America's Credit Unions

May 22, 2024

The Honorable Sandra L. Thompson
Director
Federal Housing Finance Agency
725 17th Street, NW
Washington, DC 20503

RE: Freddie Mac Proposed Purchase of Single-Family Closed-End Second Mortgages (No. 2024-N-5)

Dear Director Thompson:

On behalf of America's Credit Unions, I am writing in response to the Federal Housing Finance Agency's (FHFA's) Request for Comment for "Freddie Mac Proposed Purchase of Single-Family Closed-End Second Mortgages" (RFC).[1] America's Credit Unions is the voice of consumers' best option for financial services: credit unions. We advocate for policies that allow the industry to effectively meet the needs of their nearly 142 million members nationwide. America's Credit Unions appreciates the opportunity to comment on the potential for Freddie Mac to purchase closed-end second mortgages as an alternative to cash-out refinances. As a voice for credit unions, America's Credit Unions supports the introduction of this new product and Freddie Mac's efforts to increase liquidity in the housing market. We also encourage Freddie Mac to institute a smooth process to facilitate these transactions and provide support for the responsible scaling of this product.

General Comments

Freddie Mac proposed to purchase closed-end second mortgages as an alternative to cash-out refinances which cancel a borrower's first mortgage, which, if recently purchased or refinanced, is likely to have a more attractive interest rate than one that could be acquired presently. In accordance with the Federal Housing Enterprises Financial Safety and Soundness Act of 1992, you, as the FHFA director, are reviewing this product to determine whether it is in the public interest. America's Credit Unions believes the proposal is in the public interest and advances Freddie Mac's public mission. We wish to stress that it is important consumers use this process thoughtfully and refrain from exposing themselves to delinquency or default by withdrawing the balance of their savings. The current environment of high interest rates and inflation has stressed the budgets of American consumers. If a consumer is determined to borrow money, it is more sensible to borrow it from themselves at a reasonable interest rate than to turn to high interest options like credit cards and payday loans. Should this product be approved, we expect Freddie Mac recognize this increased risk and account for it as the new program is developed.

[1] https://www.federalregister.gov/documents/2024/04/22/2024-08479/freddie-mac-proposed-purchase-of-single-family-closed-end-second-mortgages-comment-request

We further believe that Freddie Mac should tailor its product to interact smoothly with the underwriting process and be scalable to higher amounts. We also recommend Freddie Mac consider the level of credit risk and the role of Loan Level Pricing Adjustments (LLPAs) when designing its final product.

Smooth, Scalable Process

America's Credit Unions encourage Freddie Mac to institute a smooth, scalable process to allow maximum benefit to lenders seeking additional liquidity while keeping risks low. The process must not be cumbersome for the lender, the pricing for the product must be clear and sensibly recoup costs for the lender, and it must be scalable to allow for products that far exceed the example shown in Table 3 of the RFC. While those numbers are on point for some borrowers, others may request $130,000 of equity rather than just the $30,000 used in the illustration.

The requirement for Freddie Mac to hold the first lien is a guardrail to curtail risk. That does create an atypical discovery process where the lender must manually confirm the ownership of the first lien. Utilizing the lookup tool on the Freddie Mac website is an additional underwriting step. The process could be streamlined if a better method to surface the data could be applied, such as integrating the lookup tool with common underwriting software.

Additionally, our members would like to see more details regarding the pricing of this product. Many lenders already offer second mortgage products that benefit homeowners, with low to no closing costs or fees. Lenders recoup these costs through interest income. To encourage participation in the program, Freddie Mac must set prices with a premium to offset these costs or the lender will have reduced incentive to sell the second mortgage.

We also encourage scalability. Table 3 in the RFC illustrated an example of borrowing against an 80 percent LTV mortgage. The payment for the original mortgage of $150,000 with a 3 percent interest rate and the payment for the new second mortgage combined would be approximately 13% lower than the newly refinanced mortgage of $150,000 with a 7.5 percent interest rate. However, those savings would decrease for loans with lower LTV ratios and borrowers with higher interest rates, which would lead to fewer borrowers benefiting from this program.

Credit Risk

America's Credit Unions encourage the consideration of credit risk to play a role in the purchase of these second mortgages. We supports equal access to the secondary mortgage market for lenders of all sizes, but are concerned that if too many lightly supervised entities such as nonbank mortgage companies (NMCs) fintechs, and high-volume lenders participate in this program, delinquencies could rise. Traditionally, those lenders service fewer loans than they make and do not cultivate the everyday, long-lasting financial relationships with their borrowers that one sees with credit unions and other community lenders. Regular communication with consumers encourages loss mitigation measures before the borrower has fallen too far behind. Delinquencies can raise the costs for other entities that retain stakes in the loans they make.

On May 10, 2024, the Financial Stability Oversight Council (FSOC), on which you as FHFA Director are a voting member, released its most recent report on NMCs. It detailed some of the vulnerabilities of those lenders, including “reliance on debt that can be repriced, reduced, or canceled in times of stress, can lead to significant liquidity risk, which is exacerbated by high leverage carried by some NMCs.”[2] We encourage Freddie Mac to follow FSOC’s recommendations to mitigate these vulnerabilities and be discerning in its choice of loan acquisition.

Loan Level Pricing Adjustment

Customers deserve to choose from a menu of sensible options. While the RFC clearly demonstrates how a consumer would have a lower monthly payment and less total interest under its second mortgage option, America’s Credit Unions also supports the lowering of LLPAs for cash-out refinances to lower the overall interest rate and make them a more competitive product. The Freddie Mac LLPA matrix for cash-out refinance loans shows that all borrowers are subjected to additional fees that inflate the cost of cash-out refinance mortgages and make them less competitive when compared with second mortgages. Even borrowers with excellent credit must pay a 1.375 percent fee with an LTV between 75 and 80 percent and a 0.375 fee with an LTV under 60 percent. Those fees increase the interest rate the borrower would otherwise be paying, which increases their monthly payment. A cash-out refinance with a lower overall interest rate would be more competitive against a closed-end second mortgage. no matter their LTV.[3] Freddie Mac should lower its LLPA percentages, especially for those with higher credit scores if it wants to make it more affordable to convert home equity to cash.

Conclusion

America’s Credit Unions appreciates the opportunity to comment on this topic. If you have any questions or concerns, please do not hesitate to contact me at asmith@AmericasCreditUnions.org or (703) 842-2803.

Sincerely,

Amanda L Smith

Amanda L. Smith
Senior Regulatory Affairs Counsel

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[2] https://home.treasury.gov/news/press-releases/jy2331
[3] https://guide.freddiemac.com/euf/assets/pdfs/Exhibit_19.pdf