January 12, 2023 (revised from December 5th, 2022 comment)

Marcea Barringer
Supervisory Policy Analyst
Attention: Duty to Serve 2022 RFI
Federal Housing Finance Agency
Eighth Floor, 400 Seventh Street, S.W.
Washington, D.C. 20219

RE: Request for Input on Fannie Mae and Freddie Mac 2022 Duty to Serve Plan Modifications

Dear Ms. Barringer and esteemed colleagues,

We thank the Federal Housing Finance Agency (FHFA) for providing this opportunity to respond to the Request for Input (RFI) on Fannie Mae's and Freddie Mac's 2022 Duty to Serve (DTS) Plan Modifications. Grounded Solutions Network (Grounded Solutions) has long been an active participant in the duty-to-serve process, and we appreciate the chance to provide our input on the proposed Plan modifications. Under DTS, Grounded Solutions has played a leadership role in representing the interests of shared equity homeownership programs and borrowers. These have included community land trusts, nonprofits with shared equity homeownership programs, government-based inclusionary housing programs and deed-restricted housing programs that are all designed to provide homeownership opportunities with lasting affordability.

In this comment today, we would first like to provide some general comments for FHFA to take under advisement about the current proposed modifications. We will then focus on our deep concerns related to the Government Sponsored Enterprises' (GSEs) progress under DTS as it relates to increasing liquidity and access to mortgages for shared equity borrowers, including an explanation on why we believe further modifications to the Plans are warranted.

GENERAL COMMMENTS

While the RFI appears focused on gathering input on the activities that the GSEs propose for modification, we believe that it is critically important for FHFA to consider what modifications are *missing* from their proposals that could strengthen the performance of the GSEs to meet the mandate of serving underserved markets. The GSEs have an opportunity during plan modifications to not only strike or lessen their proposed activities, but to also modify or change activities that have yet to result in the outcomes they expected to best serve underserved markets and/or increase or deepen productive activities to support even more ambitious goals.

We are surprised to not see substantial proposed changes to the Plans in light of inflation, real estate market trends, and housing finance changes that have taken place since the Plans were created. In multiple recent meetings that we have participated in with GSE staff, we have heard them acknowledge that inflation and market changes are increasing the challenge of reaching their DTS objectives. This is particularly true in the single-family space, where the impact of rising interest rates on lower income buyers has been referenced as a reason for potentially not meeting loan purchase targets.

This raises two questions:

(1) Given the GSE's acknowledgement that the current economic and real estate market conditions are anticipated to injure their DTS performance, why are they not proposing further modifications that reduce loan purchase targets?

(2) If the state of the markets is so different from when the Plans were originally developed, why are the GSEs not proposing radically different and more intensive activities that respond to these new market challenges?

We see two potential explanations for this inaction on the part of the GSEs. We previously commented that the GSEs' loan purchase targets were too low. It is possible that the GSEs initially set loan purchase targets so low in many activities that current market setbacks do not threaten their performance. It is also possible that the GSEs anticipate that current market challenges will act as a sufficient excuse during the DTS evaluation to explain their underperformance, and they are failing to propose the Plan modifications that would be needed to overcome market challenges and meet performance targets.

The GSEs should not cite market challenges to explain any DTS shortcomings while also failing to propose substantial modifications to their DTS plans to address those market challenges. FHFA should have required them to initially set ambitious enough loan volume goals and other associated activities when the market conditions were more conducive to reaching purchase goals, and FHFA must hold them accountable for making needed adjustments related to current market conditions to advance DTS goals now that reaching underserved markets has become even more challenging.

SHARED EQUITY HOMEOWNERSHIP COMMENTS

Neither of the GSEs has included proposed changes to their Activities or Objectives related to shared equity homeownership. We are surprised by this, as Grounded Solutions has long provided both with public feedback on barriers related to increasing liquidity and access to mortgages for shared equity borrowers. Unfortunately, by not following this feedback, some of the actions they have pursued under DTS have increased barriers or failed to remove barriers for shared equity borrowers to access loans. We ask that FHFA get more involved in these matters and work with us to ensure that the GSEs meet their DTS mandate for shared equity homeownership.

