December 8, 2016

The Honorable Melvin L. Watt
Director
Federal Housing Finance Agency
400 7th Street NW
Washington, DC 20219

The Honorable Jacob J. Lew
Secretary
U.S. Department of the Treasury
1500 Pennsylvania Ave NW
Washington, DC 20220

Dear Director Watt and Secretary Lew:

We, the undersigned, are writing to express our concerns about the Government Sponsored Enterprises' (GSEs) performance on some of their Single Family Housing Goals, and pricing issues affecting a range of low-and moderate-income borrowers. The constraints on access to affordable mortgage credit seen across the broader mortgage market for a range of borrowers reflect, in part, how the Federal Housing Finance Agency (FHFA) is pricing the Enterprises' affordable housing business and managing their charter mandate to undertake "activities relating to mortgages on housing for low- and moderate income families involving a reasonable economic return that may be less than the return earned on other activities."[1] This is evidenced in both the Enterprises' sporadic performance on some of their affordable housing goals and the relatively low number of loan guarantees for a range of borrowers across the credit score spectrum. We also believe it reflects the constraints of the conservatorship on the ability of the Enterprises to develop products, make investments and conduct outreach in communities to facilitate affordable housing.

Under their affordable housing goals and Housing and Economic Recovery Act (HERA), the GSEs have explicit responsibilities to ensure that borrowers from traditionally underserved and/or excluded communities will have access to the mortgage market. Not only are these obligations addressed by statute, they are essential to the recovery of the housing market and the U.S. economy. Historically, the GSEs have played a vital role in creating a national mortgage market, providing access during times of market stress, and preserving the thirty-year fixed rate mortgage – all of which promote access and affordability. The GSEs are in a position to pool large amounts of mortgages across all geographic locations over time, and may though this provide a greater degree of access to the nation's mortgage finance system while also mitigating risk. Through the scorecard process, FHFA must address areas where the GSEs could reduce fees to promote greater access to the housing market.

FHFA's 2017 Scorecard must target a greater level of average-cost pricing than is reflected in the Enterprises' current pricing and a lower return on capital

[1] 12 U.S.C. 1716(3)

FHFA's upcoming 2017 Scorecard must target a greater level of average-cost pricing and lower the rate of return on capital being reflected in the pricing at both Enterprises. Quite simply, the Enterprises' average guarantee fees are too high. The differences between capital and fees on the Enterprises' loans across the credit score spectrum and for various LTV ranges have undermined their ability to average pricing effectively, and to ensure that the broadest range of underserved borrowers have access to the wealth-building opportunity of homeownership.

The companies' current average guarantee fees are far higher than is required to cover the expected losses on their current book of pristine business. Defaults on the most recent originations are tracking well below 2001–04 mortgages at the same age,[2] when average guarantee fees were far lower and there were no loan-level price adjustments (LLPAs). We believe that FHFA has considerable latitude to allow both Enterprises to reduce their average guarantee fees as well as their pricing on lower credit score and higher LTV loans without significantly affecting the Enterprises' overall economic results.

Both FHFA and the Treasury Department have acknowledged tight credit across the credit spectrum and both have a role in alleviating it.

In October, both FHFA and the Treasury Department acknowledged the challenges facing a range of creditworthy borrowers who are not being served in the conventional mortgage market. Both agencies have also acknowledged that the Enterprises should do more to help. Even within the confines of conservatorship, the Senior Preferred Stock Purchase Agreements (PSPAs), a declining capital buffer and investment portfolios, we believe both FHFA and the Treasury Department can ensure that creditworthy borrowers across the credit spectrum have better access to homeownership. While we remain concerned that accounting volatility at the Enterprises could lead to a draw on the Treasury Department's line of credit that might further undermine the Enterprises' ability to carry out their affordable housing mission, we also believe that both agencies can find ways to ensure appropriate flexibility to their contractual obligations to mitigate that possibility while ensuring that affordable mortgage credit is made more available to underserved borrowers today.

Top officials at the Treasury Department recently acknowledged that 40 percent of all FICO scores nationally fall below 700 and that a relatively small share of new mortgages are being originated to that share of creditworthy borrowers[3]. Although

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[2] *Squeaky-clean loans lead to near-zero borrower defaults—and that is not a good thing,* Urban Institute (August 31, 2016). The report also found that: "The performance of mortgages originated over the past few years has been extraordinarily good by historical standards. Not only is the credit box exceptionally tight, but even controlling for credit characteristics, mortgages are also performing much better."

