Statement of
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Committee on Financial Services
U.S. House of Representatives

"A Legislative Proposal to Protect American Taxpayers and Homeowners by Creating a Sustainable Housing Finance System"

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Chairman Hensarling, Ranking Member Waters, and members of the committee, thank you for the opportunity to testify today on behalf of the Mortgage Bankers Association (MBA). My name is David H. Stevens and I am the President and CEO of MBA. From 2009 to 2011, I served as Assistant Secretary for Housing and FHA Commissioner at the U.S. Department of Housing and Urban Development (HUD). I have over 30 years experience in real estate finance.

The release of the PATH Act represents an important step in defining the boundary of the debate over the government role in housing finance. Fannie Mae and Freddie Mac have been in conservatorship for almost five years now, and it is important that policymakers begin defining a long-term plan for the future role of the federal government in the mortgage market. I compliment Chairman Hensarling for introducing his approach to begin this discussion. MBA also appreciates the Chairman's efforts to tackle other key housing finance concerns in the bill, including the long-term financial viability of the Federal Housing Administration's single-family programs, and welcome many of the much-needed reforms to the Dodd-Frank Wall Street Reform and Consumer Protection Act that are contained in the PATH Act.

We are eager to work with the Chairman, the Ranking Member, and all other members of the House Financial Services Committee to improve the bill in a way that ensures a vibrant housing finance system that works for lenders of all sizes and business models and provides consumers with affordable mortgage financing.

MBA's Goals for Secondary Market Reform

MBA believes that the future secondary market should address the needs of borrowers, lenders, investors, and taxpayers. Private capital should be the first line of defense against losses, with no institution too big to fail. The ideal system should:

- promote liquidity and stability by connecting global pools of capital to the U.S. mortgage market;
- provide certainty in mortgage transactions for all borrowers:
- provide competitive pricing for a consistent offering of core products including the 30-year, fixed-rate, prepayable mortgage and well-underwritten multifamily mortgages;
- provide an efficient means of hedging interest rate risk, i.e., a TBA market; and
- support vibrant, dynamic, and competitive primary and secondary markets composed of lenders with a wide range of sizes and business models, with this competition ultimately benefitting homeowners and the broad owner-occupied and multifamily rental markets.

The government role, to provide quality regulation of guarantors and systems and to provide a clearly defined, but limited, catastrophic credit backstop is an important component of this ideal system. Without this government backstop, the mortgage market would be smaller and mortgage credit would be more expensive, meaning that qualified lower and middle class households would have less access to affordable mortgage credit and be less able to qualify to achieve sustainable homeownership and the multifamily rental market, which predominantly serves those of modest incomes, would be adversely impacted.

It is important to recognize that today's market and MBA's vision of the future secondary market are composed of three segments, ranging from fully private to fully government-insured:

- *A sizeable fully private market that is not limited by loan size or by the Qualified Mortgage (QM) definition.* Fully private loans will still be required to meet the ability to repay standard and all other applicable regulations, and may be held on balance sheets or securitized through non-agency channels. The fully private market will overlap and be competitive with the core market in terms of execution during normal market conditions.
- *A conventional conforming market with a government backstop.* Working class households need access to a market that has private capital taking the first loss, but an ultimate government backstop to ensure ongoing market liquidity. Only traditional, well documented loans that qualify as QMs should be able to enter this core market. This portion of the market should be comprised of originators that bring pools of significantly credit enhanced core mortgages to a central platform for issuance and government reinsurance.
- *A government market.* The FHA/VA/RHS should continue in their present roles performing critical social policy functions. These programs are directly backed by the government and are targeted to support lending to first-time homebuyers and others who could only access homeownership through a low downpayment product. MBA views these programs as critical to the health of the U.S. housing market, but recognizes that certain changes may be necessary to ensure their long-term financial stability.

Market shares among these segments should not be fixed, but should vary over time with economic conditions. The government-backed or supported markets will be countercyclical, increasing in times of market stress, decreasing when credit is widely available.

Why is a government backstop needed for the conventional conforming market?

The American mortgage market has long been dominated by 30-year, fixed-rate, fully amortizing loans, with no penalty for refinancing the loan. The advantage for borrowers is that it protects them against increases in interest rates while providing a long period over which to amortize the loan principal, thus providing more affordable monthly payments than would be available under a shorter amortization schedule.

The advantages for borrowers, however, are offset by the risks posed to depository institutions trying to hold 30-year fixed-rate mortgages in portfolio, given the short duration of most bank deposits and other liabilities. When interest rates rise, banks may end up earning negative spreads on the mortgages they hold. This funding mismatch can be dangerous for financial institutions.