For 2022, both GSEs included in their Plans activities and objectives related to building upon a Model Deed Restriction, the development of which was part of both of their previous Underserved Market Plans. These activities and objectives included, but were not limited to the following:

- Under Fannie Mae's Regulatory Activity H. Objective 1, "execute policy and programmatic changes necessary to accommodate model deed restriction documents" in 2022.
- Under Freddie Mac's Regulatory Activity 10. Objective B, "deploy a model template to shared equity program providers for income-based deed-restricted properties to facilitate standardization of the language that is used to support resale restrictions across applicable shared equity programs" and "provide guidance to Freddie Mac sellers on the model documents by making collateral materials available as well as publicizing the guidance on our Single-Family website" in 2022.
- Under both of these Activities, promote the marketing and adoption of the Model Deed Restriction.

To provide background, the Model Deed Restriction (MDR) was completed in 2021 and made public on Grounded Solutions' website along with associated commentary. The MDR and its commentary were developed by Reno & Cavanaugh, LLC on behalf of Grounded Solutions Network in partnership with Fannie Mae and Freddie Mac (the Government Sponsored Enterprises) with substantial guidance from an Inclusionary Housing Advisory Group of practitioners. The objective of this project was to promote best practices, standardize the field while providing adequate flexibility in program design, and increase access to mortgage financing for shared equity homebuyers. Our hope was that both Enterprises would expressly state that programs using the MDR were in compliance with their Selling Guides and design incentives for lenders who were originating loans to shared equity borrowers during transactions that used the MDR.

The final MDR template includes color coding that specifies exact language that cannot be changed in order to comply with the Selling Guides. Because this project was not under mandated alignment, both GSEs had the option to then incorporate the MDR template into their Selling Guides so that lenders felt confident that, if a shared equity program was using the MDR template, the loan could be originated and sold to either GSE and be in compliance with both Guides. What has happened instead is that Freddie Mac has minimally incorporated mention of the MDR into its Selling Guide and incorporated requirements that render the MDR out of compliance for meeting Selling Guide requirements, while Fannie Mae has yet to introduce Selling Guide changes per their Underserved Market Plan activities that would incorporate the MDR and minimize lender burden for evaluating Guide compliance.

Additionally, in 2015—prior to the implementation of DTS—Grounded Solutions provided both Enterprises with a white paper that provided a detailed analysis of their Selling Guides and the barriers they pose for shared equity transactions (broken out by ground leases and deed restrictions). Grounded Solutions Network also submitted public comments on the GSEs' 2018-2020 Underserved Market Plans that made reference to this white paper and summarized barriers to increasing access to mortgages for shared equity borrowers for each GSE. We also submitted a public comment on the proposed Underserved Market Plans for 2022-2024. In this letter, we praised both GSEs for developing the MDR but stated, "they are falling short on following this effort through by investing in a comprehensive and effective strategy to get the MDR adopted and implemented." We requested further detail on their plans for incorporating the MDR into the Selling Guides and acknowledged that major changes are needed to address vague, contradictory, or overly complex aspects of the Guides for lenders originating loans to shared equity borrowers using deed restrictions. For instance, we have pointed out to both

GSEs that their Guides have sections related to second mortgages that limit appreciation sharing in ways that render shared equity programs not compliant with the Guides. We have also recommended that both GSEs make a separate "shared equity homeownership" section in their Guides because currently a lender must cross reference sections pertaining to second mortgages, resale restrictions, community land trusts, and appraisals to understand how to treat various loans for shared equity borrowers. To date, <u>little-to-no action has been taken on our recommendations</u>.

