans are retained on bank balance sheets instead of being sold to the Enterprises, if more higher-risk loans are sold to the Enterprises, or if the overall mix of originated loans changes. What alternatives, other than risk-based pricing, should be considered? What are the pros and cons of each alternative?

Some level of "risk-based" pricing is a reasonable and efficient tool to ensure that the GSEs' collect enough revenue to adequately protect themselves against the level of risk in their portfolios. Risk-based pricing will also help protect the GSEs from "cherry-picking," where lenders sell their riskiest loans to the GSEs, while keeping their more profitable lower-risk loans on their own books.

That being said, those loans that are traditionally considered riskier, such as those with a high loan-to-value (LTV) ratios or a low borrower credit scores, usually represent a higher percentage of loans made to first-time home buyers and low- and moderate-income borrowers. If the g-fees for these kinds of loans are adjusted upwards too much, it could make them prohibitively expensive for such borrowers, preventing them from accessing credit to purchase homes. FHFA should balance these concerns when structuring a risk-based pricing system.

To ensure that the GSEs collect g-fees that accurately reflect their level of risk while also allowing them to meet their affordable housing missions, FHFA should require the GSEs to consider more than a loan's LTV ratio and a borrower's credit score when determining a loan's risk level and pricing. The GSEs should adopt a holistic analysis that takes into account a number of factors, including any elements that would reduce the loan's risk. As part of this approach, we believe that the risk level of loans originated through state HFA programs should be substantially reduced.

As we described earlier, state HFAs have a strong track record of responsible affordable housing lending. A 2013 study conducted by the University of North Carolina Center for Community Capital credited HFAs with proving that high LTV lending done right can be successful. In recognition of HFA loans' strong performance, Fannie Mae does not apply loan-level price adjustments to loans originated through its state HFA Preferred program. A review Fannie Mae conducted in 2011 found that its HFA-financed loans outperformed its other affordable housing program loans. Reducing the risk-based pricing for HFA loans will not only make it easier for HFAs to assist creditworthy low- and moderate-income borrowers through the GSEs, but will also accurately reflect the reduced level of risk HFA loans pose relative to other loans with similar LTVs.

In addition, FHFA should also allow Fannie Mae and Freddie Mac to charge lower g-fees for high-LTV and/or low credit score borrowers who receive pre-purchase housing counseling. Numerous independent studies have demonstrated that first-time home buyers who receive housing counseling are substantially less likely to become delinquent on their

mortgages and lose their homes to foreclosure. State HFAs have long recognized the importance of housing counseling, and virtually all have integrated it in some fashion into their homeownership programs. Eliminating risk-based fee increases for loans to borrowers that have completed counseling courses will encourage more potentially high-risk borrowers to participate in such courses, potentially reducing the firms' losses.

Question 3: Currently, target return on capital and the amount of capital largely determine required g-fees. What factors should FHFA and the Enterprises consider in setting target return on capital and amount of capital required? How should the Enterprises allocate capital across risk buckets?

The g-fees should always be set at a level that will allow Fannie Mae and Freddie Mac to build up and maintain a healthy level of capital that allows them to adequately protect against potential losses. However, FHFA should also take care not to set the g-fees at such a high level that GSE-loans become prohibitively expensive for more borrowers, resulting in a weaker housing market and reduced access to credit. Striking this balance is of paramount importance to the housing market and consumers.

At this time it would appear that GSEs' g-fees are already set at a level that is above what is needed to support their current portfolios. In addition, they have already paid back all of the financing they have received from the federal government and have even sent the Treasury Department over $25 billion in additional revenue. At the same time, the g-fee increases that FHFA has implemented in recent years have contributed to the difficulty many creditworthy borrowers have encountered in trying to obtain affordable home financing. We thus urge FHFA to adjust g-fees to a level that will allow the GSEs to build up the capital they need but will also support a robust and liquid housing finance market.

Questions 4, 5, and 7:

- ***At what g-fee level would private-label securities (PLS) investors find it profitable to enter the market or would depository institutions be willing to use their own balance sheets to hold loans? Are these levels the same? Is it desirable to set g-fees at PLS or depository price levels to shrink the Enterprises' footprints, even if this causes g-fees to be set higher than required to compensate taxpayers for bearing mortgage credit risk and results in higher costs to borrowers?***
- ***If the Enterprises continue to raise g-fees, will overall loan originations decrease? That is, will Enterprise loans decline without a commensurate increase in private capital?***
- ***Is it desirable for the Enterprises to (a) charge higher g-fees on high credit score/low LTV loans if it causes these loans to be insured/securitized through PLS or (b) held on depository balance sheets, rather than guaranteed by the Enterprises?***

The PLS market in recent years has been largely dormant. What limited activity has occurred has largely been limited to securities composed entirely of "jumbo" loans with predominately low LTVs that have been extended to higher-income earners. This suggests that there is little investor interest for PLSs comprised of more conventional mortgages and probably even less appetite for securities comprised of high LTV/low credit score loans. Much of this lack of interest is probably a reflection of investor wariness of PLSs following the collapse of the housing market, as well as general investor concern over taking on interest rate risk.

