October 27, 2017

Director Mel Watt
Federal Housing Finance Agency
400 7th St SW
Washington, DC 20024

Re: CRL Comment on FHFA Strategic Plan 2018-2022

Dear Director Watt:

The Center for Responsible Lending[1] thanks you for the opportunity to comment on FHFA's strategic plan for the fiscal years 2018-2022. While we agree with FHFA's general direction, CRL would like to provide feedback regarding pricing, the duty to serve rule, the housing goals, and how the credit risk transfer program impacts borrowers. Specifically, we recommend:

- Holding the Enterprises accountable for their duty to serve obligations;
- Setting a higher benchmark standard for the affordable housing goals and using the full extent of FHFA's statutory authority to assertively enforce the goals;
- Eliminating the LLPAs and setting g-fees in such a way as to pool risk and encourage wide access to responsible homeownership;
- Permit the use of responsible alternative credit scoring by the Enterprises; and
- Monitoring the impact credit risk transfer structures might have on borrowers.

Performance Goal 2.2: Promote Stability in the Nation's Housing Market

Among the means and strategies for Performance Goal 2.2, the FY 18 Performance Plan states that FHFA will continue to assess opportunities to address credit access and develop recommendations for improvements where appropriate. In addition, FHFA will analyze and define the characteristics of future mortgage borrowers, such as millennials, student loan debt holders, non-W-2 wage earners, people of color, and seniors. We are glad to see FHFA's focus on credit access, and as explained below, we hope FHFA will consider how its ongoing work on pricing policy, duty to serve, the housing goals, and credit risk transfer all interact to influence credit access. Additionally, FHFA should permit the use of responsible alternative credit scoring by the Enterprises.

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[1] The Center for Responsible Lending (CRL) is a nonprofit, non-partisan research and policy organization dedicated to protecting homeownership and family wealth by working to eliminate abusive financial practices. CRL is an affiliate of Self-Help, one of the nation's largest nonprofit community development financial institutions. Since 1980, Self-Help has provided over $7 billion in financing to 131,000 families, individuals and businesses under-served by traditional financial institutions. It helps drive economic development and strengthen communities by financing hundreds of homebuyers each year, as well as nonprofits, child care centers, community health facilities, public charter schools and residential and commercial real estate projects. Through its credit union network, Self-Help's two credit unions serve over 130,000 people in North Carolina, California, Chicago, Florida and Wisconsin and offers a full range of financial products and services.

Performance Goal 2.3: Expand Access to Housing Finance for Qualified Financial Institutions of All Sizes in All Geographic Locations and for Qualified Borrowers

We are pleased to see FHFA's emphasis on expanding access to housing finance for qualified financial institutions of all sizes, in all geographic locations, and for qualified borrowers. We are also pleased that FHFA states that it is committed to reducing barriers that restrict creditworthy borrowers' access to responsible lending and that FHFA expects the Enterprises to assess whether there are additional opportunities, including pilots and initiatives, to reach underserved creditworthy borrowers.

Duty to serve and the housing goals are mentioned by name in a catch-all strategy as "oversee the regulated entities' additional statutory requirements." No additional detail is provided aside from stating in the FY 18 performance plan that FHFA will finalize the housing goals rule and review the Enterprises' duty to serve plans. We would like FHFA to emphasize the importance of these two statutory requirements and we urge FHFA to make them a more prominent focus under its strategies to expand access to credit.

Duty to Serve

As we have discussed in previous comments,[2] the goal of the duty to serve rule and process is to encourage and hold the Enterprises' accountable for serving three specific underserved markets – manufactured housing, rural, and shared equity markets. Although the Enterprises play an important role in designing pilot programs, developing new product offerings, and engaging in outreach to influence lender behavior, loan purchases are the single most important aspect of the Enterprises' activities. The Enterprises' loan purchases are what provide liquidity in the mortgage market and ensure that lenders can replenish their supply of capital funds and make additional mortgage loans to borrowers. The duty to serve process must be robust and FHFA should hold the Enterprises' accountable for proposing and implementing strong duty to serve plans.