For example, the thrift industry debacle of the 1980s largely grew out of the removal of interest rate ceilings on bank and thrift deposits for many years. The resulting spike in the interest rates on the deposits funding long-term, fixed- rate mortgages essentially wiped out the capital at many thrifts. Similarly, funding mortgages with long-dated fixed-rate deposits can be a problem if rates fall and borrowers exercise their options to refinance their mortgages at lower rates. The bank then faces low or negative interest rate spreads when it reinvests the funds from the paid-off mortgages at lower rates. Thus, relying on bank portfolios to fund 30-year fixed-rate mortgages places tremendous risk on the existing government support of the mortgage market through the FDIC.

Securitization developed as a means of removing this interest rate risk from depository balance sheets, while providing a long-term, fixed-rate asset for investors that had a better capacity to manage such cash flows. However, securitization relies on a steady presence of private investors willing to take on the risks of mortgage-backed securities. We have seen repeatedly over the last twenty years that while investors are generally willing to buy guaranteed MBS, even during a market disruption, they are unwilling to take on uncertain credit risk during these times.

When depositors or security holders become concerned over the health of the assets supporting their investments, they want to liquidate their positions and hold on to their cash until the situation settles. In the case of banks, this is a run on deposits. For securitization, it is a panic sale of the securities with a large drop in price. It is as if bank depositors were forced to sell their deposits to another investor at a deep discount rather than attempting to redeem them at par at the bank. Because those who sell first suffer the smallest losses, there is an advantage to sell quickly before a panic, thus helping fuel a panic. Even if they do not sell, mark-to-market accounting rules do not distinguish between normal price drops and those caused by panic selling, causing large losses for investors

The question is not whether a government guarantee will limit the potential damage of periodic panics in the securities. The benefit is clear. The real question is how to go about limiting the risk to the taxpayers that comes with any sort of government support. Adequate private capital in a first loss position, the establishment of an insurance fund, and a limited, clearly defined credit box (such as has been accomplished with the QM rule) all would be strong steps in this direction.

In summary, the U.S. mortgage market is unique in the degree to which 30-year fixed-rate mortgages play such a large role in financing home purchases. To date, however, that market has been supported by securitization and the implicit and explicit support the taxpayers have given to that market. MBA believes that such a guarantee can be put in place in order to reduce the volatility that would exist in a purely private market, but that would be implemented in such a way as to limit the exposure of the taxpayers.

Getting private capital into the mortgage market: key transition steps that can be taken today

Let me turn now to the current market situation and steps we can take in the short term to move towards a market more in line with these goals.

Fannie Mae and Freddie Mac have recently reported substantial profits, leading some to ask whether the business models of Fannie Mae and Freddie Mac have regained credibility that was lost during the financial crisis. Record GSE profits do not tell the whole story. In their current form, GSE profits are dependent in large part on three factors:

- Guarantee fees, which have more than doubled in recent years.
- Remarkably low- risk business, a sign of tight credit.
- Their ability to shift legacy costs back to lenders

This current status is not sustainable over the longer term, and MBA believes that we should begin moving toward a more sustainable environment. While the legislative process will continue to refine the desired end state, MBA has proposed a set of transition steps designed to move in the direction of the developing consensus regarding the shape of the future secondary market. The steps we propose, none of which require legislation, create an even greater competitive landscape for all originators beyond where we are today, and provide better value to borrowers. Further, they are consistent with the vast majority of end-state proposals.

- FHFA and the GSEs should move to a common, fungible MBS to improve liquidity in the market. The discount on Freddie Mac's security represents a loss to the taxpayer, as it is being implicitly subsidized by lower guarantee fees resulting in lower dividends to the Treasury. We should act now to remove this distortion by moving to a common, fungible security.
- FHFA should mandate that the GSEs accept deeper credit enhancement on pools from lenders in exchange for reduced guarantee fees in order to lower costs and increase access to credit for consumers. The PATH Act includes language to this effect, which we would support as a means of bringing additional private capital into the market. Importantly, we believe that lenders should have "front-end" credit enhancement options in addition to the "back-end" options, as we believe the former have the potential to produce greater cost savings for consumers.
- Regardless of which end state Congress decides upon, we need to ensure that lenders of all sizes have securitization options to directly access the secondary market in order to level the playing field.
- FHFA should impose a well-regulated and fully transparent credit framework with clear representation and warranty protections to increase transparency in the system and enable lenders to responsibly expand access to credit.
- FHFA should continue to seek stakeholder input regarding the Common Securitization Platform to lay the groundwork for a more efficient market in the future. The PATH Act also contains plans for a new market Utility that would perform many of the roles and functions envisioned for the platform, with the exception that the bill would not permit the Utility to securitize government-backed loans. While we appreciate the agreement that such a central, operationally focused utility is needed, we do believe that some level of government backstop is needed for the conventional conforming market.

