MORTGAGE BANKERS ASSOCIATION

Statement for the Record
For the Housing and Insurance Subcommittee
House Financial Services Committee
"Current Mortgage Market: Undermining Housing Affordability with Politics"
Wednesday, May 17, 2023

The Mortgage Bankers Association (MBA)[1] appreciates the opportunity to comment on the issues raised by the Housing and Insurance Subcommittee's May 17, 2023, legislative hearing entitled, *"Current Mortgage Market: Undermining Housing Affordability with Politics."*

Background

The Federal Housing Finance Agency (FHFA) has implemented a capital framework to promote safety and soundness at the housing Government Sponsored Enterprises (the GSEs), Fannie Mae and Freddie Mac, which has included ongoing efforts to ensure GSE pricing is structured to permit the agencies to increase liquidity for loans to historically underserved borrowers (as required by their charters) and foster a level playing field in the mortgage market.

MBA agrees that there is a need for recalibration of fees to improve access to credit for historically underserved borrowers. Such a recalibration is particularly warranted following recent fee increases for certain high balance loans and second home loans. Balancing these fees to better support "core mission borrowers," as is noted in the FHFA's Strategic Plan, can be done in several ways, including, but not limited to, targeting certain housing types such as manufactured housing or condominiums, or compressing the pricing grids across loan-to-value ratio and credit score dimensions in a targeted fashion. While conducting this pricing review, MBA has encouraged FHFA to continue to facilitate access to the secondary market on equal terms for lenders of all sizes and business models.

MBA has also proposed that the GSEs be regulated similarly to investor-owned utilities. Typically, price regulation in these markets requires nondiscriminatory pricing across the customer base, i.e., there is a level playing field. Pricing also tends to be transparent, with rates and the rate calculation posted for public input. FHFA in its role as conservator has moved regulation of pricing in this direction already, with more level and more transparent pricing than was the case pre-crisis. Pricing and underwriting across various programs and markets should be as transparent as possible to ensure that eligibility, qualification, and pricing information is

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[1] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 390,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets, to expand homeownership, and to extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of more than 2,200 companies includes all elements of real estate finance: independent mortgage banks, mortgage brokers, commercial banks, thrifts, REITs, Wall Street conduits, life insurance companies, credit unions, and others in the mortgage lending field. For additional information, visit MBA's website: www.mba.org.

clearly communicated to the market and balanced by sound risk-management practices. The impact of loan-level price adjustments and other credit enhancements must be evaluated as part of any affordable housing strategy. Lenders in the primary market are better able to serve borrowers to the full extent of the credit box when the parameters of eligibility requirements are well understood and consistent.

Through recent directives, FHFA has taken positive steps to ensure that single-family guarantee fee discounting or other favorable pricing or underwriting variances are not provided to market participants based on their volume, size, or business model.

MBA supports this comprehensive review of the existing GSE pricing framework, including FHFA's attempts to determine appropriate pricing levels that enhance support for mission-focused lending. As always, safety and soundness remain paramount, and any changes to pricing should not introduce excessive risk to the Enterprises – or unduly raise costs for borrowers in the heart of their traditional market.

Changes to the GSEs' Loan-Level Price Adjustments (LLPAs)

On Thursday, January 19, the FHFA announced changes to the GSEs' loan-level price adjustments (LLPAs) and a recalibration and reformatting of their entire pricing matrix. The industry has already adjusted to the first two iterations of changes to the pricing framework – increases to LLPAs for certain second homes and high balance loans and LLPA waivers for certain first-time homebuyers, Home Ready and Home Possible loans, HFA Advantage and HFA Preferred loans, and single-family loans supporting the Duty to Serve program. Together, those changes significantly rebalanced the LLPA framework toward mission-focused lending.