Instead, <u>Freddie Mac has introduced *additional* requirements to its Selling Guide for shared equity programs using deed restrictions, and Fannie Mae has yet to introduce changes to its Selling Guide to capitalize upon the MDR or minimize lender burden</u>. A consistent piece of guidance that we have provided since the beginning of DTS is to not ask lenders, who are completely unqualified to evaluate programs, to underwrite aspects of shared equity homeownership programs or whether the programs are abiding by best practices. When lenders are asked to do this, it adds <u>time and burden to underwriting the loan, introduces inconsistency in the assessment of programs, and results in uncertainty about what needs to be documented during underwriting to pass an audit</u>. As a result, lenders opt not to originate conforming loans for shared equity borrowers, or they do not sell the loans to Fannie Mae or Freddie Mac. Instead, Freddie Mac has incorporated vague requirements for lenders to ensure there are "established procedures to screening, processing applicants and approving transactions" and "procedures to approve capital improvements on the property and guidelines that allow the Borrower to receive credit for any cost of capital improvements." Meanwhile, neither Fannie Mae nor Freddie Mac has addressed the sections of their Guides that pertain to limitations in appreciation sharing for shared equity transactions, which requires lenders to review complex resale formulas that rarely can be interpreted based upon Guide requirements.

The Selling Guides are so convoluted and difficult to follow that Grounded Solutions senior staff specializing in mortgage financing has been unable to understand what aspects of the Guides pertain to various shared equity loans. We have received unclear guidance on what documentation lenders would be required to collect to meet the requirements of the Guides. <u>If shared equity experts cannot sort through what requirements are necessary for a loan to be in compliance, how could lenders with little to no expertise in affordable housing and shared equity homeownership programs be expected to do so?</u>

Adding an additional complication, each GSE is using a different approach in its Guide for shared equity loans using deed restrictions or the Model Deed Restriction, and both approaches have undermined the purpose the MDR template: minimizing lender burden during underwriting and ensuring that adoption of the MDR would produce compliant loans. Freddie Mac has incorporated various requirements into its Guide that now contradict the terms in the MDR. For instance, the Guide does not permit the shared equity program to recoup excess proceeds after foreclosure while the MDR does. Meanwhile—despite what it states in its Underserved Market Plan—Fannie Mae's Guide remains silent a year later on the MDR, and therefore, a lender must review multiple sections of the Guide just like any other deed restriction designed for shared equity homeownership.

Misguided changes or inaction create problems for both shared equity programs and the lenders who work with them and are fundamentally inconsistent with the GSEs' stated objectives to reach this underserved market that is so critical to addressing the racial wealth gap. How are staff at a shared equity program supposed to possibly understand how to structure their legal documents for a loan to be able to be sold to either Freddie Mac or Fannie Mae? Meanwhile, a lender will have to intensively review every MDR to determine what changes are needed to match Freddie Mac's Selling Guide (which runs counter to what is coded in the template) *and* review Fannie Mae's Selling Guide without being entirely clear if requirements across the GSEs are aligned or contradictory.

In summation, over the course of duty-to-serve, both Enterprises have <u>not adequately increased</u> access to mortgages for shared equity borrowers and <u>not adequately increased</u> liquidity in the shared equity field, especially for borrowers with shared equity deed restrictions. Their Selling Guides have not decreased lender burden for originating and selling loans for shared equity borrowers, specifically those in deed-restricted housing programs. <u>Their implementation (or lack thereof) of their Objectives and Activities for shared equity homeownership has not enabled the intended result of the duty-to-serve rule. This is unacceptable and warrants substantial and more detailed proposed Plan Modifications</u>.

Grounded Solutions Network understands that the GSEs are broadly concerned about "consumer protections" and "safety and soundness." Therefore, we would like to point out that shared equity homeownership programs have a mission-based and financially vested interest in the success of their homeowners. Despite this commitment, the concerns outlined here demonstrate that the shared equity homeownership field is being disproportionately scrutinized on their policies, practices, and affordable housing model relative to other government-based or nonprofit-based affordable homeownership models or programs. For instance, when second mortgages are provided to make homeownership affordable for lower income households, these programs are not required in the Guides to evidence their screening, processing applicants, and transaction approval process. When second mortgages incorporate a shared appreciation component that is not related to permanent affordability, these programs are not required to illustrate their capital improvements approval procedures and provide credits. Why is Freddie Mac exerting so much oversight specifically over shared equity homeownership programs, especially when these programs have demonstrated a mission and material interest in protecting and ensuring the ongoing success of lower-income homeowners?

