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November 23, 2021

Clinton Jones
General Counsel
Federal Housing Finance Agency
400 Seventh Street SW
Washington, DC 20219

RE: Enterprise Regulatory Capital Framework Rule—Prescribed Leverage Buffer Amount and Credit Risk Transfer (Comments/RIN 2590–AB17)

Dear Mr. Jones:

The Credit Union National Association (CUNA) represents America’s credit unions and their more than 120 million members. On behalf of our members, we are writing in response to the Federal Housing Finance Agency’s (FHFA’s) notice of proposed rulemaking and request for comments on proposed amendments to the Enterprise Regulatory Capital Framework (ERCF).¹ CUNA supports the amendments as more accurately assessing capital requirements and better facilitating the ability to meet the mission of the Federal National Mortgage Association (FNMA or Fannie Mae) and the Federal Home Loan Mortgage Corporation (FHLMC or Freddie Mac) (collectively, the Enterprises) through all economic cycles.

Background

On September 6, 2008, in response to solvency concerns that arose when the financial crisis severely crippled America’s housing market, FHFA placed the Enterprises into conservatorship. The inadequacy of the Enterprises’ previous capital reserves is commonly cited as the primary reason why they were unable to withstand mortgage losses during the financial crisis. For example, the Financial Crisis Inquiry Commission (FCIC) described the Enterprises as “the kings of leverage . . . [whose] combined leverage ratio, including loans they owned and guaranteed, stood at 75 to 1,” meaning that for every \$75 in assets held by the Enterprises, they held only \$1 in capital to cover losses.

On June 12, 2018, FHFA issued a proposed rule for Enterprise capital requirements (2018 Proposal), which would “implement a new framework for risk-based capital requirements and a

¹ Enterprise Regulatory Capital Framework Rule-Prescribed Leverage Buffer Amount and Credit Risk Transfer, 86 Federal Register 47398 (Sept. 27, 2021) (ERCF Amendments).

revised minimum leverage capital requirement for the Enterprises.”² On June 30, 2020, FHFA published a re-proposed regulatory capital framework (ERCF Re-Proposal), which built upon the foundation of the 2018 Proposal.³ In the ERCF Re-Proposal, FHFA states that the changes were designed to achieve three primary objectives: to simplify and refine the 2018 Proposal’s mortgage risk-sensitive framework; increase the quantity and quality of regulatory capital; and to address the pro-cyclicality of the 2018 Proposal.⁴

The FHFA adopted the ERCF Final Rule on December 17, 2020.⁵ The ERCF Final Rule established risk-based capital requirements, adjusted by a prescribed capital conservation buffer amount (PCCBA).⁶ As a backstop to these risk-based capital requirements and to avoid limits on capital distributions and discretionary bonus payments, the Enterprises would also be required to retain tier 1 capital in a leverage ratio requirement plus additional capital equal to the prescribed leverage buffer amount (PLBA) of 1.5 percent of the Enterprise’s adjusted total assets.⁷

In the ERCF Final Rule, the FHFA recognized that many commenters criticized the PLBA as being too large.⁸ Others suggested that as it existed in the ERCF, the PLBA-adjusted leverage ratio requirement likely would often exceed the PCCBA-adjusted risk-based capital requirements, and therefore be binding as the capital requirements for the Enterprises.⁹ Commenters stated that a consistently-binding PLBA-adjusted leverage ratio requirement could reduce the risk sensitivity of the regulatory capital framework and incentivize risk taking by the Enterprises.¹⁰ Ultimately, the FHFA adopted the PLBA as proposed, though it also recognized that the analysis suggesting that the PLBA-adjusted leverage ratio would generally exceed the PPCBA-adjusted risk-based capital requirements as described by some commenters would evidence flaws in the FHFA’s method for calibrating both of these back-stops.¹¹

Also in the ERCF Final Rule, the FHFA made changes with regard to risk retained by an Enterprise on its credit risk transfer (CRT). In a CRT program, an Enterprise pays private market participants to assume credit risk in a severe stress scenario on mortgages the Enterprise guarantees. CRT programs transfer credit risk away from American taxpayers and to private investors. These programs have been included in the Strategic Plans for Conservatorships of Fannie Mae and Freddie Mac since 2012, and the programs have been viewed as a success.

The ERCF Final Rule nonetheless proposed a prudential floor of 10 percent on the risk weight assigned to any retained CRT disclosure and added an overall effectiveness adjustment to

² Enterprise Capital Requirements, 83 Fed. Reg. 33312 (Jul. 17, 2018) (2018 Proposal).

³ Enterprise Regulatory Capital Framework, 85 FR 39274 (Jun. 30, 2020) (ERCF Re-Proposal).

⁴ ERCF Re-Proposal, 85 FR at 39275.

⁵ Enterprise Regulatory Capital Framework, 85 FR 82150 (Dec. 17, 2020) (ERCF Final Rule).

⁶ ERCF Final Rule, 85 FR at 82154.

⁷ *Id.*

⁸ *Id.* at 82167.

