May 15, 2023

Director Sandra Thompson
400 7th St. SW
Washington, DC 20219

RE: Request for Input on Enterprise Single-Family Social Bond Policy

Dear Director Thompson and esteemed colleagues,

We applaud the Federal Housing Finance Agency (FHFA) for taking a proactive and contemplative approach in this Request for Information (RFI) for how the Government-Sponsored Enterprises (GSEs) may create single-family social bonds to have a meaningful impact on disadvantaged households' ability to access sustainable homeownership[1].

Our comment proposes that FHFA should utilize an approach to developing single-family bond policy (or social index pools with disclaimers) that prioritizes the generation of revenue devoted to the production and preservation of affordable homeownership opportunities, aligned with the GSEs' obligations under Duty-to-Serve (DTS) and the forthcoming Equitable Housing Finance Plans (EHFPs) rules.

We largely address questions A-1, A-2, B-1, and C-1 from the RFI, although the structure of our letter does not directly match the questions.

Our proposal:

We recommend that the FHFA permits the GSEs to issue single-family bonds (or perhaps even specified pools with certain disclosures) on a broad application of their single-family mortgage business that meets a basic definition of "social benefit" and provides sufficient information for investors to pay maximized premiums on these securities. The parameters on eligible loans should prioritize volume and maximizing pay-ups without introducing disruption in the standardization and opacity in the TBA market. The GSEs should then be required to take the additional proceeds from the pay-ups and create a joint Homeownership Trust Fund (HOTF), where funds should be used to create and

[1] The terms disadvantaged and underserved refer to the broad swath of households who are unable to access homeownership due to systemic racism, lack of economic opportunity, or geographic disparities in access to safe and sound financing.

preserve affordable owner-occupied homes for lower-income households, especially people of color.

The HOTF should have sufficient flexibility to creatively address single-family homeownership activities as described in the Duty-to-Serve rule as well any activities described in the forthcoming Equitable Housing Finance Plans rule. However, the majority of the funding should be used to create and support shared equity homeownership programs, which would yield a permanently affordable stock of homes that will enable people of color and lower-income people to enter and sustain homeownership now and into the future. This approach would yield below market-rate homes that are accessible and affordable to lower-income people of color, enable homeowners to build wealth, and contribute to the overall supply of affordable housing in the country.

Much attention will need to be paid to the governance and administration of the HOTF, which we would be happy to discuss further.

Rationale

Due to the dwindling supply of so-called starter homes that low- or moderate-income households can afford, addressing access to mortgage financing is categorically insufficient to help a large proportion of these households enter and sustain homeownership. Even when these households are mortgage-ready, their incomes relative to the cost of homes in many markets keeps homeownership out of reach.

Hence, while the GSEs can play a critical role in enabling mortgage financing to be more affordable and accessible to disadvantaged households, the impact of these types of interventions — whether lender incentives, rep and warrant relief, changes in credit score requirements, etc. — remains constrained by the lack of affordable homes for the homebuyers to borrow against. Additionally, these interventions translate to relatively minor financial benefits or minor changes in the number of qualifying borrowers, resulting in very modest increases in the disadvantaged households in underserved markets who ultimately purchase homes. The impact of these changes is too insignificant to enable the vast majority of disadvantaged households to purchase and afford homeownership, especially since they do not address the root problem: the lack of affordable homes available for purchase.

This story is plainly told when evaluating the performance of the GSEs in their recent Equitable Housing Finance Plans' progress reports. Unlocking mortgage financing or minor borrower benefits, such as modest down payment support or credit score requirement changes, is not meaningfully moving the needle for the communities who are meant to benefit, especially Black and brown households.

Therefore, in this letter we are calling for FHFA and the GSEs to focus any single-family social bond policy on creating and preserving affordable owner-occupied homes. We believe that FHFA and the GSEs must approach single-family social bonds with an out-of-the-box approach, one that stretches beyond the customary secondary market levers on financing to instead yield funding for the production and preservation of affordable homes.

Why this approach?

Based upon the RFI, we assume that FHFA is thinking about “benefit” in two ways: (1) designing loan eligibility for entry into the social bonds in such a way that lenders are more likely to originate loans to disadvantaged borrowers or underserved markets, and (2) passing through some proportion of the pay-ups on any social bonds to the borrowers of loans that fulfill social bond requirements.

We see several weaknesses in this approach. First, if loan eligibility for social bonds is too narrow then there will be insufficient loan volume for lenders and investors to build a meaningful capital markets strategy on the issuances. The result is that originating institutions won’t meaningfully invest in expanding their lending to disadvantaged borrowers or underserved markets, since a lower loan volume results in diminished financial incentives. The investors will also not be willing to pay a maximum pay-up amount without sufficient and reliable volume, watering down the additional proceeds.

