March 19, 2014

The Honorable Melvin L. Watt
Director
Federal Housing Finance Agency
400 7th Street, SW
Washington, D.C. 20024

RE: Docket No. 2013–N–18, Fannie Mae and Freddie Mac Loan Purchase Limits: Request for Public Input on Implementation Issues

Dear Director Watt:

The Mortgage Bankers Association (MBA)[1] appreciates the opportunity to comment on the proposal (Proposal) issued by the Federal Housing Finance Agency (FHFA) to reduce the maximum size of loans (hereinafter "loan limits') that the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation (together, the Government Sponsored Enterprises or GSEs) may purchase. Specifically, FHFA has proposed reducing the maximum conforming and high-cost loan purchase limits. FHFA's proposal suggests that the conforming loan limit would be reduced from $417,000 to $400,000, and from $625,500 to $600,000 for high-cost areas. The Proposal suggests that these changes could take place as soon as October 1, 2014.

MBA commends FHFA for seeking input on this important issue, which we believe in large measure will determine how many families will access what is likely to be the most affordable mortgage financing available. While MBA fully supports FHFA's goal of reducing the Government's footprint in the housing finance industry, for the reasons explained in this comment, we oppose the proposed reductions in the GSEs' loan limits at this time. We believe any changes to the GSEs' loan limits should only be considered as part of comprehensive housing finance reform. While the Proposal admits that the proposed action alone will do little to reduce taxpayer exposure to risk, we are concerned that these reductions instead will have a deleterious effect on government housing finance.

Housing markets remain fragile and moving forward with this option risks further constricting access to credit and reversing progress made in the housing recovery without achieving a meaningful return of private capital. Many potential homeowners remain on the sidelines unable to purchase a home or refinance their mortgage due to rising rates, tight housing inventory, and restrictive credit standards. In key housing markets, the proposed loan limit changes could exacerbate the problem.

MBA believes there are better options currently available to FHFA to increase private capital participation without harmful effects. These options include expanding the GSEs' successful use of risk sharing, which began during 2013, as well as offering lenders the option to arrange for deeper private mortgage insurance coverage in exchange for a reduced guarantee fee from the GSEs.

[1] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 280,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,200 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mba.org.

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MBA believes these alternatives will not only increase private capital's role in housing finance, but also produce tangible savings that can be passed on directly to borrowers.

However, if FHFA chooses to pursue a reduction in the loan limits notwithstanding our concerns, we respectfully urge that it take several actions before implementing any changes. Specifically, FHFA should further study the matter in light of the recently finalized rulemakings required by the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank), coupled with the market's change from a refinance to a purchase market. With these concerns in mind, MBA respectfully offers this comment.

Discussion:

1. **FHFA should not reduce the GSEs' conforming or high-cost maximum loan limits.**

As indicated, FHFA has proposed reducing the maximum conforming and high-cost loan purchase limits. FHFA's proposal suggests that appropriate reductions would be from $417,000 to $400,000 and from $625,500 to $600,000 respectively.

MBA data shows, however, that home prices continue to rebound from the housing crisis. Growth in mortgage applications for purchasing a home of late has been driven by applications for loans that are greater than $417,000, while the data continues to show a slowdown in applications for loans under $417,000 relative to a year ago.

<u>Purchase Application Activity in January 2014</u>

Loan Balance	Share of Purchase	Change from January 2013
<=150K	36.20%	-14.30%
>150K and<=300	36.90%	-9.60%
>300K and<=417k	12.90%	-18.10%
>417K and<=625k	7.60%	18.00%
>625K and <=729k	2.10%	20.60%
>729K	4.40%	24.00%

While MBA supports FHFA's goal of reducing the GSEs' role in the mortgage market, MBA strongly believes that reducing the GSEs' maximum loan limit at this time would unduly impact areas with higher housing costs and be disruptive to the ongoing housing recovery. The following are MBA's specific concerns relating to the Proposal:

a. **Any changes in loan limits should only be contemplated as a part of a broader coordinated package of housing market reforms.**
In the past year, legislation has been introduced in both chambers of Congress articulating visions for end-state reform of the GSEs. The most recent GSE reform plan proposed by Senators Tim Johnson and Mike Crapo would maintain the GSEs' current conforming and

high-cost loan limits without change and would not allow for these limits to be lowered.[2] In the meantime, recent regulatory changes have made it more expensive for banks to hold loans in their portfolio, while the still-outstanding risk retention and asset-backed securities disclosure rules will impact lenders' ability to securitize their loans.