MBA also supports provisions in the PATH Act that create a framework and regulatory structure for financial institutions to issue covered bonds. Covered bonds are used by financial institutions as a vehicle for attracting private funds to support homeownership, affordable rental housing and commercial real estate.

Adopting covered bond legislation is necessary to provide certainty and clarity with respect to the rights and obligations of parties to covered bond transactions. Covered bonds so far have been limited to large financial institutions, but MBA believes added legal and regulatory certainty would make it cost-effective for smaller ones as well.

Additionally, MBA believes serious consideration should be given to expanding Federal Home Loan Bank membership eligibility to include access for non-depository mortgage lenders. These lenders are often smaller, community-based independent mortgage bankers focused on providing mainstream mortgage products to consumers. In exchange for membership in the FHLB system, these institutions could be required to hold a limited class of stock with appropriate restrictions. Expanding FHLB access to these institutions would enhance market liquidity and ensure a broader range of mortgage options for consumers.

GSE Multifamily Programs

Future of the Multifamily Housing Finance Market

Our views on the multifamily housing finance market run parallel and are consistent with our views on the single-family residential market.

More than one in three American households rent their home, and more than 16 million[1] of those households live in multifamily rental housing, a development with five or more units. Renters include workers who want to live near their jobs, young professionals, empty-nesters, retirees on a fixed income, families with children, students, and households who value the convenience and mobility that renting offers. Notably, the vast majority of multifamily rental housing provides homes for households earning modest incomes, with 93 percent of multifamily rental apartments having rents affordable to households earning at or below the area median income.[2]

Recognizing the unique attributes of the multifamily market as a key component of the broader housing finance system, we believe that policy makers should pursue the following principles in shaping the government's role in the multifamily housing finance system.

Key Principles for Multifamily Housing Finance Reform

First, our nation's housing policies should reflect the importance of multifamily rental housing, the range of capital sources that support this market, and the need for liquidity and stability in all market cycles. The number of renter households in multifamily housing is expected to grow from the current estimate that exceeds 16 million. A broad range of capital sources support the multifamily finance market, including private capital sources. The roles of the GSEs and FHA in financing multifamily mortgages have been substantial, but other market participants – including life insurance companies, banks and other lenders – have maintained a strong presence as well. With respect to the GSEs' multifamily activities, credit performance has been strong during the recent market downturn and, with government support, the GSEs have served a countercyclical role that provided liquidity when private capital sources largely exited the market.

Second, private capital should be the primary source of financing for multifamily housing with a limited, government-backed insurance program ensuring that the market has access to liquidity in all cycles. The risk insurance program would provide support at the mortgage-backed security, rather than at the entity, level. The role of private capital is vital in several respects: (1) the deployment of private capital through market participants that have historically supported multifamily finance, such as portfolio lenders and CMBS investors; (2) the private capital that is already embedded within existing market executions (e.g., DUS, K-Deals) through risk-sharing structures; and (3) the investment of private capital in entities that would be permitted to issue government-backed securities. We believe that a focused role for the federal government through a government-backed risk insurance fund, with a federal catastrophic backstop, would ensure continuous liquidity and stability in all market cycles. Eligible mortgage-backed securities would have a government wrap. The insurance fund, paid for through risk-based premiums, could be modeled after FDIC programs and would support such mortgage-backed securities, not at the level of the issuer, as is the case today.

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[1] 2011 American Housing Survey
[2] Joint Center for Housing Studies tabulations of 2009 American Housing Survey, US Census Bureau.

Third, entities eligible to issue government-backed securities should be funded by private capital, be focused on securitization, serve the workforce rental market, and be regulated in a manner that protects taxpayers and ensures robust competition among capital sources. A strong government regulator with market expertise would provide oversight regarding the issuing entities, including their safety and soundness, risk-based capital requirements, and products offered. The entities, which would not be limited to potential successor entities to the GSEs, also would assume a significant risk position by providing an entity-level buffer, placing private capital at risk ahead of any government backstop. Risk-based premiums would be deposited into a federal insurance fund, to be drawn upon only if and when the entity becomes insolvent. The pricing of the premiums would be structured in a manner that allows robust competition. Importantly, the issuing entities would need to attract private capital and maintain financial viability. We believe, however, that they should be mono-line institutions limited to secondary mortgage market activities and the housing finance sector, with a focus on workforce and affordable rental housing.

Fourth, stewardship of existing GSE assets and resources on behalf of taxpayers should be a core consideration for any action – during the current period of conservatorship, any transition period, and in the future state of multifamily finance. The talent and expertise at the GSEs, their existing books of business, their market executions and any profits generated by their multifamily businesses are valuable to U.S. taxpayers and should be deployed in a manner that supports the future state of multifamily housing finance. Preserving and dedicating such resources would support an orderly transition to a new mortgage finance system and optimize potential returns to taxpayers. Fundamentally, the "do no harm" principle should govern, particularly in light of the stability and successes of the multifamily market overall.