Second, even if the loan eligibility is set to moderately or maximally capture loan volume in the social bonds to activate the interest of investors and lenders, the question then becomes how should the additional proceeds that flow back to the GSEs be used for social benefit? Incentivizing the lenders to originate more loans that fulfill the social bonds may be somewhat helpful. However, this approach would perpetuate the focus on mortgage liquidity for disadvantaged borrowers and underserved markets, which is insufficient given the lack of affordable homes on which to originate mortgages. For instance, if you ask either of the GSEs why they aren’t purchasing more shared equity loans, they will likely tell you they are constrained by the overall supply of shared equity homes. Increasing the number of shared equity homes requires subsidies in order to make the homes permanently affordable, but these subsidies remain scarce. The same issue applies to Special Purpose Credit Programs (SPCPs). A key challenge for SPCPs in helping households of color to enter homeownership is simply the lack of affordable housing for purchase and the lack of subsidy dollars for down payments. Increasing originators and origination is clearly a problem, but it’s not the only problem, nor is it the biggest.

Flowing from this, the question becomes why not direct the additional proceeds from the social bond issuance back to the homeowners the social bond comprises? By definition, these borrowers have already achieved homeownership. If we want to expand the reach of the GSEs' social benefit into the most disadvantaged communities, then directing the social bond proceeds back to the homeowners is not the most impactful use of pay-ups (not to mention that an astounding amount of infrastructure would need to be built out by originating institutions, servicers, and the GSEs to accurately track the distribution of those funds). Moreover, even if we instead focus on directing some portion of the proceeds back to any eligible potential borrowers, the magnitude of benefit is likely insufficient to serve anyone but those on the verge of homeownership who need minimal assistance (e.g. small down payment assistance or closing cost relief). *In order to effectively serve disadvantaged households — especially households of color, who disproportionately have lower incomes, less savings, and lower credit scores — FHFA and the GSEs must find ways to more deeply subsidize homeownership and to ensure more affordable homes are available for purchase*.

This is why our proposal focuses on maximizing pay-up proceeds and providing flexible funds to produce and preserve affordable homeownership rather than focusing on loan eligibility and liquidity as the primary drivers of social benefit. In order to capture pay-ups on single-family UMBS issuances that will yield investors greater profits, FHFA should consider whether this can be done with single-family loans that are not necessarily packaged into "social bonds" or whether this can be done with disclosures on certain single-family pools. There is currently already investor demand for pools with lower pre-payment rates. These already include some loans in underserved markets or to disadvantaged borrowers, hence the focus should be on ensuring that their pricing maximally captures profits and regulating how those profits are used by the GSEs, namely for increasing the affordable homeownership stock.

A very important caveat to our proposal is that it may be possible to design an "and/both" approach rather than an "either/or" approach, whereby the social bond requirements could increase liquidity to underserved markets or disadvantaged populations while yielding sufficient volume and the additional proceeds required to establish a Homeownership Trust Fund. It is challenging to comment on what is possible or feasible without more information and analysis on the GSEs single-family loan volume and characteristics. However, we urge FHFA to explore this.

Why a Homeownership Trust Fund (HOTF)?

We propose a Homeownership Trust Fund is established to capture and distribute the additional proceeds on the pay-ups from the social bonds (or other single-family bonds or disclosures that yield additional proceeds to investors). The purpose of the HOTF would be to create a dedicated funding source to produce and/or preserve affordable homeownership opportunities aligned to the GSEs' obligations under DTS and the EHFPs (or forthcoming EHFP rule). This would include, but not be limited to, providing resources to:

- Increase the supply of shared equity homes[2];
- Rehabilitate, repair, weatherize, or energy efficiency upgrades on naturally occurring affordable homes;
- Provide down payment or closing cost assistance to address the racial and ethnic homeownership gaps;
- Provide loss mitigation for lower-income homeowners, especially people of color;
- Acquire REOs or distressed assets by nonprofits to convert them to affordable owner-occupied homes.

We anticipate questions regarding our proposal for the creation of a new fund with the proceeds from any social bond.

