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Submitted by email to: RegComments@fhfa.gov

RE: Comments/RIN 2590-AA49
2012-2014 Enterprise Housing Goals Proposed Rule

Dear Mr. Pollard:

The Federal Housing Enterprises Financial Safety and Soundness Act of 1992, as amended (the "1992 Act"), requires the Federal Housing Finance Agency ("FHFA") to set housing goals for Fannie Mae and Freddie Mac (the "Enterprises"). On June 11, 2012, FHFA published the "2012-2014 Enterprise Housing Goals" proposed rule (the "Proposed Rule").[1] The Proposed Rule sets forth single-family and multifamily housing goal and subgoal levels for 2012, 2013, and 2014 as well as a request for comment. Fannie Mae appreciates the opportunity to submit comments in response to the Proposed Rule.

Pursuant to the 1992 Act, FHFA has proposed three goals and one subgoal for single-family purchase money mortgages and a single-family refinance goal. FHFA has also proposed one goal and one subgoal for multifamily mortgages financing housing affordable to low- and very low-income families. FHFA also requested comments on whether housing goals credit should be granted for the purchase of a multifamily mortgage that facilitates the conversion of the property secured by the mortgage from affordable rents to market rate rents.

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[1] 2012-2014 Enterprise Housing Goals, 77 Fed. Reg. 34263 (Proposed June 11, 2012) (amending 12 CFR Part 1282).

Fannie Mae is submitting comments on the proposed multifamily goals. Fannie Mae is also responding to FHFA's request for comments.

I. Multifamily Goals

The Proposed Rule follows the structure established in the 2010-2011 final housing goals rule and requires Fannie Mae to finance multifamily units affordable to low-income families and very-low income families. However, the increases in the goals as compared to 2011 are very significant. The specific requirements for each year, as compared to those for 2011 (and the percentage increase for each), are set forth in Figure 1 below.

Figure 1

Year	Low-Income Units	Very Low-Income Units
2011	177,750	42,750
2012	251,000 (≈ 41%)[2]	60,000 (≈ 40%)[3]
2013	245,000 (≈ 38%)	59,000 (≈ 38%)
2014	223,000 (≈ 25%)	53,000 (≈ 24%)

In setting the proposed 2012-2014 multifamily goals, FHFA considered the six statutory factors established by the 1992 Act:

(A) National multifamily mortgage credit needs and the ability of the Enterprise to provide additional liquidity and stability for the multifamily mortgage market;

(B) The performance and effort of the Enterprise in making mortgage credit available for multifamily housing in previous years;

(C) The size of the multifamily mortgage market for housing affordable to low-income and very low-income families, including the size of the multifamily markets for housing of a smaller or limited size;

[2] Percentage of increase over 2011 housing goals.

[3] Percentage of increase over 2011 housing goals.

(D) The ability of the Enterprise to lead the market in making multifamily mortgage credit available, especially for multifamily housing affordable to low-income and very low-income families;

(E) The availability of public subsidies; and

(F) The need to maintain the sound financial condition of the Enterprise.[4]

Based upon 2012 multifamily market activity, the Enterprises continue to be the principal providers of liquidity for multifamily, even with other multifamily participants reentering the market. As discussed below, Fannie Mae estimates that the proposed goal levels could be unattainable, particularly in 2013 and 2014, if either or both of the following occur: (a) the overall multifamily originations market remains flat, or (b) private capital returns to the multifamily market. It is highly unlikely that Fannie Mae will continue to maintain its elevated market share in the future as other private capital sources become more active in the market. In light of these factors, Fannie Mae requests FHFA to consider reducing the multifamily housing goals for 2013 and 2014.

A. Flat Multifamily Market with Slow Improvement

The overall multifamily originations market is expected to remain fairly flat over the next two years due to several factors. The key factor is the lack of upcoming multifamily housing supply. As shown in Figure 2, multifamily new construction starts are just beginning to return to more normalized historical averages. Over the 10-year period of 1989 through 2008, the annual average for multifamily starts was approximately 265,000 units. At the end of the second quarter of 2012, that average had returned to slightly more than 220,000 annualized units. As a result, the sector could return to a more normalized annualized rate of about 245,000 units started as early as the end of this year.

