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September 14, 2016

The Honorable Jeb Hensarling
2129 Rayburn HOB
Washington, DC 20515

The Honorable Harold Rogers
H-305, The Capitol
Washington, DC 20515

The Honorable Maxine Waters
2129 Rayburn HOB
Washington, DC 20515

The Honorable Nita Lowey
H-305, The Capitol
Washington, D.C. 20515

Dear Chairman Hensarling, Ranking Member Waters, Chairman Rogers, and Ranking Member Lowey:

On behalf of the National Community Reinvestment Coalition (NCRC) and our more than 600 member organization, I am writing to express our strong opposition to any congressional attempts to attach piecemeal GSE reform provisions dealing with credit risk transfer transactions or the Common Securitization Platform (CSP) to any must-pass or FY2017 omnibus appropriations legislation. While comprehensive GSE reform legislation has stalled, we oppose congressional efforts to adopt without a full congressional debate individual provisions that would have significant impact on the direction of housing finance reform and further constrain the availability and affordability of credit for a range of low- and moderate-income (LMI) homebuyers. In a June letter to the Federal Housing Finance Agency (FHFA), the American Bankers Association, National Association of Home Builders, National Association of Realtors, and National Housing Conference all opposed a "piecemeal approach" to reform of the government-sponsored enterprises (GSEs) as "counterproductive." Similarly, we oppose a piecemeal approach to housing finance reform through the appropriations process.

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Mandating More Credit Risk Transfers and GSE Revenue Sharing With the Private Sector is Ill-Advised Without a Better Congressional Understanding of These Transactions and Their Impact.

We are very concerned about any bill language that would set arbitrary targets for or require the GSEs to increase first-loss, mezzanine or catastrophic risk sharing without any serious congressional consideration of the impact on the capital position of the GSEs; the availability and affordability of credit for a range of different types of LMI borrowers; and overall fair access to the secondary mortgage market.

The GSEs' Declining Capital

In February, Director Mel Watt stated: "The most serious risk and the one that has the most potential for escalating in the future is the Enterprises' lack of capital."[1] Among the non-credit-related factors that could lead to a loss, he identified the increasing volume of credit risk transfer transactions that also transfer "current revenues away from the Enterprises to the private sector."[2] As you know, starting January 1, 2018, the GSEs will have no capital buffer to offset quarterly losses. We oppose appropriation riders that would arbitrarily increase credit risk sharing transactions and GSE revenue sharing that would further deteriorate the GSEs' capital position, without any real consideration of the impact on their safe and sound operations, their affordable housing mission, or the housing market overall.

Does Credit Risk Transfer Really Mean Private Investors are at Risk?

Before rushing headlong into more risk sharing, Congress should also evaluate and better understand various aspects of how current credit risk transfer transactions work. This includes how much actual credit risk is being transferred from the books of the GSEs to private investors for the price the GSEs and, importantly, borrowers are paying for these transactions.

Since at least 2012, FHFA has sought to "Contract the Enterprises dominant presence in the marketplace" by, among other steps, increasing credit risk transfer transactions beyond the normal charter-required mortgage insurance. Congress and the Administration have placed increasing pressure on both FHFA and the GSEs to share more credit risk with the private sector. Among many questions that should be asked, however, is whether private investors are really at much risk of loss in these transactions.

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[1] *Prepared Remarks of Melvin L.Watt Director of FHFA at the Bipartisan Policy Center,* February 18, 2016.
[2] Ibid.

In one recent Connecticut Avenue Securities (CAS) deal, for example, the prospectus models projected credit losses in 64 different combinations of annual default rates under various prepayment scenarios for investors in the 1M-1 tranche. In none of those instances do private investors sharing risk experience credit losses because the tranche is structured to pay off early, before losses occur.[3] Private investors sharing risk in the 1M-2 tranche are modeled to experience credit losses in only nine of 64 instances.[4] For no or very low projected levels of credit losses, 1M-1 tranche investors receive the LIBOR rate plus 1.45 percent in interest payments from the GSEs, and the 1M-2 tranche investors receive the LIBOR rate plus 4.25 percent. In addition, it is unclear whether borrowers are still paying guarantee fees that imply holding capital on the same credit risk that is supposedly shared with the private sector through Fannie Mae's CAS and Freddie Mac's STACR deals. In other words, are borrowers in essence paying twice through their guarantee fees, both for the GSEs' cost of capital for Fannie and Freddie to protect against credit risk and then again in interest payments to private investors to share that same credit risk? Are these credit risk transfer transactions economic or uneconomic, given the GSEs' cost of capital?