We wish to underscore that as policy makers deliberate the future of the government's role in multifamily housing finance, it is vital they ensure that capital continues to be available to support this essential source of housing.

Federal Housing Administration

Single Family

The PATH Act proposes major changes to the structure and programs of FHA that fundamentally alters the agency's future and its ability to serve American families. MBA appreciates that the legislation recognizes the significance of the FHA to the housing finance system and affirms that FHA should continue to have an important role in providing affordable lending options to first-time and low- and moderate-income homebuyers. The key to a vibrant FHA, however, is to strike the appropriate balance between strengthening the agency's fiscal solvency and maintaining its traditional role as a critical source of affordable credit for first-time homebuyers and working families.

Since the onset of the financial crisis, FHA has taken a series of steps to protect the fiscal health of FHA. It has raised premiums, tightened credit standards, and banned seller-funded downpayment assistance programs from participating in the program. The credit profiles and performances of the FY2010 to 2012 portfolios show these changes are working: the average FHA credit score for FY2011 was 696[3] and the serious delinquency rate was 2.07 percent in the

[3] U.S. Dept. of Housing and Urban Development, Annual Report to Congress Fiscal Year 2012 Financial Status FHA Mutual Mortgage Insurance Fund (November 2012) at p. 18. Can be accessed at: http://portal.hud.gov/hudportal/documents/huddoc?id=F12MMIFundRepCong111612.pdf.

fourth quarter of 2012.[4] The economic value of these books of business is positive three percent compared to the negative seven percent economic value of the 2007-2009 books of business.[5]

MBA applauds the recent actions of FHA Commissioner Carol Galante to address programmatic issues that could continue to damage the Mutual Mortgage Insurance (MMI) Fund, including increasing the annual mortgage insurance premium (MIP), requiring that most loans charge the MIP for the life of the mortgage, requiring that borrowers with credit scores under 620 must be manually underwritten, and consolidating the HECM Fixed Rate Standard Program and the HECM Saver Program. These changes were appropriate and necessary, given that the MMI Fund's capital ratio is well below its two percent statutory requirement. Overall, MBA believes that FHA loans are more appropriately priced and its programs have significantly better risk management policies than they did before the economic crisis.

FHA's market share has declined since the height of the crisis, a trend MBA believes should be encouraged through the re-entry of private capital into the housing market. We have supported policies that are intended to reduce the government's share of the mortgage market – currently at 28 percent and comprised primarily of FHA loans – such as FHA's recent proposal to lower the maximum loan-to-value (LTV) on loans over $625,500 from 96.5 percent to 95 percent. MBA would consider supporting other policy changes and reforms that ensure FHA maintains its focus on serving its targeted population and continues on a path to solvency.

MBA has strong concerns, however, about proposed changes in the PATH Act we believe would have substantial negative consequences for consumers in four key areas: reducing FHA's guarantee, risk-sharing, indemnification, and loan limits.

Reducing the 100 Percent Loan Guarantee

The PATH Act would reduce FHA's mortgage insurance coverage from 100 percent to 50 percent over a period of five years. MBA has serious concerns with the implications of such a significant policy change for the price availability of mortgage credit through the FHA program. Even if it were well constructed, such a change could significantly reduce the number of lenders willing to participate in FHA, given the increased risks to the lender. Such a decrease in competition would necessarily reduce lending and increase costs for consumers.

Mortgage lenders are accustomed to managing representation and warranty risk, but are not structured to take on large amounts of credit risk. If they were forced to take on this risk through a reduction in the coverage of FHA insurance, it could potentially cause them to restrict credit or go out of business.

Lenders who choose to hold FHA loans as investments would also be disadvantaged. Because of the 100 percent guarantee, FHA-insured loans held in lenders' portfolios receive a 20-percent risk weight. Reducing the FHA guarantee could lead to different accounting and bank capital treatment for holding or servicing FHA-insured loans, further impacting the cost and availability of credit to American homebuyers.

[4] Mortgage Bankers Association, National Delinquency Survey 2012 Fourth Quarter.
[5] U.S. Dept. of Housing and Urban Development, Actuarial Review of the Federal Housing Administration Mutual Mortgage Insurance Fund Forward Loans for Fiscal Year 2012 (November 2012) at p. 32-33. Can be accessed at: http://portal.hud.gov/hudportal/documents/huddoc?id=ar2012_forward_loans.pdf.

Finally, decreasing insurance coverage would necessitate that Ginnie Mae increase its guarantee fees. Ginnie Mae relies upon a full credit guarantee from FHA. Reducing FHA's guarantee would simply move risk from one government entity to another.