Some might argue that a substantial g-fee increase is necessary to change relative prices enough to jump-start the PLS market. Such an increase is likely to make GSE-guaranteed loans prohibitively expensive for many borrowers. Also, we believe there is little indication that the private market would be willing and/or prepared to significantly expand their business at this time.

While a vibrant PLS market is likely to be a key part of a well-functioning housing finance market in the future, we do not believe that time has come. We strongly urge FHFA not to increase g-fees for the purpose of increasing PLS activity, an effort we believe would be largely fruitless—and likely harmful to affordable lending.

Question 8: What approaches or alternatives should FHFA consider in balancing increased use of risk-based pricing with the HERA mission requirements of (1) liquid national housing markets and (2) acceptability of lower returns on loans made for low- and moderate-income housing?

NCSHA and its HFA members strongly support the mission requirements authorized under HERA and believe that they should always be taken into consideration by FHFA and the GSEs when setting policies. We are encouraged by recent actions taken and statements made by FHFA leaders that indicate that FHFA is placing a renewed emphasis on these requirements.

With regard to potential approaches for balancing the use of risk-based pricing with the GSEs' missions, we refer you to our answer to Question 2, in which we urge that Fannie Mae and Freddie Mac be allowed to reduce or eliminate risk-based fee increases for high LTV/low credit score loans originated through state HFA programs. FHFA should also consider reducing or eliminating risked-based fees for those loans that contain other features proven to lower the likelihood of default.

Question 11: Taking into consideration that FHFA has previously received input on state-level pricing adjustments, do the g-fee changes proposed in December 2013 have any additional implications that should be considered in deciding whether to price for the length of state foreclosure timelines, unable to market periods or eviction timelines? Foreclosure rates are dramatically dropping, fees should also be dropping. Are there interactions with other pricing

components under consideration that FHFA should consider in making decisions on the state-level adjustments?

NCSHA strongly opposes any effort to vary the GSEs' g-fees by state based on foreclosure timelines. Such a policy would:

- Unfairly punish states for adopting strong consumer protections;
- Represent an unwarranted federal intrusion into a traditionally state-based area of policymaking;
- Set a dangerous precedent that would detract from the GSEs' core mission of supporting a liquid housing market; and
- Jeopardize the housing market in states that are already struggling to recover.

For more details on NCSHA's position on this issue, we have attached the comments we submitted to FHFA in November 2012 (Attachment A), in response to its initial proposal to increase g-fees for five states.

Question 12: Are there interactions with the Consumer Financial Protection Bureau's Qualified Mortgage definition that FHFA should consider in determining g-fee changes?

NCSHA does not believe that there is any reason for FHFA to consider the Consumer Financial Protection Bureau's (CFPB) definition of "Qualified Mortgage" (QM) when setting g-fees. CFPB's final Ability-to-Repay/Qualified Mortgage Rule classifies all loans guaranteed by either Fannie Mae or Freddie Mac as QMs as long as the GSEs remain in conservatorship, so all GSE-guaranteed loans currently qualify for the same level of legal protection under CFPB's standards.

In the event that FHFA determines that Fannie Mae and Freddie Mac should charge lower g-fees for those loans that meet all aspects of the QM definition's standards, independent of whether they are guaranteed by Fannie Mae or Freddie Mac, we ask that you explicitly apply the same fee reduction to state HFA loans, which are exempt from the Ability-to-Repay rule. CFPB granted HFAs an exemption from this rule because it recognized that, given HFAs' strong track record of responsible lending to low- and moderate-income borrowers, forcing them to comply with the rule's requirements would provide little benefit to consumers and might limit lower-income borrowers' access to affordable home lending.

Because HFA loans are exempt from the requirements of the Ability-to-Repay rule, they are not legally considered to be QMs. However, as we noted above, CFPB did not exempt HFA loans because they felt that they were risky and should not be afforded the legal protections extended to QM loans. Rather, HFA loans were exempted because they had demonstrated an ability to responsibly and effectively serve low-and moderate-income consumers. Consequently, failing to extend any reduction in g-fees for QMs to state HFA loans would be unfair and hinder the GSEs' ability to responsibly serve their affordable housing missions.

Thank you for your consideration. We would be happy to discuss these issues with you at your convenience.

Sincerely,

Garth Rieman
Director of Housing Advocacy and Strategic Initiatives

ATTACHMENT

NCSHA'S RESPONSE TO FEDERAL HOUSING FINANCE AGENCY

PROPOSAL TO INCREASE G-FEES FOR MORTGAGES ORGINATED IN STATES WITH

HIGH FORECLOSURE-RELATED COSTS

NOVEMBER 26, 2012

November 26, 2012

Mr. Edward J. DeMarco
Acting Director, Federal Housing Finance Agency
400 Seventh Street SW, Eighth Floor
Washington, DC 20024

RE: No. 2012–N–13

Dear Mr. DeMarco,

On behalf of the state Housing Finance Agencies (HFAs) it represents, the National Council of State Housing Agencies (NCSHA) writes to express our strong opposition to the Federal Housing Finance Agency's (FHFA's) recent proposal to increase the guarantee fees that the Government Sponsored Enterprises (GSEs) charge on single-family mortgages issued in five states. We believe that this proposal unfairly punishes states for adopting reasonable consumer protections and represents an unwarranted effort by a federal agency to influence state policy.