With all this uncertainty, we urge FHFA not to make piecemeal changes affecting key market components. Rather, the ultimate determination of what level of loans should qualify for a government or GSE guarantee—whether catastrophic or otherwise—should be considered and addressed as part of comprehensive secondary mortgage market reform.

Furthermore, one of FHFA's stated reasons for proposing to reduce the GSEs' loan limits has been to limit taxpayer exposure to losses. In its Proposal, FHFA admits, however, that some of borrowers looking for loans that would no longer be eligible for purchase by the GSEs might obtain an Federal Housing Administration (FHA) -insured mortgage. Currently, FHA and the GSEs have the same high-cost loan limit, $625,500, and HUD has not commented on whether it would reduce FHA's loan limits. If FHFA alone reduced the GSEs' loan limits, risk to the government would not be reduced; it would merely shift to FHA.

Before FHFA acts on this proposal, comprehensive reform efforts should be allowed to move forward.

b. Reducing loan limits will harm borrower's access to credit, without delivering commensurate savings to the borrowers who are able to obtain a mortgage.

The private label mortgage-backed security (MBS) market has yet to revive following the financial crisis, and there is significant concern about its present capacity to invest in the housing market. Reducing the loan limits will result in affected loans losing the ability to meet the Qualified Mortgage (QM) definition under the "temporary patch" established by the Consumer Financial Protection Bureau. This would apply a firm 43% maximum debt-to-income ratio for these loans in order to meet the QM definition, resulting in many formerly QM loans being subject to higher compliance costs – costs that would ultimately be borne by borrowers through higher interest rates or reduced access to credit.

Prior to the housing crisis, the private label MBS market provided an vibrant alternative that allowed borrowers to access loans which may not have met the GSEs' purchase eligibility requirements. This market has been frozen since the financial crisis – in part due to persistent regulatory and structural uncertainty.[3] Over 90 percent of mortgage loans originated today are either bought by the GSEs or guaranteed by the government, with the remainder being held predominantly on the balance sheets of depository institutions. Spurring a vibrant private sector MBS market will require wholesale regulatory and structural developments; simply reducing the conforming loan limits will not be sufficient and may in fact be counterproductive by concentrating lending within affected loan amounts to the few lenders who have the portfolio or balance sheet capacity.
In its Proposal, FHFA says that its proposed loan limit reductions will affect a very small percentage of the market. While the number of loans affected by the Proposal may be relatively small, all lenders will be forced to implement these changes in their systems, resulting in significant testing, training, and other compliance costs.

[2] The bill, like the Corker-Warner bill introduced in 2013, would use mandatory risk-sharing to reduce the government's footprint.
[3] As noted above, the risk retention rule and amended Reg AB securities disclosure rules remain unfinished, preventing market participants from committing to private-label investments in any noticeable scale.

Reducing the GSEs' loan limits would also have the effect of disallowing those loans that were previously eligible for GSE purchase from qualifying for what has come to be known as the "temporary patch" under the ATR/QM rule.[4] Under the ATR/QM rule, loans generally must have a debt-to-income (DTI) ratio of no more than 43 percent; however, under the temporary patch loans do not have to meet a specific DTI ratio so long as they are eligible for Enterprise purchase (while they remain under conservatorship) or guarantee by a federal agency such as FHA, Veterans Administration, or Department of Agriculture. Under the general QM standards, loans which fail the 43 percent DTI test cannot qualify for QM status—regardless of compensating factors such as the borrower's cash reserves, residual income or payment history. Consequently, because of QM's strict DTI requirement, MBA believes that loans that fall outside the patch will be harder to obtain, and some loans that may have been made under the "temporary" patch will no longer be available to borrowers.

MBA believes that under the circumstances, changes to the loan limits will reduce borrowers' access to credit and that the associated costs to the market generally will outweigh any benefits associated with reducing the GSEs' footprint.

c. There are other more effective options to reduce taxpayer exposure.

As indicated, FHFA's stated purposes in considering a reduction of the GSEs' loan limits is to "invite private capital to re-enter the [housing finance] market." But there are far more effective means than reducing the loan limits to achieve this goal and reduce taxpayer exposure.