[4] Proposed Rule at 34274.

Figure 2. Multifamily starts at below average levels.[5]

Nevertheless, while the potential of oversupply occurring is limited to a few submarkets, the outlook for new multifamily construction in 2013 and 2014 remains cautious. Although as of April 2012 there were more than 500,000 apartment units in the planning stages, it is uncertain how many of those units will make it to groundbreaking. Historically, less than half of all units in the planning stages actually make it to completion. At this rate, an estimated 215,000 of the planned units will eventually come online, less than the previous 10 year annual average of 265,000 units.

More importantly, over the short-run completions of multifamily units currently underway are also projected to remain below historical averages. Figure 3 demonstrates the decline in completions from the first quarter of 2012 through the first quarter of 2013. The projected multifamily volume of new construction and the decline in completions create a smaller potential for multifamily financing over the next few years, as there will be fewer properties in need of permanent mortgage financing. In fact, only about 120,000 new apartment units are expected to be completed in 2012. Moreover, after this year only 72,000 additional apartment units are expected to be completed in 2013 and fewer than 14,000 in 2014 and beyond.

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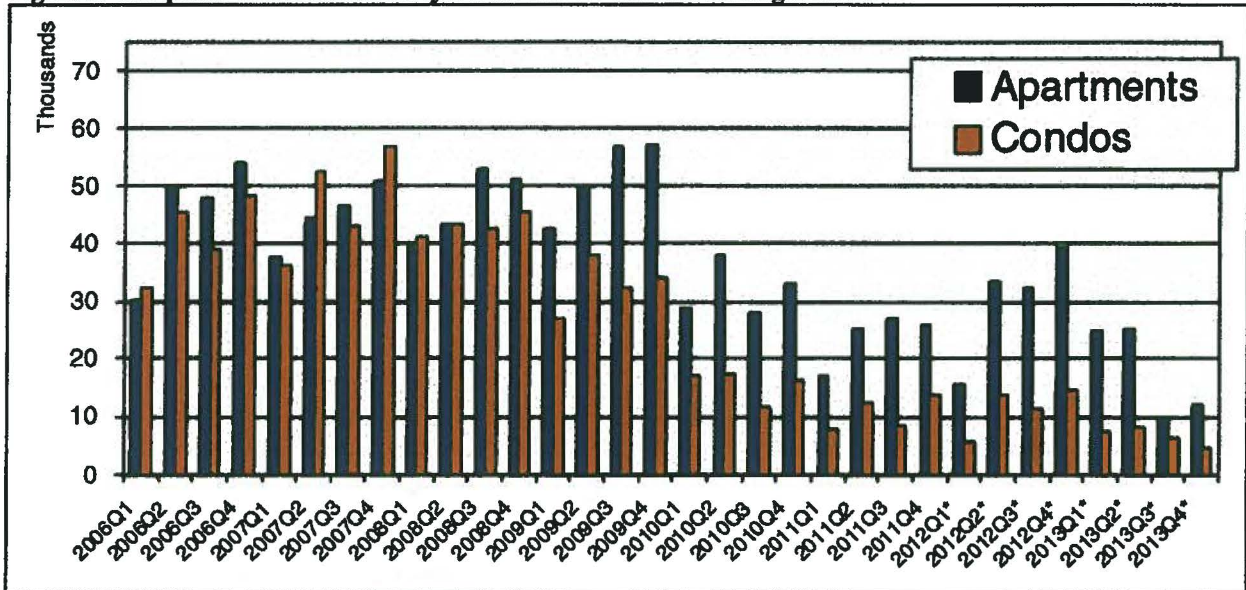
[5] CBRE Global Research and Consulting Econometric Advisors, *Too Much New Supply or Not Enough?, Multi-Housing Client Conference Call, Q1 2012*, page 15 (May 15, 2012).