Why not just permit the GSEs to retain the proceeds and have the discretion to deploy the funds as they see fit? It is our understanding that the multi-family social bonds issued by the GSEs are absorbed into their bottom line without sufficient accountability for how the proceeds are used. Formally establishing a Homeownership Trust Fund where both GSEs contribute proceeds will enable a high degree of accountability in the administration, usage, and reporting of the funds. Combining the pooling of proceeds with a meaningful level of outside stakeholder engagement in decisions regarding fund priorities, eligible uses, and awards will help keep the GSEs focused on the goals of the social bond and the HOTF rather than manipulating the use of funds for competitive advantages while they pursue their goals in DTS and EHFPs.

Why not just take the additional proceeds and put them into the National Housing Trust Fund (HTF)? The HTF is targeted at extremely low-income and very low-income renters. Only 10% of funds may be used on homeownership for households making up to 50% of the Area Median Income, and very few states opt to use any funds on homeownership. It is critical that the GSEs are held to account for meaningfully contributing funds to advance lower-income homeownership. Depending upon the amount of funds yielded by single-family bonds, social bonds, or a indexed pool with social disclosures, the NHTF could potentially be a model for structuring the HOTF (i.e. administered by HUD, state allocations with competitive awards, reporting requirements). Ultimately, the profits yielded from the social bonds will be generated from the GSEs single-family business based upon loans that meet some "social" criteria (e.g. lower-income and/or BIPOC borrowers). Therefore, proceeds from any pay-ups based on these loans should be used to improve opportunities for the hardest-to-serve or markets that are the most underserved and advance racial and economic equity through homeownership.

[2] We encourage unique approaches to increase the supply of shared equity homes that utilize investments as efficiently as possible. For instance, Grounded Solutions Network is pursuing the development of the Homes for Future Fund, whereby single-family homes would be acquired in relatively low-cost markets, rented for a period of time until homes have sufficiently appreciated to effectively create a "subsidy." The homes would then be sold close to the original price that the Fund purchased them at to enable lower income households to afford them, and the homes would be brought into a local community land trust's portfolio.

Why not just take the additional proceeds and put them into the Federal Home Loan Banks' Affordable Housing Programs (AHPs)? We are not proposing the funds go towards AHPs because the homeownership set-aside does not provide adequate down payment assistance to serve the vast majority of prospective homebuyers who are people of color. Moreover, down payment assistance helps one household achieve homeownership but does not contribute to the overall affordable housing stock. The competitive AHP has its own set of competing priorities, which do not sufficiently align with DTS or EHFPs and predominantly support rental projects. Additionally, the application process is extremely costly and difficult for nonprofits and relies upon willing bank partners. We advise the HOTF directly advances affordable homeownership and the funds are designed flexibility enough to pursue innovation and impact while directly aligning to underserved markets in DTS and to addressing race and ethnic homeownership disparities in the EHFPs.

Why Shared Equity Homeownership should be a priority for the Homeownership Trust Fund

We propose that a core component of the Homeownership Trust Fund should be the expansion of shared equity homeownership, defined as resale-restricted owner-occupied housing for lower-income households that remains affordable in perpetuity, providing households that may struggle to purchase a home a clear path to sustainable homeownership.

There are a number of reasons to make shared equity homeownership (SEH) the central element of a Homeownership Trust Fund, including increased access to homeownership, increased stability of homeownership, and the permanent expansion of the stock of affordable owner-occupied homes.

Access to Homeownership

Because SEH homes are sold at affordable prices significantly below their fair market value (resulting in LTVs between 50-80%), homebuyers are able to:

- Purchase the homes with very small down payments (e.g. 1%),
- Access conventional mortgages with lower credit scores,
- Avoid paying mortgage insurance, and
- Have affordable monthly mortgage payments that are often lower than what households were previously paying in rent.

These characteristics of the SEH model render it uniquely suited to enable lower income people of color to attain and sustain homeownership, as people of color disproportionately have lower incomes, less savings, and lower credit scores. The largest performance evaluation of share equity programs in the U.S.— which studied 58 programs and 4,108 shared equity homes— found that 95% of homes were affordable to households at or below 80% AMI (of which, 51%

were affordable to households at or below 50% AMI)[3]. The median home was priced at 31% below its fair market value. Over the course of 2013-2017, 43% of the lower income households owning a shared equity home were headed by a person of color.

In addition, while the resale value of shared equity homes is limited to ensure affordability, homeowners in shared equity programs *are* able to build wealth. For homeowners who sold their shared equity homes during 2013-2017, the median price they originally purchased their homes for was $118,000, and the median wealth built from appreciation and principal repayment was $13,467 (overall average duration of tenure was 6 years in the study)[4]. A strong rate of return on extremely small down payment amounts. When shared equity households sold their homes and moved, 58% purchased another home, supporting that the wealth accumulated from owning a shared equity home and the indirect savings from having a mortgage payment lower than many homeowners' previous monthly rental payments results in sufficient capital to enter private market ownership.

