NCSHA
National Council *of*
State Housing Agencies

May 22, 2022

Mr. Eric Bryant
Policy Analyst
Division of Housing Mission and Goals
Federal Housing Finance Agency
400 Seventh Street, SW
Washington, D.C. 20219

RE: Proposed Enterprise New Product; Comment Request 'Freddie Mac Single-Family Closed-End Second Mortgages,' (no. 2024-N-5)

Dear Mr. Bryant:

The National Council of State Housing Agencies (NCSHA)[1], on behalf of the nation's state housing finance agencies (HFAs), thanks the Federal Housing Finance Agency (FHFA) for the opportunity to comment on Freddie Mac's proposed new Closed-End Second (CES) mortgage loan product.

We applaud Freddie Mac for its innovation and identifying a need in the market and seeking to create liquidity for a mortgage product other than a first lien mortgage loan. The CES mortgage loan appears to be targeted to homeowners who do not have mortgage loans for down payment assistance (DPA) and who would otherwise seek to do a cash-out refinance, for any purpose, but for whom it makes no financial sense to do so because their first mortgage interest rate is low compared to today's higher interest rate environment.

We recognize it is prudent to introduce a new product that has a narrowly-drawn credit box from which Freddie Mac can learn and expand over time as it gains more performance experience with the new product. However, while the credit box has been narrowly defined, the use of proceeds has not been defined at all, allowing homeowners to use the CES proceeds for any purpose whatsoever.

[1] NCSHA is a nonprofit, nonpartisan organization. None of NCSHA's activities related to federal legislation or regulation are funded by organizations that are prohibited by law from engaging in lobbying or related activities.

Unfortunately, the CES mortgage loan product as proposed will have extremely limited use to state HFAs and the low- to moderate-income homeowners they serve. This is largely because the DPA programs that are the hallmark of state HFA first-time homebuyer and low- to moderate- income homebuyer programs result in higher loan-to-value ratio loans and because the DPA loans are generally in second lien position. Additionally, because the proposed CES mortgage loan product does not specify eligible uses of CES mortgage loan proceeds, it misses an opportunity to explicitly advance Freddie Mac's Duty to Serve Underserved Markets (Duty to Serve) activities by specifically providing liquidity to the home improvement and repair lending market.

In its final approval, we urge FHFA to incorporate NCSHA's recommended changes below to enable the CES mortgage loan to better support the affordable housing mission of both Freddie Mac and state HFAs, but also to more explicitly advance Freddie Mac's Duty to Serve activities by supporting the liquidity of subordinate lien home improvement mortgage loans.

State HFA Mortgage Loan Programs Incorporate Second Lien Downpayment Assistance

DPA is a critical component of state HFAs' single-family home loan programs. In 2022, 80 percent of state HFA mortgage program borrowers received DPA and the average amount of DPA provided to HFA borrowers was $10,360. State HFAs provide DPA assistance in a variety of forms, including grants, amortizing second mortgage loans, and forgivable second mortgage loans.

State HFAs that originate under Freddie Mac's HFA Advantage® product guidelines structure their DPA programs to conform with Freddie Mac's Affordable Seconds® requirements. Those requirements permit total loan-to-value (TLTV) lending up to 105 percent TLTV.

Freddie Mac has been an important partner to state HFAs by encouraging the use of DPA for low- to moderate-income homebuyers through its release of DPAOne® and its work with Fannie Mae to develop state-level standard DPA documentation. It was an important partner to NCSHA in the development of the HFA1 Affordable Homeownership Toolkit, a multi-year project that makes it easier for multi-state lenders to use an "aligned" state HFA homeownership program and access state HFA DPA funds for homebuyers. The combination of these efforts and the HFAs' DPA funds are indeed making the dream of homeownership possible for those who do not have family wealth to support their purchase of a home and who need a flexible source of down payment and/or closing costs. But these activities also include higher TLTV mortgage loans that will take longer for the homeowner to achieve a TLTV ratio below 80 percent.

It would rarely make sense for a homeowner with a deferred or forgivable DPA structure to ever replace those funds with market rate ones. Hence, because of the widespread use of DPA in state HFA mortgage loan programs, the resulting higher TLTVs of the loans, and the CES mortgage loan 80 percent TLTV maximum, it is unlikely that any state HFA homebuyer with DPA will be able to take advantage of the CES mortgage loan unless our recommendations below were incorporated into the CES design.

The Great Need for Home Improvement and Repair Funds to Improve Housing Supply

According to the National Association of Home Builders, the median age of owner-occupied homes is 40 years old[2], and as each year passes by, that median age increases. Furthermore, over the course of a thirty-year mortgage, should a homeowner stay in their home during that time, they likely will need to update or replace most major appliances and systems within the home. As the Federal Reserve Bank of Philadelphia estimates, the cost of addressing physical housing deficiencies nationwide could be $149.3 billion.[3]

As Harvard's Joint Center for Housing Studies details in its "Improving America's Housing 2023," in 2021, "homeowners spent the equivalent of 10.6 percent of their incomes on home improvement and maintenance on average". However, lower income homeowners spent an equivalent of 20.1 percent of their income on home improvements and maintenance.[4] That study also notes that replacement projects represent a larger share of homeowner improvement budgets in 2021 than in 2007 – and those types of projects typically include improvements that affect the home's safety and efficient functioning and therefore cannot be delayed indefinitely.[5] Homeowners clearly could benefit from being able to access their home equity to make such improvements, particularly homeowners who have a lower interest rate first mortgage.