In terms of "safety and soundness" claims, shared equity homeownership transactions have LTVs anywhere between 50-80% because the programs sell their homes at such substantially discounted prices to lower income buyers. This demonstrates that shared equity loans have a very low risk profile relative to other affordable products and affordable homeownership models that have much higher LTVs. Why is Freddie Mac undercutting the terms in the approved MDR by insisting that no excess proceeds can go to the shared equity program after the first mortgage lien holder is made whole in instances of foreclosure? Why is Fannie Mae taking so long to incorporate the MDR into their Selling Guide?

Grounded Solutions is committed to ensuring that shared equity homeownership programs protect their consumers and are safe and sound lending opportunities. We have provided the GSEs with various solutions to address their concerns and help to standardize the field, without increasing burden on lenders or decreasing liquidity to the field. These include:

- Optimizing the use of the Model Deed Restriction so that any program using the MDR is automatically in compliance with both Selling Guides;
- Amending the Model Ground Lease to have clear and consistent required language to comply with both the Selling Guides (similar to what is proposed for the MDR);

- Adopting a program certification through which any program that is certified is automatically deemed in compliance with the Selling Guides[1];
- Issuing consistent Guidance on how shard equity properties should be appraised across GSEs;
- Removing unnecessary requirements in the Selling Guides; and
- Consolidating and simplifying the Selling Guides with a dedicated shared equity section.

At this juncture, we ask that FHFA hold Fannie Mae and Freddie Mac accountable for changing their Objectives and Activities related to shared equity homeownership, so that the outcomes actually advance—rather than run counter to—the mandate of duty-to-serve.

As a first step, we request that FHFA and possibly your contractors who advise on shared equity, convene separate in-person meeting with each Enterprise and GSN, Lincoln Institute and other shared equity stakeholders to develop an action plan to correct these deviations from their prior commitment to shared equity.

Sincerely,

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About Grounded Solutions Network

Grounded Solutions Network (Grounded Solutions) supports strong communities from the ground up by furthering housing solutions with lasting affordability and inclusionary housing policies to advance racial and economic equity. We are a national nonprofit membership organization of over 260 community land trusts, nonprofits, inclusionary housing government programs, and allies located in 46 states, Washington DC, and Puerto Rico that all support the creation and preservation of housing with lasting affordability. These models go by many names, such as "shared equity homeownership," "community land trusts," "below market-rate programs" or "deed-restricted housing."[2] Our members and the broader field have created over 250,000 shared equity homes (aka permanently affordable owner-occupied homes) and approximately 150,000 permanently affordable rentals. We provide our members and the broader field with training, technical assistance, policy and program design, resources, research, and advocacy. Grounded Solutions champions evidence-based policies and strategies that work. We promote housing solutions that will stay affordable for generations so communities can stabilize and strengthen their foundation, for good.

[1] Fannie Mae is currently pursuing a certification with Grounded Solutions, and we encourage them to maximize its utility and ability to increase access to mortgages.

[2] Despite similarities in the name, for-profit or nonprofit "shared appreciation mortgages" are not designed to restrict the sales prices of homes or keep properties permanently affordable, and therefore, are *not* part of the shared equity homeownership landscape.

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About the Lincoln Institute of Land Policy

The Lincoln Institute of Land Policy seeks to improve quality of life through the effective use, taxation, and stewardship of land. A nonprofit private operating foundation whose origins date to 1946, the Lincoln Institute researches and recommends creative approaches to land as a solution to economic, social, and environmental challenges, including housing affordability; efficient and equitable tax systems; reduced poverty and spatial inequality; fiscally healthy communities and regions; and functional land markets and reduced informality.