Figure 3. Completions for 2012 and Beyond at Below Historical Average Levels.[6]



In addition, multifamily refinance volumes are likely to remain muted through 2014 as depicted in Figure 4. This is largely due to the concentration of refinance activity that occurred during the peak of the multifamily market from 2005 through 2007. Most mortgage loans originated during this period are not expected to be refinanced until after 2014. As indicated below, projections from the Mortgage Bankers Association indicate that non-bank loan maturities will only marginally increase from 2010 and 2011 levels, to approximately $25-$30 billion annually for the 2012-2013 period.

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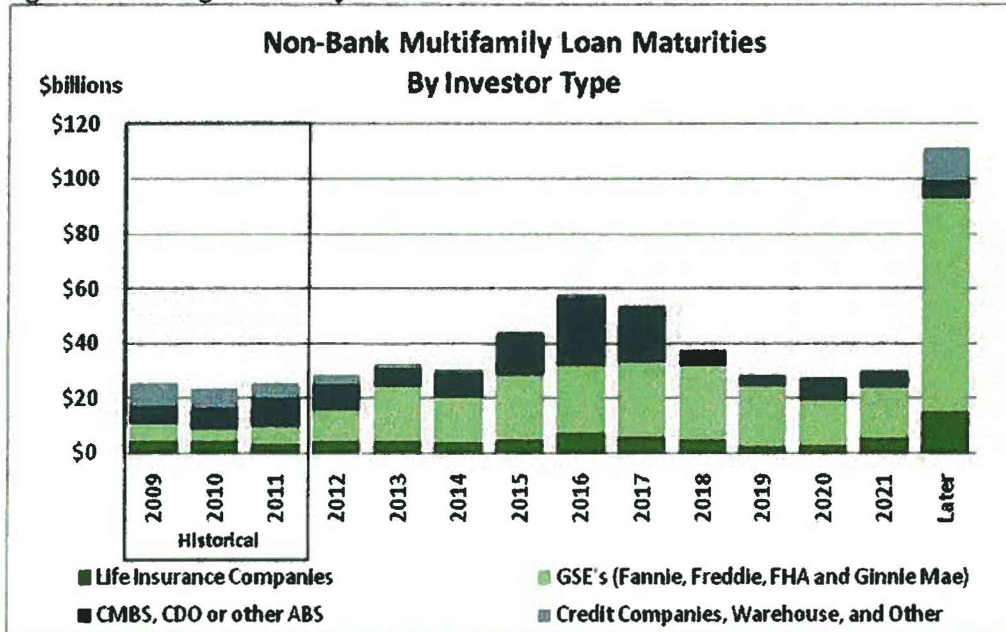
[6] This chart was created by Fannie Mae's Multifamily Economics and Multifamily Research team using data provided by the CBRE Econometric Advisors/Dodge Pipeline as of April 2012.

Figure 4. Maturing Multifamily Loans Remain Muted in 2012-2014.[7]



Consequently, due to all of these factors, Fannie Mae does not project the multifamily market to increase significantly over the next few years. As the market began its recovery after the Great Recession,[8] Fannie Mae estimated that the size of the competitive multifamily mortgage originations market[9] increased from approximately $42-$43 billion in 2009 and 2010 to $72 billion in 2011. Fannie Mae anticipates that the estimated competitive multifamily originations market over the next three years (2012–2014) will rise, but then remain flat in the current range of $80-$85 billion, based on the dearth of new multifamily supply requiring permanent mortgage financing, levels of multifamily starts, and the significant lack of potential mortgage refinancing

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[7] Mortgage Bankers Association Commercial Real Estate/Multifamily Finance, *Loan Maturity Volumes*, page 5 (as of December 31, 2011).

[8] The Great Recession is commonly defined as the worst economic recessional period in the history of the United States since the Great Depression and generally refers to a period starting in December of 2007.

[9] "Competitive multifamily originations market" is not an all-encompassing description or term, but refers to the multifamily mortgage market including Fannie Mae's closest competitors (e.g., Freddie Mac, depository institutions, life insurance companies, and conduits).

activity. Additional considerations that may impact the size of the multifamily market include the national economy remaining stable and not experiencing any further deterioration, job growth remaining positive, and interest rates not beginning to increase. Any change in all or some of these factors could adversely affect multifamily acquisition and refinance activity for permanent mortgages.