Both GSEs have successfully met FHFA's mandate to engage in at least $30 billion worth of risk sharing transactions. The GSEs accomplished this through a multitude of transactions, entering into reinsurance contracts and issuing general obligation bonds linked to borrower performance. The general obligation bonds in particular were well over-subscribed and have seen yields fall since the deals were consummated – indicating high market demand for the investment. Moreover, private firms have been developing risk transfer securities and other products that would enable the GSEs to offload even greater risk to the private market. Finally, still other market participants are exploring arrangements to provide even deeper credit enhancements at the individual loan level.

All of these options are currently available to the GSEs, and offer significant advantages over a reduction in the loan limits. In particular, these options allow for private capital to compete directly for borrower credit risk regardless of loan size, creating potential savings that can be passed along to the borrowers.

FHFA should more aggressively pursue these options instead of loan limit reductions. In doing so, FHFA would attract the private capital that is available now, while giving the private label MBS market time to work through the regulatory and structural issues noted above – in essence, paving the way to a more dynamic and competitive private label market in the future.

[4] The patch applies until Fannie Mae and/or Freddie Mac leave conservatorship or the agencies issue their own rules (as HUD has done for FHA effective January 10, 2014), but in no later than 7 years from January 10, 2014.

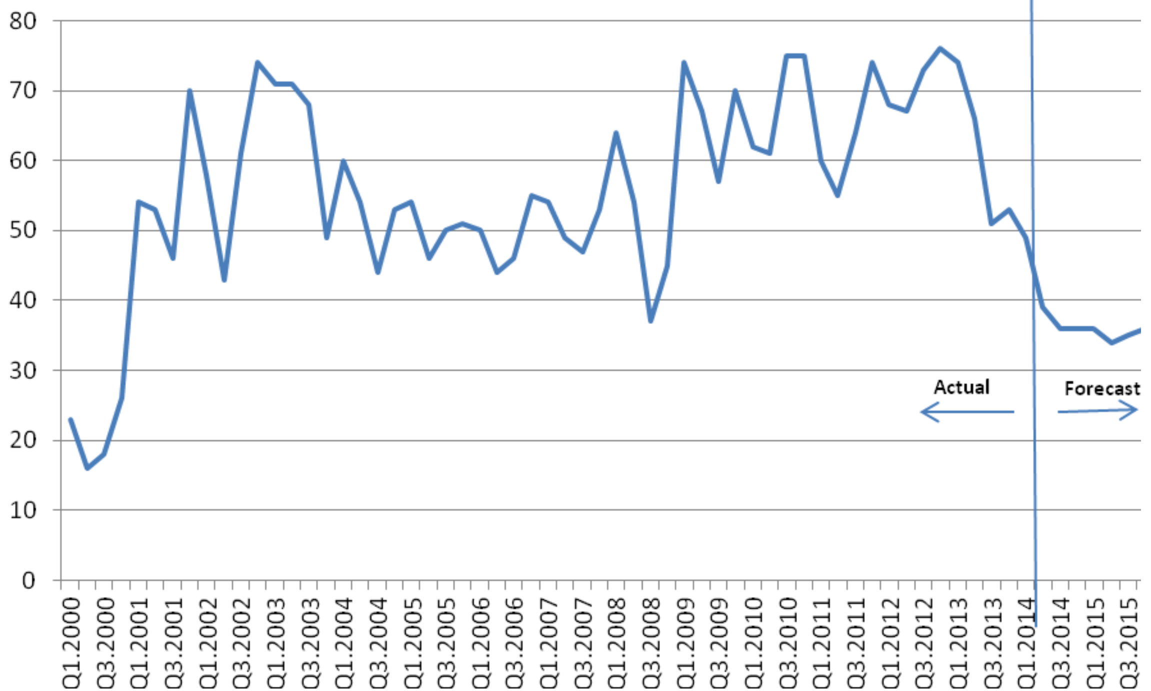
2. If FHFA seeks to reduce the GSEs' loan limits nonetheless, MBA urges that the following actions be taken first:

As previously stated, MBA strongly believes that FHFA should not reduce the GSEs' loan limits. However, if FHFA plans to move forward with loan limit reductions notwithstanding our concerns, MBA urges the following.

a. Given changing market conditions, the matter should be carefully studied during the next year to measure the impact of the proposed reductions across the nation.