The changes announced earlier this year marked the third iteration of FHFA's ongoing pricing review since early 2022. Pricing grids are now broken out by loan purpose – purchase, rate/term refinance, and cash-out refinance – and are recalibrated to new credit score and loan-to-value ratio categories along with associated loan attributes for each. FHFA noted that these changes will be a way to lock in the previous pricing changes in a more effective framework. The changes took effect for loan deliveries on May 1, 2023, and lenders priced them into loans in the weeks beforehand.

As expressed in MBA's February 3 letter to FHFA Director Sandra Thompson, we were concerned about the unfortunate timing of the new fees at the peak of the spring homebuying season and given current affordability challenges. MBA was particularly troubled and consistently voiced our concerns to FHFA about the addition of an LLPA for loans with a debt-to-income ratio (or "DTI") greater than 40 percent. The implementation of a DTI-based LLPA would have led to several problems, including multiple changes to a borrower's pricing throughout the loan application process, operational and system issues, compliance implications related to TILA-RESPA Integrated Disclosures (TRID), compromised borrower trust, and post-closing quality control (QC) issues.

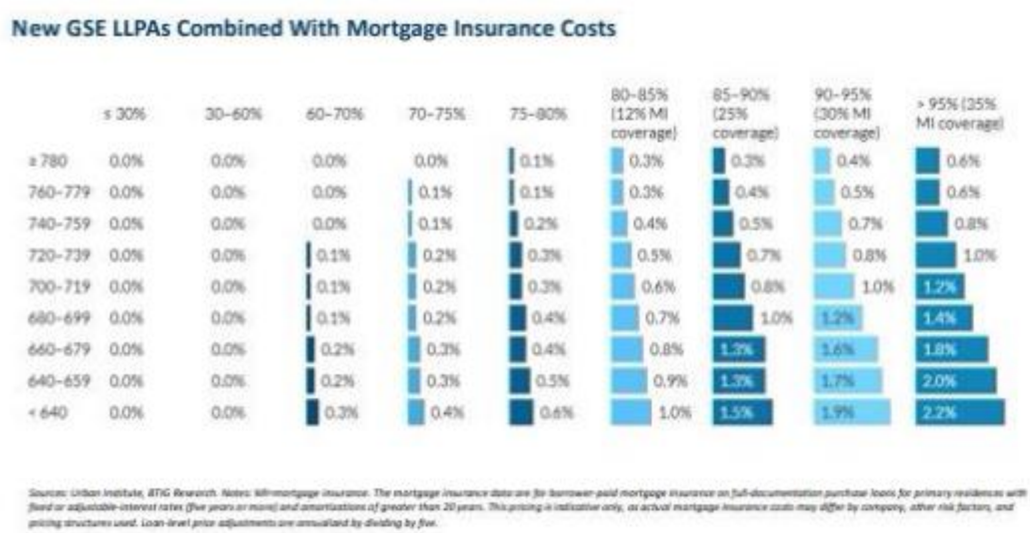
In response to our concerns and to more recent inquiries about the LLPA changes, FHFA announced last week that it is rescinding the DTI-based LLPA. We are pleased that FHFA engaged with industry stakeholders and the Congress, recognized the negative impacts of the fee, and rescinded its implementation.

Concurrently with the rescission of the fee, FHFA has issued a Request for Input (RFI) to provide additional transparency and receive public comment on the process for setting single-family guarantee fees. MBA will continue its engagement with lawmakers (including this Subcommittee), FHFA, and other industry stakeholders to ensure clarity and transparency regarding the GSEs' pricing framework and looks forward to responding to the RFI.

Recent Debate Regarding the LLPA Changes

Over the past few weeks, coverage of the FHFA's new LLPA grid, and in particular the extent to which the new pricing framework departs from a purely risk-based framework, has gone "viral" and resulted in significant discussion, in both the media and the Congress, igniting a spirited policy debate.