Many Low- and Moderate-Income Borrowers are Boxed Out and Priced Out

Congress should also consider the impact on the cost of credit for low- and moderate-income (LMI) borrowers. Already, many types of borrowers are being "boxed out" of the mortgage market by extraordinary credit standards[5] and the extent of risk-based pricing[6] at the GSEs and in the overall mortgage market. What impact will greater front-end risk sharing, such as deeper mortgage insurance, have on the cost of credit and access to credit for various types of borrowers?

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[3] *Prospectus,* Fannie Mae, Connecticut Avenue Securities, Series 2016-C04. The table at the bottom of page 135, *Class 1M-1 Cumulative Write-down Amount,* shows the projected credit losses (or write-downs) in 64 different combinations of annual default rates (CDRs) and prepayment rates (CPRs). The table on page 132 shows the outstanding balance of the 1M-1 tranche, over a 13-year period under eight different annual prepayment rates (zero to 35 percent per year). Even with zero prepayments, this tranche amortizes completely before it matures. At a relatively moderate annual prepayment rate of 10 percent per year, the 1M-1 amortizes over four years, and at a 15 percent prepayment rate, it amortizes in three years. The average annual mortgage prepayment rate in the high-loss years following the financial crisis exceeded 20 percent per year; at that rate, the 1M-1 tranche would barely be at risk of loss for two years.

[4] Ibid.

[5] *Squeaky-clean loans lead to near-zero borrower defaults–and that is not a good thing,* Urban Institute, August 31, 2016.

[6] *Who Will Receive Home Loans and How Much Will They Pay?* Michael Calhoun and Sarah Wolff, June 2, 2016.

During the financial crisis, both the GSEs and mortgage insurers (MIs) suffered significant losses as a result of defaults and foreclosures. Because many MIs did not have sufficient capital to withstand the sharp downturn, the GSEs and taxpayers suffered losses when some MIs failed to pay their mortgage insurance claims. As a result, and to mitigate the GSEs' counterparty risk with MIs, FHFA finalized Private Mortgage Insurer Eligibility Requirements (PMIERS) last year requiring MI companies to hold more capital and also calculate capital based on the credit quality of the individual loans they insure. In response, private mortgage insurers increased their mortgage insurance pricing this spring, as well as the extent of their risk-based pricing.[7] The more than 250 percent increase in the GSEs guarantee fees since 2009,[8] increasing prices charged by private MIs, the extent of risk-based pricing and the capital considerations and other factors driving that cost of mortgage credit all impact the availability and affordability of mortgages for LMI borrowers.

FHFA's Request for Input on Credit Risk Transfer

FHFA is currently conducting a formal Request for Input (RFI) on their credit risk transfer transactions from all interested parties. Congress should not short-circuit this approach through arbitrary directives to engage in more or particular forms of risk sharing.

Shifting Ownership and Control of the Publicly Financed Common Securitization Platform to the Private Sector through the Appropriations Process Could Also Undermine Affordable Housing

Throughout the GSEs' conservatorship, a time when FHFA has been charged with preserving and conserving the assets of the Enterprises as required by the 2008 Housing and Economic Recovery Act (HERA) that created FHFA, both GSEs have used substantial financial and personnel resources to build the Common Securitization Platform (CSP). The CSP is the core back-end infrastructure of the Enterprises that is envisioned by many reformers to function largely as a public utility to standardize securitizations for much of the larger secondary mortgage market in a reformed housing finance system. We oppose efforts to transfer control of the CSP through the appropriation process to the private sector, and primarily to the largest private financial institutions. The implications of transferring control and direction over how the CSP would be built and the rules of access to the CSP for mortgage loan originators and issuers of mortgage-backed securities should be given full congressional consideration and review. Among other issues, we are concerned that the piecemeal transfer of the CSP to the private sector will undermine the statutory obligations that the GSEs have to facilitate the financing of affordable housing for LMI families and the Affordable Housing

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[7] Ibid.

[8] Fannie Mae and Freddie Mac Single-Family Guarantee Fees in 2014, FHFA (June 2015); Fannie Mae and Freddie Mac Single-Family Guarantee Fees in 2015, FHFA (August 2016)

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Goals. Will the private secondary market players issuing through and using the CSP be subject to the same statutory obligations around affordable housing that the GSEs are now?

For these reasons and more, Congress should not arbitrarily adopt piecemeal provisions in the FY2017 appropriations bills that could impact both the direction of housing finance reform and the availability and affordability of mortgage credit for a range of LMI borrowers. Risk sharing and CSP provisions should not be adopted outside of a comprehensive approach to reforming the housing finance system that will ensure stability and liquidity in the mortgage market, better serve the full range of LMI borrowers and ensure fair access to the secondary mortgage market.

Thank you for your consideration of these views. If you should have any questions, then please feel free to contact Gerron S. Levi, Director of Policy and Government Affairs at 202-464-2708.

Sincerely,

John Taylor
President/CEO
NCRC

cc: Members of the House Financial Services Committee
Members of the House Appropriations Committee