If FHFA intends to move forward, MBA strongly suggests that FHFA and the GSEs use the next year to comprehensively study the impact of these reductions. As many of the new regulations required by Dodd-Frank—most notably the ATR/QM rule—have only just come online, it remains to be seen how these rules will affect the mortgage markets and consumers access to credit.

Moreover, FHFA's Proposal is based on 2012 numbers which do not reflect the shift from a refinance to the purchase driven mortgage market that prevails today. As seen in the following chart, refinance activity reached a high of 76 percent of the market in the fourth quarter 2012, and has since fallen under 40 percent. Accordingly, any review should examine the implications of a change in the loan limits in a purchase environment.



When conducting this study, MBA recommends that FHFA be particularly mindful of continued home price appreciation, which MBA has forecast at 4.4 percent in 2014 and 3.5 percent in 2015.

MBA believes that until the true impact of the Dodd-Frank regulations and the market's adjustment from refinance to purchase activity is carefully considered, it would be inappropriate to consider the proposed reduction in loan limits.

b. **If necessary, loan limits changes should be effective on January 1st every year.**

If the GSEs are to make changes to their loan limits, these changes should only be effective for applications dated on or after January 1st of the applicable year. The certainty of making the date for loan limit changes the same year after year is essential to give lenders and vendors critical lead time to prepare the required operational changes. If changes are made more frequently, or at irregular times, lenders and vendors may have difficulty keeping up, resulting in errors, potentially leading to some loans becoming unsalable.

c. While it is important to provide lenders with advance notice of loan limits changes, locking into a multi-year schedule for any changes would reduce the ability of the GSEs to use loan limits to respond to changing market conditions.

MBA deeply appreciates that FHFA has pledged to provide at least six months notice before implementing any loan limit reductions contemplated in its proposal. In recent years, FHFA has provided lenders with considerably less - sometimes one month's notice of the following year's maximum loan limits. When loan limits remain static, or increase, as they have in some cases over the past several years, lenders can have confidence that loans in their pipelines will not exceed the next year's limits. However, if loan limits are reduced, lenders report that they need at least six months to clear their pipelines to ensure that they do not originate loans that exceed the new limits.

In its request for comment, FHFA inquired whether it would be preferable for the GSEs to announce a multi-year schedule of loan limit reductions. MBA strongly believes that locking the GSEs' into a multi-year schedule of loan limit reductions—at a time when home prices are widely expected to continue appreciating—would be inappropriate. Preemptively committing to such loan limit reductions would greatly reduce the GSEs' ability to respond to changing market conditions and reform efforts. We believe ongoing monitoring by FHFA and the GSEs would ensure that the loan limits are responsive to continued home price appreciation and regulatory changes.

d. In those areas with loan limits between the conforming and high-cost limits, changes to those limits should be tied to changes in median home prices in those areas.

MBA believes that FHFA should continue existing policy and tie future changes in loan limits for areas between the conforming and high-cost limits to shifts in median home prices in those areas. Tying a change in the loan limit to a shift in the median home prices in a particular area will ensure local housing market conditions are reflected in the loan limits.

e. Loan limits should always be rounded up to the nearest multiple of $1,000.

Lenders have indicated that future changes to the GSEs' loan limits should be rounded up to the nearest multiple of $1,000. Loan limits rounded to the nearest multiple of $1,000 are easily remembered, reducing the chance of data entry errors which could make loans unsalable since lenders are unable to cure loans that exceed the GSEs' loan limits.

Conclusion

For the reasons explained here, while MBA fully supports FHFA's goal of reducing the footprint of the GSEs in the mortgage market, MBA does not believe that the conforming loan limits should be reduced at this time. FHFA's goals would be better served by pursuing other policy measures that would reduce taxpayer exposure without harming the housing market. If FHFA still wishes to pursue loan limit reductions, we urge it to study the matter further, taking into consideration recent Dodd-Frank rulemakings, changes to the market, and current legislative proposals.

Should you have questions or wish to discuss any aspect of these comments further, please contact Tamara King, Associate Vice President for Loan Production at (202) 557-2758 or tking@mba.org: Joe Gormley, Assistant Regulatory Counsel at (202) 557-2870 or jgormley@mba.org: or Dan McPheeters, Policy Advisor at (202) 557-2780 or dmcpheeters@mba.org.

Sincerely,

David H. Stevens
President and Chief Executive Officer