⁹ *Id.*

¹⁰ *Id.*

¹¹ *Id.* at 82163.

deductions in capital related to CRT.¹² Commentors pointed out that neither of these treatments of CRT were included in the 2018 Proposal.¹³ Commentors also noticed the lack of analytical support for this treatment, recommended reducing or eliminating the floor, and identified that the overall effectiveness adjustment reduces the capital relief afforded by CRT to the point of disincentivizing the transactions. The FHFA recognized that the effects of the ERCF Final Rule’s treatment of CRT are difficult to predict and that given the complexity of the issues, the FHFA was contemplating future rulemakings to address CRT further.¹⁴ Freddie Mac has continued to execute CTR transactions following the implementation of the ERCF Final Rule.¹⁵ Fannie Mae, however, has not as it considers the costs and benefits in light of the capital relief provided, market conditions, and other business factors.¹⁶ Both Enterprises are considering potential changes to their CRT programs to optimize risk transfer and capital relief under the ERCF.¹⁷

General Comments

CUNA has consistently supported FHFA’s efforts to ensure that the Enterprises have strong capital requirements that will allow them to withstand an economic downturn and provide liquidity to the mortgage market without taxpayer intervention.¹⁸ We applaud this continued effort to ensure capital requirements are part of a strong supervisory regime that ensures the safety and soundness of the Enterprises during various economic cycles.

Such supervision is a key component of CUNA’s Housing Reform Principles, which include:

- Equal secondary mortgage market access to lenders of all sizes on an equitable basis;
- A neutral third party in the secondary market, independent of any firm that has any other role or business relationship in the mortgage origination and securitization process, with its sole role as a conduit to the secondary market;
- An emphasis on affordability, in recognition of the fact that smaller lenders, such as credit unions, often meet mortgage needs that banks are unwilling or unable to address in rural and working-class communities that require greater flexibility in underwriting requirements;
- A reasonable and orderly transition to a new housing finance system;
- Strong oversight and supervision to ensure the safety and soundness of secondary market entities;

¹² *Id.* at 82178.

¹³ *Id.*

¹⁴ *Id.* at 82183.

¹⁵ ERCF Amendments at 53235.

¹⁶ *Id.*

¹⁷ *Id.*

¹⁸ See CUNA Comments to Enterprise Capital Requirements Proposed Rule (Nov. 15, 2020) available at <https://www.cuna.org/content/cuna/cuna-org/advocacy/letters---testimonies/2018/cuna-letter-on-enterprise-capital-requirements-proposed-rule.html>. See also CUNA Comments to Enterprise Regulatory Capital Framework (Aug. 31, 2020) available at <https://www.cuna.org/content/cuna/cuna-org/advocacy/letters---testimonies/2020/cuna-comments-to-fhfa-on-the-gse-recapitalization-framework.html>.

- Durability, by including an explicit federally insured or guaranteed component to ensure that, even in troubled economic times, the secondary mortgage market continues to exist; and
- Preserving what works, such as cost-effective and member-oriented credit union mortgage servicing options, emphasizing consumer education and home-purchase counseling, and applying reasonable conforming loan limits that adequately consider local real estate expenses in higher cost areas.¹⁹

We view these proposed amendments to the ERCF through the lens of these principles.

Any capital framework for the Enterprises must be properly balanced to ensure that the Enterprises are resilient in the face of significant stress events, while still meeting their public mission and responsibilities to low-income and very low-income borrowers and communities. If capital requirements are set too high, the Enterprises' ability to fulfill their statutory mission across all economic cycles becomes significantly hampered.

CUNA supports the proposed amendments. The ERCF Amendments would replace the fixed PLBA of 1.5 percent of adjusted total assets with a dynamic PLBA of 50 percent of an Enterprise's stability capital buffer. This change would more strongly tie capital requirements at the Enterprises to true risk and allow the PLBA to serve as a true back-stop, rather than a primary driver of capital requirements.²⁰ Further, the Enterprises' CRT programs help facilitate the continued acquisition of higher risk loans throughout the economic cycle due to capital relief afforded to risk transfer.²¹ Accurate capital requirements and the ability to consistently facilitate higher risk lending throughout all cycles will enable the Enterprises to meet their missions more efficiently and effectively.

It should be noted that as in the 2018 Proposal and the ERCF Re-Proposal, the ERCF Amendments do not contain an explicit analysis of the potential impact the proposed amendments to the ERCF may have on mortgage pricing. As not-for-profit, financial cooperatives, credit unions have a specified mission "to meet the credit and savings needs of consumers, especially persons of modest means."²² Pursuant to that mission, in 2020 alone, credit unions originated a record of almost \$256 billion in first-lien mortgages, selling over 21% into the secondary mortgage market.²³ The importance of mortgage affordability as part of the core mission of the Enterprises cannot be overstated since, like many federal credit unions, it is inextricably shaped by Depression-era concerns with access to credit for people of modest means. Accordingly, CUNA urges that the FHFA undertake and release an analysis of the pricing impacts of the amendments to the capital

¹⁹ See Credit Union Principles for Housing Finance Reform, available at <https://www.cuna.org/content/cuna/cuna-org/advocacy/letters---testimonies/2018/cuna-letter-on-enterprise-capital-requirements-proposed-rule.html>.

²⁰ ERCF Amendments at 53238.

²¹ ERCF Amendments at 53236.

²² *Credit Union Membership Access Act*, Pub. L. No. 105-219, § 2(4), 112 Stat. 913, 914 (1998).

²³ CUNA Analysis; NCUA Quarterly Credit Union Call Report Data (Dec. 31, 2020).

requirements it is proposing, and all future proposed amendments to the ERCF should require a similar analysis.

Conclusion

Thank you for this opportunity to comment on these proposed amendments to the ERCF. If you have questions or if we can be of any assistance, please do not hesitate to contact me at (202) 503-7184 or elaberge@cuna.coop.

Sincerely,

A handwritten signature in black ink that reads "E Young LaBerge". The signature is written in a cursive, flowing style.

Elizabeth M. Young LaBerge
Senior Director of Advocacy & Counsel