[3] *Housing Finance Reform: Access and Affordability in Focus*, Counselor Antonio Weiss and Assistant Secretary for Economic Policy Karen Dynan, Medium (October 26, 2016).

the Enterprises' underwriting guidelines allow purchases down to a 620 credit score, the Enterprises are guaranteeing few loans in that range. From 2011 through Q1 2015, at Fannie Mae less than 10 percent of borrowers had FICO scores below 700, 22 percent were from 700 to 750, and 69 percent were above 750.[4] The guarantees at Freddie Mac are very similar.[5] The increase in the Enterprises' guarantee fees and risk-based pricing (LLPAs) has had a number of effects to varying degrees that some predicted, including more banks are holding fixed-rate loans on portfolio, more financing of lower-credit score borrowers by the Federal Housing Administration, and fewer originations to the underserved overall.

Since the introduction of LLPAs, the Enterprises have substantially reduced the level of average cost pricing. In addition, given the context of conservatorship status of the Enterprises, we do not believe the Treasury Department should require a return on capital consistent with the company being shareholder-owned. Whether the Enterprises eventually exit conservatorship or not, the Treasury Department should be willing to accept a positive, though submarket, return on capital on loan guarantees for underserved borrowers to ensure that they have better access to affordable mortgage credit in the conventional market.

The PMIERS rule is further complicating access to affordable mortgage credit. The current "test-and-learn" pilots are not enough.

In addition, the recent increases in mortgage insurance premiums following FHFA's Private Mortgage Insurance Eligibility Requirements (PMIERS) rule last year are further complicating affordable access for a substantial segment of creditworthy borrowers who are also facing other pricing constraints, such as LLPAs. We believe FHFA should ensure that PMIERS and mortgage insurance pricing is not imposing additional barriers on the ability of those borrowers who might qualify, for example, for mortgages through Fannie Mae's HomeReady or Freddie Mac's Home Possible products. Both Enterprises should ensure that profile pricing extends to mortgage insurance to mitigate the finer risk-based pricing implemented since PMIERS.

The Enterprises have a significant history of developing underwriting guidelines and products, making investments and developing partnerships that have safely expanded credit to underserved communities. While we appreciate the recent "test-and-learn" pilot programs, we believe those projects are limited in scope and more significant steps should be taken now to expand access to credit to a broader swath of creditworthy borrowers. The Enterprises are no longer purchasing the nontraditional loans that led to the bulk of their high delinquencies and defaults during the crisis, such as Alt-A and interest-only loans. The Consumer Financial Protection Bureau's Qualified Mortgage rule, as well as other post-crisis regulation, has helped shape an exceptional crop of mortgages. This should grant the Enterprises the flexibility to call on their considerable historical data of safe and

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[4] Ibid. 2.
[5] Ibid. 2.

sustainable products and investments to ensure the broadest possible market of creditworthy borrowers is served across the credit spectrum, including those who are low- and moderate-income, minority and rural.

Conclusion

We are seeking meetings with both agencies to discuss these issues and your recent statements about access to credit. We urge FHFA to outline significant and explicit steps in your 2017 Scorecard to address the Enterprises' sporadic performance on their housing goals by, among other measures, addressing a number of mortgage pricing issues. FHFA should immediately improve the level of average pricing and/or their return on capital reflected in your current guarantee fees to ensure greater access across the credit score spectrum. The agency should also require more profile pricing by mortgage insurers to reverse the negative effects of the more granular pricing they have adopted since PMIERS. Both Enterprises should also call upon their institutional knowledge of safe and sustainable products, investments and partnerships so that both can better fulfill their affordable housing missions and provide better mortgage access to the creditworthy families across the country who are currently being frustrated in their efforts to achieve homeownership – a critical wealth-building tool needed to bridge the nation's growing wealth gap.

If you should have any questions, then please do not hesitate to contact Gerron Levi, Director of Policy and Government Affairs at the National Community Reinvestment Coalition (NCRC) at 202-464-2708.

Sincerely,

Americans for Financial Reform
California Reinvestment Coalition
Center for Responsible Lending
Consumer Action
Corporation for Enterprise Development
Empire Justice Center
The Greenlining Institute
Grounded Solutions Network
The Kirwan Institute for the Study of Race and Ethnicity
The Leadership Conference on Civil & Human Rights
League of United Latin American Citizens
National Community Reinvestment Coalition
National Consumer Law Center (on behalf of our low income clients)
National Council of La Raza
National Fair Housing Alliance
NAACP
National People's Action
National Urban League

National Association for Latino Community Asset Builders
Reinvestment Partners
Woodstock Institute