In late April, a spate of articles and TV news segments reported that riskier borrowers with weak credit and small downpayments were getting lower rates than high FICO borrowers with large downpayments. This is not true. While the changes to the base FICO/LTV grids narrowed the differences between high FICO/high downpayment borrowers and those with low FICOs/low downpayments, in no cases do higher risk borrowers pay lower fees than low risk borrowers. See the chart below from BTIG Research (which, importantly, factors in MI costs):



New GSE LLPAs Combined With Mortgage Insurance Costs

	≤ 30%	30–60%	60–70%	70–75%	75–80%	80–85% (12% MI coverage)	85–90% (25% coverage)	90–95% (30% MI coverage)	> 95% (35% MI coverage)
≥ 780	0.0%	0.0%	0.0%	0.0%	0.1%	0.3%	0.3%	0.4%	0.6%
760–779	0.0%	0.0%	0.0%	0.1%	0.1%	0.3%	0.4%	0.5%	0.6%
740–759	0.0%	0.0%	0.0%	0.1%	0.2%	0.4%	0.5%	0.7%	0.8%
720–739	0.0%	0.0%	0.1%	0.2%	0.3%	0.5%	0.7%	0.8%	1.0%
700–719	0.0%	0.0%	0.1%	0.2%	0.3%	0.6%	0.8%	1.0%	1.2%
680–699	0.0%	0.0%	0.1%	0.2%	0.4%	0.7%	1.0%	1.2%	1.4%
660–679	0.0%	0.0%	0.2%	0.3%	0.4%	0.8%	1.3%	1.6%	1.8%
640–659	0.0%	0.0%	0.2%	0.3%	0.5%	0.9%	1.3%	1.7%	2.0%
< 640	0.0%	0.0%	0.3%	0.4%	0.6%	1.0%	1.5%	1.9%	2.2%

Sources: Urban Institute, BTIG Research. Notes: MI=mortgage insurance. The mortgage insurance data are for borrower-paid mortgage insurance on full-documentation purchase loans for primary residences with fixed or adjustable-interest rates (five years or more) and amortizations of greater than 20 years. This pricing is indicative only, as actual mortgage insurance costs may differ by company, other risk factors, and pricing structures used. Loan-level price adjustments are annualized by dividing by five.

To be clear, there has always been cross-subsidization in federal mortgage insurance and guarantor programs. They are insurance programs at their core, and almost all insurance programs have a measure of cross subsidy. No one wants higher fees in this difficult market at this critical time. MBA and its members both understand and appreciate the concerns that the recent pricing changes represent a "turning" of the cross-subsidy dial, but this is neither new nor precedential.

Variations in GSE Pricing for Third-Party Originated (TPO) Loans

On a separate pricing topic, MBA remains concerned about reports of variations in GSE pricing for loans with substantially similar credit characteristics but a different origination channel – specifically pricing penalties with respect to third party-originated (TPO) loans. At least one of the GSEs is providing less favorable execution and pricing on TPO loans relative to retail loans, solely due to this difference in origination channel. MBA has urged FHFA to take steps to address this issue, as we believe this inappropriate use of pricing creates an unlevel playing field among lenders and harms underserved borrowers.

In order for the GSEs to adhere to their charter requirements that they "promote access to mortgage credit throughout the nation, improve the distribution of investment capital for residential mortgage financing, and provide stability in the secondary market for residential mortgages," they must do everything possible to ensure that lenders of varying sizes, charters, or business models – including those that specialize in different origination channels – have the ability to compete on a level playing field. FHFA appropriately has taken steps to eliminate any preferential pricing or underwriting for certain lenders – first through conservatorship directives and then through amendments to the Senior Preferred Stock Purchase Agreements (PSPAs). Such pricing and underwriting variances were a central feature of the GSEs' flawed pre-conservatorship business models.

The disparities in pricing for TPO loans, however, are a dramatic departure from the core level "playing field" principle FHFA has established. All pricing differences should be based on loan-level factors that influence risk or the GSEs' ability to meet their affordable housing missions. One loan is not riskier than an equivalent loan with identical characteristics simply because it was originated through a third party, nor does that loan do more or less than the equivalent loan to advance the GSEs' missions. The inappropriate use of pricing penalties clearly violates this principle and puts correspondent and wholesale lenders at a disadvantage in the market.