Housing Goals

Furthermore, the Enterprises' affordable housing goals – particularly the purchase of single-family loans from low and very low-income borrowers – are essential to encourage affordable homeownership opportunities. The Enterprises' affordable housing goals have historically had a tremendous impact on helping creditworthy borrowers purchase homes. From 2003 through 2012, the National Community Reinvestment Coalition reported that more than 25 million hard-working families nationwide were able to become homeowners due to the goals.[3] In fact, we know that loans to low and moderate-income consumers, done right, perform well and serve lenders, borrowers and communities. For example, a report on Self-Help Credit Union's

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[2] CRL Comment to FHFA, Duty to Serve Rule (March 17, 2016), *available at* http://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl_comments_duty_to_serve_mar2016.pdf; CRL Comment to FHFA, Enterprises' Duty to Serve Plans (July 10, 2017), available at http://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-fhfa-dts-plans-comment-jul2017.pdf

[3] National Community Reinvestment Coalition, Nationwide Benefits from the Affordable Housing Goals, *available at* http://www.ncrc.org/images/PDFs/ahg/nationwide%20ahg.pdf.

Community Advantage Program from the University of North Carolina's Center for Community Capital, showed that borrowers amassed a net worth of $38,000, compared with renters' $266, even as housing values plunged during the crisis.[4] The Community Advantage Program securitized mortgages for more than 50,000 families in 48 states.

In our recent comments on the 2018-2020 housing goals,[5] we offered specific recommendations to FHFA regarding the goals, including setting a higher benchmark standard and using the full extent of its statutory authority to more assertively enforce the goals. In recent years, the Enterprises have done a poor job of meeting their home purchase goals. This is unfortunate, as the housing goals are essential to expanding access to credit for underserved groups, ensuring liquidity in the financial markets, and furthering fair lending goals.

Pricing

In addition, we have previously urged FHFA and the Enterprises to revisit their pricing policies and consider how the current structure is a barrier to the Enterprises' ability to purchase loans from low-income borrowers and in underserved markets. This has an impact on both the duty to serve process and the single-family loans purchases under the housing goals. We have called on FHFA to eliminate the LLPAs and set g-fees in such a way as to pool risk and encourage wide access to responsible homeownership. FHFA should also consider the ways in which the PMIERs capital requirements have contributed to greater risk based pricing and differential pricing for private mortgage insurance.

Underwriting structures determine if borrowers are credit worthy, but pricing structures have a significant impact on whether a credit worthy borrower can afford a mortgage. Differential pricing creates an additional barrier to mortgage credit by increasing the price, sometimes significantly, for some borrowers relative to others. There is evidence of price acting as a barrier to credit access, especially in today's mortgage market. For example, although Fannie Mae's guidelines allow the Enterprise to purchase loans with credit scores down to 620 and loan-to-value (LTV) ratios of up to 97%, very few loans purchased by the Enterprise have these characteristics. Just 4.1% of Fannie Mae's 2016 single-family loan purchases had credit scores below 660, and just 1.1% had a combination of a credit score under 660 and an LTV over 80%. [6]

One reason for such low numbers is that excessive risk-based pricing by both the Enterprises and private mortgage insurers add significantly to the cost of loans for borrowers with lower scores and less wealth for a down payment. The combination of loan-level price adjustments (LLPAs) and mortgage insurance (MI) premiums, for example, adds over 300 basis points to the cost of a mortgage for a borrower with a credit score of 620 and an LTV of 97%.[7] Reducing differential

[4] Allison Freeman, UNC Center for Community Capital, The Continuing Importance of Homeownership: Evidence from the Community Advantage Program (2014), at 9, *available at* http://www.frbsf.org/community-development/files/ci_vol26no2-Continuing-Importance-of-Homeownership.pdf.
[5] CRL Comment to FHFA, 2018-2022 Enterprise Housing Goals (Sept. 5, 2017).
[6] See p. 6 of 2017 First Quarter Credit Supplement, Fannie Mae, May 5, 2017, *available at* http://www.fanniemae.com/resources/file/ir/pdf/quarterly-annual-results/2017/q12017_credit_summary.pdf.
[7] 350/4+225=312.5 basis points. Fannie's Mae's LLPA for this combination of credit score and LTV is a one-time fee of 350 basis points (see page 2: https://www.fanniemae.com/content/pricing/llpa-matrix.pdf), we assumed a

pricing and instead spreading risk across the larger pool of loans purchased would likely further the Enterprises' loan purchases in underserved markets.