Sustainability of Homeownership

SEH programs don't just help lower-income people and people of color attain homeownership; they also sustain it. Another study that reviewed 96 SEH programs found that at the peak of the foreclosure crisis (end of 2010), shared equity homeowners were 10 times less likely to be in foreclosure proceedings and 6.6 times less likely to be seriously delinquent than homeowners across all income levels across all types of loans in the private market[5].

Many SEH programs also provide post-purchase support to homeowners (e.g. loss mitigation, financial counseling, repair support), and their program design often gives them the opportunity to approve refinancing or HELOCs to ensure the sustainability of tenure is not compromised.

Permanent Contribution to the Supply of Affordable Homes

One of the most compelling reasons to expand SEH is that it is self-sustaining model: a one-time subsidy to lower a home's initial purchase price results in a home that will forever remain affordable and provide successive lower-income families with the ability to access and sustain homeownership. In the aforementioned evaluation of 58 shared equity homes, they found that the model delivers on its promise: the shared equity homes remained affordable to households at the same income level resale over resale.

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[3] Ruoniu Wang et al. 2019. *Tracking Growth and Evaluating Performance of Shared Equity Homeownership Programs During Housing Market Fluctuations*. Lincoln Institute of Land Policy. Available at https://www.lincolninst.edu/sites/default/files/pubfiles/wang_wp19rw1_rev_0.pdf.

[4] Ibid.

[5] Emily Thaden, 2011. *Stable Home Ownership in a Turbulent Economy: Delinquencies and Foreclosures Remain Low in Community Land Trusts*. Lincoln Institute of Land Policy. Available at https://www.lincolninst.edu/sites/default/files/pubfiles/1936_1257_thaden_final.pdf.

This stock of shared equity housing remains a community asset even when neighborhoods become high-cost, enabling racial and economic integration and access to high-opportunity areas. BIPOC and lower-income renters often cannot access or sustain homeownership but for the opportunity to own a shared equity home, enabling an array of families to build wealth and benefit from residential stability. And every shared equity home becomes a permanent contribution to the overall affordable housing supply, enabling family after family who lives there to experience the benefits of homeownership.

Alignment with ESG Principles

Much of FHFA's RFI deals with the definition of a social bond and the concept of Environmental, Social, and Governance (ESG) principles in investment. We feel that the reasons listed above clearly align SEH with the definitions of ESG principles referenced by FHFA and other respondents to this RFI.

The International Capital Markets Association (ICMA), for example, describes "Use of Proceeds" as the "cornerstone" of an effective social bond[6]. The use of shared equity homeownership and its inherent pursuit of equity meets two of the ICMA's Social Project suggestions: affordable housing and socioeconomic advancement and empowerment. SEH models also help to achieve several goals described in the UN Sustainable Development Goals, specifically goals 10 and 11: reducing inequality and supporting inclusive and economically sustainable cities. SEH programs expand access to homeownership and wealth building, working to reduce inequality within cities. They also encourage a more inclusive form of urban development that protects communities from displacement and provide more opportunities for stable housing.

Additional General Remarks:

We want to acknowledge that our public comment does not sufficiently address loan eligibility for a potential single-family social bond or "social" index pools with disclosures. A lot of additional research and loan analysis is necessary to determine how to balance sufficient and reliable volume with social impact and potential ESG requirements. Additionally, FHFA is raising very important concerns about disclosures and borrower re-identification.

Fundamentally, we want to avoid traders and investors from engaging in arbitrage on these mortgages that damages markets. Therefore, standardization and a certain level of opacity is vital to avoid injuring markets or hurting borrowers.

We strongly encourage FHFA to conduct a broad participatory process across stakeholder groups and interested parties to develop a single-family social bond or socially indexed pools that may yield meaningful, significant benefit to increase affordable homeownership for

[6] ICMA. 2021. *The Social Bond Principles.* Available at https://www.icmagroup.org/sustainable-finance/the-principles-guidelines-and-handbooks/social-bond-principles-sbp/.

underserved markets and advance racial equity. This must include a multitude of representatives across industry, investors, affordable housing and fair housing advocates, and consumer rights groups.

Please do not hesitate to reach out if we can provide additional information. We applaud FHFA for undertaking this effort to realize the GSEs’ obligations to provide a public benefit through their single-family business.

Sincerely,

Emily Thaden
Vice President of National Strategy
Grounded Solutions Network