These pricing variations also negatively impact borrowers, particularly those that are critical to the core missions of FHFA and the GSEs. Minority and low- to moderate-income borrowers make up a higher percentage of TPO loans than of retail loans, and the weaker pricing currently offered by at least one GSE flows through to these borrowers, resulting in higher costs for those who obtain TPO loans. FHFA consistently has reiterated its focus on efforts to address our nation's long-standing challenges related to housing equity – particularly with respect to the racial homeownership gap. The current TPO pricing disparities run contrary to this objective and do not further efforts to increase liquidity to support historically underserved borrowers.

For the reasons outlined above, MBA continues to urge FHFA to prohibit the GSEs from varying their pricing solely based on the origination channel of a loan. While the GSEs should be permitted flexibility to adjust their pricing frameworks to meet their mission and safety-and-soundness objectives, they should not be permitted to implement pricing that violates the principle of equal access to the secondary market. Elimination of these problematic pricing variances would benefit both lenders and borrowers, as well as promote FHFA's pursuit of a level playing field in the mortgage market.

Congressional Action: The Need for Broad Reform

In 2008, the financial crisis threatened the viability of the housing finance system, particularly with respect to the central role that the GSEs play in the system. The crisis exposed the fundamental problems in the GSEs' business models, as well as the weaknesses in the regulatory framework that was in place at the time. The result was a breakdown of the secondary mortgage market, $187 billion in taxpayer assistance, and continuing federal support of more than $250 billion.

Nearly fifteen years have passed since the GSEs were placed into government conservatorship, in what was described by then-Treasury Secretary Paulson as a "time out."[2] Despite the intent that conservatorship would serve as a temporary bridge to stabilize the GSEs, the conservatorship persists, and their long-term status remains unresolved.

During that time, the FHFA has begun implementing some of the necessary reforms in its role as conservator of the GSEs. These reforms include secondary market pricing parity across lenders, new mechanisms for credit risk transfer (CRT) to the private sector, an improved infrastructure for the single-family secondary market, a substantial reduction in the retained mortgage portfolios, and support for continued liquidity in the multifamily market.

These reforms, while critical, are not sufficient to fully address the problems that led to conservatorship. Indeed, as the current pricing debate has indicated, broad legislative reforms are still needed — both to bring about the remaining structural changes to the GSEs and to "lock in" the reforms instituted by FHFA through its authorities as conservator.

For example, legislation is necessary to alter the existing GSE charters, clarify the nature of any federal government guarantees, and create permanence for the reforms already undertaken by FHFA. Perhaps most importantly, legislative reform is the only outcome that provides the legitimacy and public confidence necessary for long-term stability in both the primary and secondary mortgage markets.

Conservatorship of the GSEs has already persisted far longer than intended. Congress should not allow conservatorship to continue indefinitely, as market participants will suffer in several ways. Borrowers and renters will be denied the benefits of a more vibrant secondary market, lenders will face increased uncertainty about the future, and private-label security (PLS) issuers and investors will hesitate to fully engage in the market. In short, the status quo is an unacceptable long-term outcome.

Calls to recapitalize the GSEs without further structural reforms are similarly misguided. Under such plans, the post-crisis reforms already achieved could be reversed in the absence of a regulator exerting conservatorship authorities. Recapitalization without corresponding reforms would in many ways remove the existing safeguards that are preventing the GSEs from returning to their flawed pre-crisis business models. Further, an immediate recapitalization is

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[2] "Statement by Secretary Henry M. Paulson, Jr. on Treasury and Federal Housing Finance Agency Action to Protect Financial Markets and Taxpayers," September 7, 2008. Available at: https://www.treasury.gov/press-center/press-releases/Pages/hp1129.aspx.

unnecessary from a safety and soundness perspective, as the ongoing capital support from the U.S. Treasury eliminates any practical near-term threat to the GSEs' solvency.[3] Should either GSE need to draw on this capital support, there would be no change in its existing book of business, day-to-day operations, or prospective ability to provide liquidity to mortgage markets.