<u>FHA and Risk-Sharing</u>

Many policymakers and industry participants have suggested the private sector should have a role in sharing risk with the FHA. The PATH Act would establish a risk-sharing pilot program that would give FHA two years to set the parameters of a new program. FHA would then be required to enter into risk-sharing agreements on ten percent of its business.

MBA supports exploring options for FHA to enter into risk-sharing agreements with the private sector as a way of offsetting some of the agency's current risk and reduce the size of the government's footprint, thus strengthening the MMI Fund and better protecting taxpayers. MBA agrees that the option of third-party risk-sharing should be tested before being offered on a wide scale. FHA should have adequate time to construct, test, and revise any risk-sharing policy options via a pilot program and then determine if risk-sharing is appropriate for the agency, lenders and consumers.

MBA recommends that FHA consider scenarios where first-loss private capital is ahead of the government guarantee. The risk-sharing could be at the individual loan level, such as by including private mortgage insurance, or at the pool- or vintage-level. Proponents suggest that risk-sharing not only protects taxpayers, but also could increase the quality of underwriting either by the private mortgage insurers or by lenders who will have an increased incentive to verify the borrower can afford the loan. Others are concerned that private insurers would be able to adversely select FHA, providing insurance only on lower-risk loans, while leaving the government to fully insure higher-risk loans.

Beyond the concerns about adverse selection, the details of any risk-sharing proposal will be critical; it is imperative that any structure not provide an advantage to lenders with certain business models over others. MBA would advocate that any risk-sharing proposal be economically viable for diverse lender business models, particularly community banks and independent mortgage bankers.

<u>Indemnification</u>

MBA has consistently supported high standards for all lenders that participate in FHA programs in order to protect consumers, the agency's fiscal soundness, and the reputation of our industry. MBA members recognize and accept accountability for instances of fraud and negligence within their control. Moreover, lenders take full responsibility for underwriting mistakes that lead to loan delinquencies and incorporate sophisticated quality control systems to minimize the possibility of costly indemnifications.

MBA is pleased to see that the PATH Act contains indemnification provisions that protect consumers while providing lenders with certainty and a mechanism for arbitrating disputes. Under the proposed bill:

- FHA can require a lender to indemnify a loan if a lender *knew or should have known* of a serious and material violation of FHA's mortgage underwriting standards and FHA pays an insurance claim with respect to the mortgage within reasonable period, and the violation was a materially contributing factor to cause the mortgage default.

- A “serious and material violation” is defined as a mortgage loan that should not have been approved and endorsed for insurance.
- For instance of fraud or material misrepresentation, FHA can require a lender to indemnify a loan if a lender knew or should have known of the fraud or material misrepresentation such that the loan should not have been approved and endorsed for FHA insurance, if the fraud or misrepresentation was a material contributing factor to the loan default.

MBA especially appreciates the inclusion of an appeals process that allows lenders the opportunity to present their case against a disputed indemnification determination. In addition to the appeals process, MBA urges the committee to include an arbitration process and a clear limit defining how long after a loan’s origination FHA can require indemnification – not including instances where there is lender fraud or misrepresentation. These changes would help provide assurances to lenders that indemnification requirements would be issued within a reasonable timeframe and that they would be given a fair opportunity to dispute an adverse decision.

MBA , however, strongly opposes Section 264, which requires lenders to automatically repurchase an FHA loan that is more than 60 days past due in the first two years of the mortgage. This inflexible provision fails to take into account the varied reasons why loans default within the first two years, such as job loss, and family death or disability. It also does not address fraud against the lender. Requiring lenders to enter into a binding agreement that includes such a “take-back” requirement as a condition of FHA approval would drastically reduce the number of lenders who offer FHA-insured loans and force lenders to add substantial credit overlays on top of FHA’s requirements.

<u>Loan Limits</u>

Although loan limits are not the major driver of FHA’s market share, they have historically been used as a way of targeting the program to the lower half of the housing market. Congress recognized FHA’s important countercyclical role during the financial crisis and temporarily raised loan limits to mitigate the sharp decline in private capital in the marketplace. Those limits have been extended multiple times and are currently scheduled to expire on December 31, 2013.

Importantly, the most recent extension only applied to FHA loans, which has resulted in an upper limit of $729,750 for FHA and $625,500 for the GSEs. According to MBA data, less than one percent of FHA-insured loans are between $625,500 and $729,750. FHA lending above $625,500 is most prevalent in the following areas: Washington D.C. (12.9 percent); California (3.4 percent); Virginia (3.2 percent); and New York (3.1 percent).[6]

There is evidence that the demand for larger loans is growing and that these borrowers will be adequately served by the private sector. According to MBA’s Weekly Application Survey Data, there was a 22 percent increase in the number of loans between $625,000 and $729,000 from 2011 and 2012. As the demand for this market grows, the private sector will expand its offerings to qualified borrowers.