There currently is no standardized, national home improvement subordinate lien product, let alone a liquid secondary market for such loans. Freddie Mac's CES mortgage loan could be the start of such a market and could play a significant role, over time, in bringing down the cost of home improvement and repair financing to homeowners with a Freddie Mac mortgage. The CES mortgage loan has the potential to be one of the ways that Freddie Mac and its partners, particularly the mission-focused state HFAs, can work together to help address one aspect of our national housing supply shortage – preserving single-family affordable homes. While not *low-cost*, the CES mortgage loan would be a *lower-cost* solution for homeowners who

---

[2] https://eyeonhousing.org/2024/02/the-age-of-the-u-s-housing-stock/
[3] Eileen Divringi, Community Development Research Specialist, Federal Reserve Bank of Philadelphia "Research Brief: Updated Estimates of Home Repair needs and Costs" March 2023.
[4] Joint Center for Housing Studies of Harvard University, "Improving America's Housing 2023," page 14.
[5] Ibid, page 7.

have been repaying their lower-interest rate mortgage and who want to borrow the equity that they have built up over time rather than use other, higher cost options in the market. A CES mortgage loan, for example, would certainly be more affordable than the other ways homeowners finance home repairs or energy efficiency improvements, such as with a credit card or consumer loan, and would clearly support Freddie Mac's Affordable Housing Preservation Duty to Serve Plan goals.

NCSHA's Recommendations to Improve the CES Product Proposal

To realize the full potential of Freddie Mac's CES mortgage loan and to maximize its support of Freddie Mac's Duty to Serve Plan goals, we recommend that the following characteristics be incorporated into the final approval of Freddie Mac's CES mortgage loan product:

- Where a homeowner's Affordable Second® is either a deferred or forgivable loan, permit the CES mortgage loan to be in third lien position.
- Permit the HFA to use a different Freddie Mac-approved seller for its CES mortgage loans.
  - Most HFAs serve as intermediaries and do not have a retail channel. Their program loans are originated through their approved lender partners. Hence, different Freddie Mac "sellers" could potentially originate the first and CES mortgage loans, even if those HFAs (or their subservicer) actually service both loans.
- Where a Freddie Mac first mortgage loan is originated under a state HFA mortgage loan program, allow different Freddie-Mac approved servicers to service the first and the CES mortgage loans.
  - Six state HFAs use a sub-servicer for their first mortgage portfolio and another 16 service their own mortgage program loans (and own the risk).
  - Approximately two-thirds of state HFAs sell their program loans to a master servicer. Without permitting different Freddie Mac servicers to service the first and CES mortgage loans, these HFAs would be prohibited from helping the homeowners in their homeownership programs access their equity through Freddie Mac's proposed new product unless the master servicer also serviced the CES mortgage loans.
- Where the homeowner would use a CES mortgage loan for a purpose that supports Freddie Mac's Duty to Serve Plan goals, such as Affordable Housing Preservation, permit the TLTV to be at or below 90 or 95 percent.

- Permitting origination of a CES mortgage loan at this higher TLTV level would not only strengthen the collateral backing Freddie Mac's loans, but also increase the homeowner's sustainability by lowering the cost of improving, repairing or updating their home, or allow the homeowner to age in place.
- As part of its Affordable Housing Preservation goals, Freddie Mac should support energy efficiency or renewable energy repairs under the "home improvement/repair umbrella" with the CES mortgage loan product, too, as such financings clearly support both the preservation of single-family housing, as well as increase homeowner sustainability through lower energy costs.

- Where an HFA has originated (or a program partner has originated for an existing state HFA program) CES-like mortgage loans that support Freddie Mac's Affordable Housing Preservation Duty to Serve Plan goals and which pre-date Freddie Mac's CES product approval, permit Freddie Mac to purchase bulk loans and provide liquidity to the state HFA's program.
    - A seasoned loan portfolio would enable Freddie Mac to review loan-level performance history and choose the loans that it would agree to purchase.

- Permit CES mortgage loan amortization to extend to when the final payment on the first mortgage loan is due, rather than limit it to 20 years.

- Should an appraisal be required for the CES mortgage loan (see question below), permit use of an automated valuation model (AVM) to reduce homeowner transaction costs.

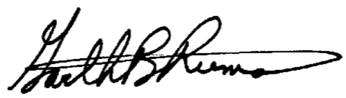
Additionally, before launching its CES mortgage loan, we urge Freddie Mac to provide answers to the following questions:

- What are the origination requirements of the proposed CES mortgage loan? For example, would an appraisal be required to establish the home's value and if so, would a valuation based on an AVM, which is of minimal cost compared to that of a full blown appraisal, be sufficient?
- What would be the closing cost requirements? Would a title update be required, for example?

* * *

While NCSHA applauds the effort Freddie Mac has put forth to create additional value as a mortgage loan liquidity provider, the true value and opportunity for the proposed CES mortgage loan is that it could provide a lower-cost option for existing homeowners and improve sustainability. Providing homeowners with options not currently generally available in the market to age in place, make needed home improvements or updates to dated properties, and conduct energy-efficiency or renewable energy upgrades, would also enable Freddie Mac to strengthen the collateral that backs its loans. By augmenting the proposal as we suggest above, state HFAs, in partnership with Freddie Mac, could serve the homeowners they work so hard to put into homes by helping them to more affordably access the equity they build up over time while also helping to address affordable housing supply challenges.

Sincerely,



Garth Rieman
Director of Housing Advocacy and Strategic Initiatives