Our nation simply should not have a housing finance system that produces suboptimal results due to the limits imposed by conservatorship, nor can we go back to a system that provides private gains when markets are strong yet relies on support from taxpayers when losses occur. Only by enacting comprehensive legislative reform can borrowers, renters, lenders, investors, and taxpayers realize the full benefits of a diverse, competitive primary market and a vibrant, liquid secondary market.

MBA Principles for a Sustainable, More Vibrant Secondary Market

To address the need for reforms, MBA convened its Task Force for a Future Secondary Mortgage Market (Task Force). The "blue ribbon" Task Force, composed of members covering a broad cross-section of the real estate finance industry, developed a comprehensive set of recommendations for an improved secondary market.

The MBA proposal recognizes the need for any comprehensive reform plan to balance three major priorities: 1) taxpayer protection; 2) investor returns; and 3) consumer cost and access to credit. Pushing too far in any one direction may lead to a mortgage market that does not adequately meet the needs of all participants. To achieve the appropriate equilibrium among these priorities, the Task Force developed the following core principles to guide its work. It is against these core principles that MBA evaluates any potential reforms to the housing finance system.

Core Principles:

- Preserve the 30-year, fixed-rate, prepayable single-family mortgage, as well as long-term financing for multifamily mortgages;
- Maintain a deep, liquid to-be-announced (TBA) market for securities backed by conventional single-family loans;
- Attract global capital and preserve liquidity during times of economic stress through an explicit government guarantee for eligible mortgage-backed securities (MBS) collateralized by single-family and multifamily mortgages;
- Limit the explicit government guarantee to the eligible MBS, while prohibiting the extension of the guarantee to institutional debt;
- Require an effective national affordable-housing strategy that helps meet the needs of low-income and underserved households and communities;

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[3] In the 2018 Dodd-Frank Act Stress Test Results, FHFA estimates that, under a severely adverse scenario, the Enterprises would require a combined draw from the U.S. Treasury ranging from $42.1 billion to $77.6 billion. These figures fall far short of the combined $254.1 billion in existing funding commitment from the U.S. Treasury. For more information, see: https://www.fhfa.gov/AboutUs/Reports/ReportDocuments/2018_DFAST_Severely-Adverse-Scenario.pdf.

- Support a competitive and diverse primary market for lenders of all sizes and business models;
- Enable a robust, innovative, and purely private mortgage market to coexist alongside the government-backed market;
- Preserve existing multifamily financing executions and permit new options;
- Establish a strong, transparent regulatory framework that promotes liquidity while protecting the taxpayers;
- Ensure that private capital assumes significant amounts of the credit risk;
- Ensure liquidity in the event of a full-blown systemic crisis; and
- Minimize risks to the liquidity and stability of the mortgage markets during the transition to the end state.

As the GSEs continue through their second decade of government conservatorship, it is critical that policymakers tackle the remaining work of housing finance reform. Access to affordable, sustainable housing is a necessity for all Americans, and as such, it requires a system of financing that is robust in all parts of the country, through all parts of the credit cycle. Legislative reforms of the GSEs, no matter how thorny the journey, offer the best path to reach this desired end state.

Conclusion

MBA continues to urge FHFA to engage with the mortgage industry to improve clarity and transparency regarding the GSEs' pricing framework. We will continue our work with lawmakers, FHFA, the GSEs, and the Biden administration on policies and actions that lower costs and advance sustainable access to homeownership while protecting taxpayers.

More broadly, the housing finance system requires structural reforms that will better ensure a stable, liquid secondary market. Comprehensive legislation remains the best vehicle for such reforms.

Thank you in advance for your consideration of the views expressed within this statement for the record. As always, MBA stands ready to work with members of this Subcommittee (and the full Committee) to ensure a robust housing market that is accessible, affordable, and sustainable – and works to benefit all borrowers, renters, and other critical stakeholders.