Credit Scoring

FHFA should also permit the Enterprises to use alternative credit scoring. Current credit-scoring models do not adequately serve today's credit market. For instance, they disqualify many first-time homebuyers with thinner credit files. Expanding the use of alternative credit scoring models is a critical element to reverse declines in homeownership, particularly for low- and moderate-income communities and communities of color.

FHFA Should Continue Broad Stakeholder Outreach

FHFA states that one of the strategies to monitor access to mortgage credit is using data reported by the Enterprises, data from third-party sources, and *discussions with industry sources*. We also urge FHFA to continue engaging in discussions with and consider information provided by consumer, civil rights, and housing counseling groups. These groups have a keen sense of what is occurring on the ground, as well as larger trends in the market.

Performance Goal 3.2: Reduce Taxpayer Risk from Enterprise Operations

Among the means and strategies in support of this goal are promoting the credit risk transfer program that reduces taxpayer risk by attracting private capital. This includes setting targets for multiple types of single-family mortgage credit risk-sharing transactions and holding Enterprise management accountable for meeting those targets.

We urge FHFA to consider how the credit risk transfer program and structure options affect mortgage borrowers. We are particularly concerned that front-end structures, including "Deeper MI," could structurally frustrate the Enterprises' statutory duties to create a well-functioning housing market and provide broad market access.

FHFA should monitor the impact credit risk transfer structures might have on borrowers. In particular, FHFA should consider potential effects on: 1) loan pricing, and thus access to credit, 2) loan quality and servicing, and 3) access for small lenders. In bringing in private capital, FHFA should be careful to ensure that it is responsible and does not exchange access to credit or borrower protections for the capital the private market offers. We are concerned that the credit risk transfer programs have the potential to:

- **Increase prices for certain borrowers,** which would effectively limit access to credit for some creditworthy borrowers. Recent pricing changes by mortgage insurance (MI) companies illustrate this risk. These risks are most acute for, but not entirely limited to, front-end credit risk transfer structures.

LLPA multiple of 4 to convert this upfront fee to an ongoing cost comparable to the MI premium. Borrower paid MI from Genworth for this combination of credit score and LTV is a continuing fee of 225 basis points. See https://mortgageinsurance.genworth.com/pdfs/Rates/11370775.Monthly_Natl.FIXED.0616.pdf.

- **Reduce incentives for strong quality control.** As the Enterprises cede credit risk they must continue to ensure quality origination and servicing. Borrowers should receive quality loans as well as loan modification and foreclosure prevention opportunities in the same way they would have had the Enterprises retained credit risk.

- **Favor larger lenders over smaller lenders** which would also effectively limit access to credit for borrowers by limiting the set of lenders who provide loans. Some front-end structures, by virtue of their complexity, are effectively only open to larger lenders. If these structures create market pricing advantages, small lenders will be disadvantaged in the mortgage market.

Finally, we are concerned about calls for the Enterprises to lay off increased credit risk to Private Mortgage Insurers (PMI) through proposed Deeper MI structures. Expanding the amount of credit risk shouldered by these companies amplifies existing risks for the Enterprises. More importantly, the front-end nature of this structure and the pricing practices of these actors raise serious questions about the impact Deeper MI would have on access to credit and a well-functioning housing market. Our June 2016 comment to FHFA in response to the request for input includes further details.[8]

Conclusion

As part of the strategic planning process, we urge FHFA to more holistically consider how its pricing policies, duty to serve, housing goals, and credit risk transfer program interact to expand (or diminish) access to credit for qualified borrowers. Thank you for the opportunity to comment. We look forward to continued discussion with FHFA as the 2018-2022 strategic plan is implemented.

Sincerely,

Center for Responsible Lending

[8] CRL Comment to FHFA, Single-Family Credit Risk Transfer Request for Input (June 2016), *available at* http://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl_fhfa_risk_sharing_comment_oct2016.pdf.