B. Reentry of Private Capital

The proposed multifamily housing goals range from 24 percent to 41 percent higher than the 2011 goal levels. Since the implementation of the separate multifamily housing goals in 2010, Fannie Mae has exceeded the goals, particularly in 2011.[10] However, while Fannie Mae's estimated competitive multifamily originations market share reached an historical high of 52 percent in 2008, it has steadily decreased since then to 33 percent in 2011. From 2003-2007, Fannie Mae's market share was in the range of 21 to 28 percent and within a range of approximately $20 billion in production during the pre-2007 boom in the market, which reflects the normal market share and production level for the company's multifamily business.

Based on past participation of other private capital participants in the multifamily market, such as depository institutions, life insurance companies, and conduits, Fannie Mae expects that other sources of capital may increase in 2013 and 2014, thereby shrinking the company's estimated competitive multifamily originations market share and overall production level. In the Proposed Rule, FHFA also acknowledges that it anticipates private capital will reenter the multifamily market.[11] Fannie Mae agrees with FHFA's statement in the Proposed Rule that by 2011 "traditional competitors such as life insurance companies, conduits and banks re-entered multifamily lending"[12] and "[t]he decline in Enterprise multifamily mortgage market share should continue through 2012-2014...[13] Consequently, Fannie Mae's ability to achieve the elevated proposed multifamily goal and subgoal for 2013 and 2014 will likely be adversely impacted.

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[10] Fannie Mae 2011 Annual Housing Activities Report and Annual Mortgage Report, March 15, 2012; Fannie Mae 2010 Annual Housing Activities Report and Annual Mortgage Report, March 16, 2011.

[11] Proposed Rule at 34274.

[12] Proposed Rule at 34279.

[13] *Id.*

C. Fannie Mae's Very Low-Income Goal is Too High Relative to Its Production Share of the Market

The Proposed Rule sets Fannie Mae's very low-income goal level at 60,000 units, nearly twice as high as Freddie Mac's goal level of 32,000 units. Total loan volume as reported in the Enterprises Forms 10-K show that Fannie Mae's differential in loan volume was only 22 percent higher than Freddie Mac's. This would seem to indicate that a production differential of 88 percent for Fannie Mae in the very low-income goal levels is too high given the lower differential in recent total production levels for Fannie Mae and Freddie Mac.

II. MULTIFAMILY AFFORDABLE CONVERSIONS

As noted above, FHFA also requested comment on whether housing goals credit should be granted for the purchase of a multifamily mortgage that facilitates the conversion of the property secured by the mortgage from affordable rents to market rate rents. Fannie Mae appreciates FHFA's concern regarding the conversion of multifamily properties from affordable rents to market rate rents, but believes that additional requirements to monitor such conversions are burdensome and impractical. Based upon its experience, the company believes that conversions of properties that result in significant rental increases are rare. Finally, Fannie Mae does not structure permanent loans using projected rents under its underwriting standards, so borrowers do not benefit from anticipated rent increases at the time of loan origination.

In the Proposed Rule, FHFA requested comment:

> ...on whether the housing goals regulation should be amended to address the possibility that a multifamily mortgage financing the conversion of a property from affordable rents to market rate rents could be treated as affordable under the Enterprise housing goals. In particular, FHFA requests comment on whether §1281.15(d) should be revised to require the Enterprises to use projected rents to determine affordability if such projected rents are available.[14]

Fannie Mae agrees that mortgages on some properties that have converted to market rate rents may not qualify for housing goals purposes, although many properties with market rate rents do qualify. However, essentially asking Fannie Mae to anticipate and potentially restrict this future possibility and using the housing goals regulation to achieve this objective is not appropriate or practical for the reasons discussed below.

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[14] Proposed Rule at 34280.