The PATH Act proposes setting FHA’s maximum loan limits at the lower of 115 percent of the Area Home Price or 150 percent of the GSE single-family loan limit for high cost-areas (maximum of $625,500). MBA believes this change would help sharpen FHA’s focus on serving low-to-moderate income and first-time homebuyers. The expiration of the higher loan limits

[6] Data Compiled from MBA Weekly Application Surveys.

would not greatly affect national FHA lending and would expand the opportunity for private lenders to serve higher-income borrowers.

MBA has concerns, however, that lowering FHA's nationwide "floor" – the loan limit for portions of the country that are not high-cost areas – to $200,000, as proposed in the PATH Act, would have a dramatic impact on the number of borrowers who would be eligible for these loans. Currently, FHA's loan limit for much of the country is $271,050. This includes 1,351 out of 1,376 non-metropolitan counties, 569 out of 582 "micropolitan" areas, and 340 out of 387 metropolitan areas.[7] The average size of an FHA-insured loan in January 2013 was $185,353.[8] Lowering the floor for FHA-insured loans to $200,000 would greatly limit mortgage financing options to the average FHA borrower and could harm the housing recovery in areas of the country where FHA lending is most needed by first-time and low-to-moderate income families. Therefore, MBA supports maintaining the current nationwide floor of $271,050 because it preserves an important credit option for FHA's core constituency and supports the housing recovery.

FHA Multifamily and Healthcare Programs

FHA is an essential source of the long-term, fixed-rate debt needed to build and refinance multifamily rental housing for working families, seniors, and underserved populations, as well as for affordable, quality healthcare facilities. Not only have multifamily and healthcare loans performed well with low default rates, but the programs generate significant revenue to the federal government in the form of a negative credit subsidy.

- *Prevent disruption to the multifamily and healthcare financial markets*. The Multifamily and Healthcare financial markets must remain stable. FHA performs a key function by guaranteeing the loans made by approved lenders, which are then securitized by Ginnie Mae. On June 28, 2013, FHA notified the multifamily industry that it would run out of its FY2013 commitment authority before the end of the current fiscal year. MBA had supported the authorization of an additional $5 billion in FHA FY 2013 commitment authority. FHA multifamily and healthcare programs now face very serious disruptions as loans that could rate lock soon now must wait until October. In a rising interest rate environment, unnecessary costs are added to the operations of these properties for the life of the loan.

- *FHA's multifamily programs are performing well*. In May, 2013, FHA published data that established the positive performance of the multifamily and healthcare loan programs.[9] Through good program design and partnership with mortgage bankers, borrowers and managers, FHA has annual claim rates below one percent in each major program since 2011 on both a loan-count and dollar basis. Despite low claims risk, as demonstrated by HUD's recently published data, the mortgage insurance premiums for most FHA multifamily/healthcare programs rose in FY2013, further strengthening the fiscal soundness of these programs.

[7] U.S. Department of Housing and Urban Development, CHUMS Data Files. Can be accessed at http://www.hud.gov/pub/chums/file_layouts.html.
[8] U.S. Department of Housing and Urban Development, FHA Single-Family Outlook (January 2013). Can be accessed at http://portal.hud.gov/hudportal/documents/huddoc?id=ol0113.pdf.
[9] Federal Housing Administration, Multifamily and Healthcare Claim Rates, FHA Business Trends, May 9, 2013. Can be accessed at: http://portal.hud.gov/hudportal/documents/huddoc?id=mfahcanclarat5-15-13.pdf

- *No need for across the board income limits for renters.* The proposed legislation would require unit level occupancy and rent restrictions on an annual basis in properties with FHA multifamily loans for the life of the mortgage (at Section 237). We respectfully request this provision be removed for the following reasons. The vast majority of all multifamily rental housing serves families earning up to 93 percent of median income, and, in FHA's multifamily portfolio, in particular, nearly half of FHA's approximately 10,000 multifamily loans in portfolio already have affordability provisions.[10] To add annual personal income verification or rent certification where one is not needed for subsidy eligibility purposes adds a significant government reporting burden to individuals and over-reaches the requirements of the Community Reinvestment Act. Such a certification process, even if for only new FHA multifamily mortgages, would add significant and unnecessary costs.

  The variety of loans in the FHA program, originated by nearly 90 FHA lender firms, with funding from private investors, represent a significant, stable source of capital for properties that might not be served by other capital market sources. We therefore believe that it is not necessary to add an income limitation to the FHA multifamily programs because the current program already serves this need. Further, the resource-intense nature of affordable housing production should be balanced with market rate finance activities.