We are also deeply concerned that this proposal will set a dangerous precedent that will detract from the GSEs' mission to expand access to affordable home financing. Finally, the increase in guarantee fees will weaken the already struggling housing markets in these states and make it more difficult for lower-income consumers to obtain affordable home financing.

Do Not Intrude on States' Rights to Set Consumer Protection Laws

FHFA's proposed rule says its goal is to increase fees on those states where foreclosure-related costs are significantly higher than average. In calculating each state's costs, FHFA utilizes a vague formula based on the length of time it takes the GSEs, on average, to foreclose upon a loan and the costs that lenders and investors are responsible for when carrying a nonperforming loan.

Under this formula, FHFA singles out for fee increases five states that have instituted strong consumer protections designed to help homeowners contest wrongful foreclosures and seek out options to remain in their home. Many of these protections were put in place as a direct response to the wave of wrongful foreclosures that occurred following the financial crisis.

FHFA attributes the states' foreclosure-related costs to such policies. But, in fact, many of these state policies reduce foreclosures and foreclosure-related costs. The FHFA formula does not appear to factor in the reduction in the number of foreclosures and associated costs that results from these policies.

We are concerned that FHFA's policy, given the GSEs' significant role in the housing market, may inappropriately discourage states from adopting additional consumer protections. FHFA notes in the proposed rule that it plans to periodically adjust its guarantee price guidance to reflect the impact of newly enacted state laws that affect foreclosure timeliness and costs. Since many consumer protections will likely increase both these factors, states will have to be wary of implementing such initiatives out of concern that it could result in increased guarantee fees. This is an inappropriate effort on the part of a federal agency to influence state policy.

FHFA seeks comment on whether it should adopt a system in which all states would be assessed an upfront credit or fee based on how its foreclosure-related costs differ from the national average. We oppose such a system. If one were established, it would represent unwarranted interference into state policy-making by creating an incentive for states to weaken consumer protections in order to secure lower borrowing fees for their citizens.

Do Not Set a Dangerous Precedent that Detracts from the GSEs' Mission

The GSEs were created to provide a stable source of funding for residential mortgages across the country that would allow borrowers everywhere to secure affordable home lending. Fannie Mae and Freddie Mac have charged the same guarantee fees to all borrowers regardless of where they reside, making it possible for lenders to originate loans to consumers in rural and other underserved areas.

By proposing that certain states pay increased fees, FHFA is breaking from the uniform fee policy that has served the GSEs and the nation so well. Reversing this well-established policy would detract from the GSEs' critical mission to make homeownership affordable for working- and middle-class families throughout the country. National and regional lenders may be prompted to curtail their lending in states with higher guarantee fees, limiting options for consumers. In addition, once the precedent has been established for charging different fees in different states based on their consumer protection and housing policies, it raises the possibility FHFA and the GSEs will adjust guarantee fees based other factors.

Do Not Undermine the Struggling Housing Market

While there are several signs that the housing markets in the affected states have begun a slow recovery, their markets remain fragile. Given the dominant role that the GSEs currently play in the single-family mortgage market, these proposed additional fees could undermine the

housing recovery in the impacted states by increasing monthly payments and deterring potential buyers. This is especially likely when considered together with FHFA's recent decision to increase guarantee fess on all mortgages by an average of 10 basis points and increased efforts by the GSEs to force lenders to repurchase loans. These steps combined have made lenders more reluctant to originate loans to otherwise creditworthy borrowers. The additional fees will amplify these negative effects.

The increased fees will disproportionately impact lower-income borrowers, for whom the fees represent a larger share of their income. While the expected average monthly increase that borrowers will face appears to be relatively low ($3.50 to $7.50, according to FHFA's estimate), such an amount's effect can be substantial for low-income borrowers. Further, the increased fees will reduce these borrowers' disposable incomes, thus limiting their resources for other basic needs.

NCSHA understands that FHFA's role as conservator requires it to take steps to improve the GSEs' financial condition. However, increasing guarantee fees for loans originated in certain states is a counterproductive approach that could end up doing more harm than good for the GSEs by making it more difficult for consumers to purchase a home, undermining states' consumer protection efforts, and disrupting a uniform fee policy that has been a cornerstone of American's housing finance system. We strongly urge FHFA to rescind this proposal.

Thank you for your consideration of our comments. Please do not hesitate to contact me if we can provide additional information.

Sincerely,

Garth Rieman
Director of Housing Advocacy and Strategic Initiatives