A. Projected Versus Actual Rents

As FHFA acknowledged in the Proposed Rule, Fannie Mae underwrites actual rents when determining loan amounts and does not use projected rents. Loans are sized and structured based on actual rents. This is sound underwriting and avoids speculative over-lending. Under Fannie Mae's Delegated Underwriting, Selling and Servicing ("DUS®") platform, there is no protocol to capture borrowers' prospective plans for properties. Loans delivered to Fannie Mae by DUS lenders and their affiliates represented 86 percent of the company's multifamily guaranty business as of December 31, 2011.

Challenges would most certainly exist if Fannie Mae were required to determine projected rents. Given the uncertainty of market conditions, particularly further into a loan term, it would be very difficult to predict what those rents might be. There are many factors that influence rents including supply, demand, economic conditions, and other variables.

Imposing this requirement would also raise the possibility of potentially discouraging re-investment through capital expenditures to improve the conditions of properties if borrowers thought that permanent financing could not be secured if they planned to increase rents. It should be noted that property rents will always be tempered by the prevailing market rate rents. Many properties that qualify for housing goals are market rate properties (non-rent restricted) whose rents are affordable at the prescribed area annual median income levels. Fannie Mae does not recommend allocating credit away from properties that are currently affordable and may well remain affordable for the long run based on speculative plans to increase rents in the future. Therefore, Fannie Mae does not believe that amending the housing goals regulation to impose this requirement is an effective mechanism to support long-term affordability.

B. Projected Rent Rolls

A number of challenges would be created if the housing goals regulations were amended to use projected rents to determine affordability. Fannie Mae's multifamily business does not currently collect projected rents and believes it would be very difficult to predict what such rents might be during the term of the loan. In order to accommodate the request associated with the collection of projected rents for scoring purposes, significant expenditures would be required to modify the company's housing goals systems. It would be necessary for Fannie Mae to collect two sets of rent rolls (actual and projected) for properties that might undergo conversion. To accommodate the collection of dual rent rolls would require that Fannie Mae incur significant expenses (estimated at over $1.5 million) to change its technology systems. These expenses would be in addition to the costs associated with the manual processes to perform quality control, compile, and report on those transactions. Fannie Mae's lenders would also incur significant expenses related to technology and processes as well.

Additionally, Fannie Mae has serious concerns about the certification of the projected rent rolls. The current certification process for the actual rents used for housing goals purposes is based upon the certified rent rolls received from the borrower. Rent rolls are tied back to actual leases. It is uncertain what would be the basis for certification of the projected rents. It is also unclear how the certification of the projected rent roll would be implemented. As a result, many questions emerge. Does it become a new representation and warranty under the loan documents? What is the scope of the certification? There are numerous reasons why a property owner may raise rents over time from an affordable to market level (e.g., unit turnover, updating of the unit, increased costs, etc). If a property owner certifies that a property is not the subject of an overall conversion, does that mean there cannot be rental increases for individual units? What would be the consequences for a breach of a representation and warranty on this subject? Does it bind the borrower for the entire term of the loan or a set period? Does Fannie Mae hold the borrower in default for a breach of this representation or merely exclude the mortgage from consideration for housing goals credit retroactively? The list of possible enforcement mechanisms and inherent challenges posed by using projected rents is limitless. Moreover, to add this requirement, which would necessarily trigger the implementation of a new initiative, seems unjustified at a time when FHFA has directed Fannie Mae to conserve its resources.

C. Focus on Affordable Housing Preservation

As opposed to financing conversions of affordable units to market rate units, Fannie Mae has been actively promoting the preservation of affordable units. A dedicated team within the multifamily business oversees the financing of rent or income restricted multifamily properties. A significant portion of Fannie Mae's multifamily business is related to the preservation of affordable units at properties that are at or near the end of the property's low income housing tax credit ("LIHTC") period. At these properties, there are typically long-term rent or income restrictions that extend beyond the respective LIHTC period. The combination of Fannie Mae long-term financing and these rent and income restrictions assure continued affordable rents at the properties.

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Fannie Mae hopes that these comments on the Proposed Rule are helpful as FHFA works to finalize the housing goals for 2012-2014. We look forward to working with FHFA to address the issues raised by the Proposed Rule.

If you have questions regarding the matters addressed in this letter, please feel free to contact me at (202) 752-1648.

Sincerely,

Judith C. Dunn