- *Efficiency and markets served.* FHA has restructured its business operations to make them more efficient and currently has a major restructuring effort underway in the Office of Multifamily Housing. According to the FHA Annual Management Report for FY 2012 released by HUD on November 15, 2012, refinances accounted for 73 percent of the FY 2012 FHA multifamily originations, thus stabilizing multifamily housing resources. [11] During the credit crisis, FHA provided stability and liquidity when other capital sources for refinancing evaporated. Most non-FHA multifamily loans have much shorter terms and thus must be refinanced to avoid default at maturity of the loans. Had FHA been blocked from this sector through income limitations, there would have been more devastation in the market. Also, FHA has been able to accommodate much smaller loans than most other capital sources particularly in refinancing existing FHA loans. Meanwhile, FHFA has constrained Fannie Mae and Freddie Mac by reducing their maximum 2013 volumes by 10 percent from their 2012 volumes. There is a volume of non-discretionary loan refinances which must occur in the next couple of years. Such factors are exacerbating stress on rental communities. It is important to maintain FHA as a resource for multifamily and healthcare markets.

- *FHA's Healthcare loan programs are necessary*. More than two thirds of FHA healthcare loans are for nursing homes, including assisted living facilities. Many of FHA's hospital loans are made pursuant to the Critical Access Hospital program which is targeted to rural communities where FHA's program may be the difference in the ability to fund new construction of a clinic or needed wing to an existing medical facility.

[10] Federal Housing Administration communication to Multifamily and Healthcare industry, May 15, 2013

[11] Federal Housing Administration, FHA Annual Management Report, Fiscal Year 2012 (November 2012) at p. 29. Can be accessed at: http://portal.hud.gov/hudportal/documents/huddoc?id=FHAFY12AnnualMgmntRpt.pdf.

Regulatory Relief

The PATH Act contains a number of regulatory relief provisions that will help aid our nation's mortgage markets in their recovery and ensure consumers have access to safe and affordable mortgage credit.

The Ability to Repay rule and Qualified Mortgage (QM)

MBA strongly supports enactment of H.R. 1077, the Consumer Mortgage Choice Act. Introduced by Representative Bill Huizenga (R-MI) and a bipartisan group of eight members of the Financial Services Committee, the legislation would modify the definition of "points and fees" used to determine whether a loan meets the QM test.

The Dodd-Frank Act establishes a Qualified Mortgage (QM) as the primary means for mortgage lenders to satisfy its "ability to repay" requirements. Dodd-Frank also provides that a QM may not have points and fees in excess of 3 percent of the loan amount. As currently defined, "points and fees" include (among other charges): (i) fees paid to affiliated (but not unaffiliated) title companies, (ii) salaries paid to loan originators, (iii) amounts of insurance and taxes held in escrow, (iv) loan level price adjustments, and (v) payments by lenders to correspondent banks, credit unions and mortgage brokers in wholesale transactions.

As a result of this problematic definition, many affiliated loans, particularly those made to low- and moderate-income borrowers, would not qualify as QMs and would be unlikely to be made or would only be available at higher rates due to heightened liability risks. Consumers would lose the ability to choose to take advantage of the convenience and market efficiencies offered by one-stop shopping.

MBA appreciates that the provisions of H.R. 1077 have been incorporated into the PATH Act. We hope the continued bipartisan support for this Dodd-Frank fix leads to its enactment before the Ability to Repay rule takes effect in January of 2014.

MBA also appreciates that the PATH Act delays the implantation of the Ability to Repay rule for an additional year. While our members are moving forward to make the changes necessary to comply in time, we remain concerned about the limited timeframe for complying with what is undoubtedly the most significant mortgage rule in a generation. The complexity of this rule, as well as the many remaining questions for the CFPB, warrants an additional year to ensure a seamless transition and minimal disruptions to the mortgage markets. The additional year will also provide more time for the CFPB to make the necessary changes to the "points and fees" calculation, as discussed above.

Risk Retention

Since the CFPB finalized the QM definition in January, MBA has urged the six federal regulators responsible for drafting the risk retention rules to synchronize the QRM definition with the QM definition.

Creating separate and inconsistent definitions for QM and QRM was always a flaw in the Dodd-Frank Act. Both provisions were intended to promote safer lending and sounder underwriting. And a safe loan for a borrower being a sound investment for an investor, the goals of these two rules naturally align.

While MBA continues to have concerns with the Ability to Repay rule, we would note that the QM designation has eliminated many of the loan-level factors that contributed to the mortgage crisis. Indeed, seasoned loans underwritten to standards similar to QM have performed far better than even traditional prime loans, even during the recent financial crisis. Drafting the QRM exemption more narrowly than QM will further tighten credit for loans nationwide, and eliminate any opportunity for private capital to compete with federally-subsidized, taxpayer-supported loan programs.

MBA has also strongly objected to the proposed premium capture cash reserve account (PCCRA) proposal embedded in the risk retention rule and recommends its elimination. As proposed, we believe that it would be exceedingly disruptive to the CMBS market, and effectively would remove the financial incentive to issue CMBS, possibly eliminating CMBS as a potential source of permanent mortgage capital for commercial/multifamily real estate borrowers.

Because of the harm the PCCRA would do to our nation's commercial real estate markets, and because the QM is a superior construct for defining safer residential mortgage products, MBA believes the Dodd-Frank Act's risk retention requirements have been rendered largely unnecessary and, barring significant improvements in the final rule, would favor their complete elimination.

Eminent Domain

MBA sympathizes with the plight faced by many homeowners across America, especially those in communities hardest hit by the housing crisis. Since 2007, the mortgage industry has completed more than six million permanent loan modifications, including more than one million loans through the Treasury Department's Home Affordable Modification Program. Combined with the more than one million short sales, the total number of permanent, foreclosure-avoiding solutions now stands above 7.2 million.

Recent efforts, however, to use the power of eminent domain as a means to reduce homeowners' monthly payments will only serve to harm our nation's mortgage markets.

MBA is concerned by recent proposals by municipal governments in various parts of the country to use the power of eminent domain to seize the mortgages of underwater homeowners who are current in their payments, reduce the principal to market value, refinance the loan through FHA and resell it to new investors.

This unprecedented use of eminent domain would constrict the availability of mortgage credit, as mortgage investors would likely refuse to purchase mortgages in participating communities due to expected lending losses and collateral risk. As investors withdraw from these markets, fewer creditworthy borrowers would be able to purchase a home, depressing demand below its current levels. The result could be many more homeowners pushed underwater by further declines in home values. Mortgage rates and/or downpayment requirements would rise to compensate for the added eminent domain risk and in turn, price many prospective homebuyers out of the market, particularly in distressed communities.

MBA believes these proposals are not constitutional. Transferring mortgages from their current holders to a privately-owned refinancing entity violates the "public use" requirement for affecting a taking under eminent domain. Moreover, owners of a seized mortgage would not receive the "just compensation" required under eminent domain, since performing mortgages would be revalued at some percentage of the value of the collateral. The proposals likely also violate the Contracts Clause of the Constitution, in that they would substantially impair existing contractual relationships. Finally, the proposals take advantage of the federal government's current refinance programs, and as a result would significantly increase taxpayer exposure. This risk prompted the FHFA to issue a statement on August 9, 2012, expressing "significant concerns" with the proposals and stating that "utilizing eminent domain in this way could undermine and have a chilling effect on the extension of credit" to prospective homeowners.

MBA strongly supports the provisions of the PATH Act that would bar Fannie Mae and Freddie Mac from purchasing or guaranteeing mortgages that are within a jurisdiction that has exercised the power of eminent domain to seize a mortgage loan during the preceding 10 years. We also support the provisions that prohibit FHA from insuring and the U.S. Department of Agriculture's Rural Housing Service from guaranteeing, making, or insuring mortgages that are within a jurisdiction that has exercised the power of eminent domain to seize a mortgage loan during the preceding 10 years.

Basel

Section 401 of the PATH Act would require the Board of Governors of the Federal Reserve, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency to conduct an empirical study of the impact of the final Basel III rules on the financial services sector, the cost to implement the complex rule, change in capital required, the potential of capital volatility, economic growth, and availability of credit to consumers and businesses. The final Basel III rule many not take effect until at least two years after the legislation is enacted.

MBA believes the final Basel III rule approved earlier this month continues to have significant flaws including the harsh treatment of servicing assets and the change in capital requirements for warehouse lines of credit. The treatment of servicing assets will likely drive a large amount servicing assets from depositories to less regulated non-depositories. Removing residential mortgages from the definition of financial collateral will increase the pricing and/or reduce the availability of warehouse funding to independent mortgage bankers who often serve rural and other under-served markets. MBA believes such a study is important and supports the proposed delay in the implementation of the final Basel III rule.

Conclusion

Thank you for the opportunity to testify on the PATH Act. MBA remains committed to its key principle that a successful secondary market should rely primarily on private capital, but will also require a limited, but explicit, government backstop to maintain stable liquidity through all market cycles. We also want to ensure that any changes to FHA ensure this important program remains a vital source of affordable mortgage financing for the targeted populations it was created to serve.

While a good starting point for the debate, we believe key changes will be necessary prior to this legislation being considered by the full House. I want to reiterate that MBA remains eager to work with Chairman Hensarling, Ranking Member Waters, and all other members of the House Financial Services Committee in the coming days to improve the bill in a way that provides consumers with affordable, sustainable mortgage credit and creates a vibrant secondary market that works for lenders of all sizes and business models.