

Future Housing Secondary Market Entities, Their Affordable Housing Responsibility, and the State HFA Opportunity

The National Council of State Housing Agencies (NCSHA) and the state Housing Finance Agencies (HFAs) it represents call on the Administration and the Congress to seize the opportunity of reform to establish a powerful commitment to affordable housing within any future housing Government-Sponsored Enterprises (GSEs) or other secondary market entities. We further appeal to you to direct future GSEs to prioritize the use of the proven HFA delivery system to fulfill this commitment in a safe and sound manner, building upon the highly productive partnerships the existing GSEs and HFAs have formed to expand affordable housing opportunity in this country. NCSHA represents the HFAs of the 50 states, the District of Columbia, New York City, Puerto Rico, and the U.S. Virgin Islands.

NCSHA believes a strong secondary market is an essential component of our country's housing finance system that must be preserved and fortified to ensure the widespread availability of and ready access to mortgage capital. We further contend that federal government support of the secondary market is necessary to ensure the constant and stable flow of capital to all housing markets at all times, including periods of economic downturn.

Federal government support, however, must carry with it an affirmative and commensurate duty on the part of the secondary market—regardless of the number of entities of which it is comprised or their structure—to finance affordable and sustainable homes and to reach underserved people, markets, and needs, including low- and moderate-income people, low-income communities and rural areas, and populations with special needs. These public-purpose obligations should be mandated and enforceable under federal law and regulation and not simply goals to which the entities aspire, without consequence for their failure to achieve them.

The secondary market's relationship with the federal government, the benefits derived from that relationship, and the public-purpose responsibilities those benefits compel must be clearly defined and understood. Secondary market entities must be held accountable for achieving their public purposes and further federal support must be conditioned upon their success in doing so.

Future GSEs must not be structured in a manner that tempts them to trade off their public-purpose responsibilities in favor of generating profit. Their governing bodies should include HFAs and other affordable housing industry representatives that will ensure their public-purpose obligations are met and not subordinated to other GSE interests. A strong, independent regulator should inspire—not impede—safe and sound GSE affordable housing investments.

NCSHA understands that some say future GSEs should not make affordable housing investments, because that is what caused Fannie Mae's and Freddie Mac's financial demise. We disagree. Buying affordable loans did not get Fannie Mae and Freddie Mac into financial trouble. Buying bad loans did.

While it is true that both Fannie Mae and Freddie Mac made investments in subprime, Alt-A, and other nontraditional mortgages that contributed significantly to their financial woes, they also made sound affordable housing investments in partnership with HFAs that have performed exceedingly well. It is also true that the Federal Home Loan Bank (FHLB) system is experiencing financial stress, but FHLB partnerships with HFAs have not contributed to it.

In fact, recognizing the strength and success of HFA lending, Fannie Mae in recent years has entered into several unprecedented, exclusive arrangements with HFAs, offering HFA customers preferred mortgage pricing and terms. Fannie Mae and Freddie Mac have also purchased HFA mortgages because of their high quality, and Fannie Mae regularly points to its HFA “book of business” as significantly outperforming its other mortgages. Several FHLBs have extended HFAs liquidity, lines of credit, and advances on the strength of their loan portfolios.

HFAs have proven over many decades that affordable housing lending done right is good lending. HFAs do it right in the case of first-time homebuyer lending through a time-tested combination of low-cost financing; traditional fixed-rate, long-term products; flexible, but prudent, underwriting with careful credit evaluation; diligent loan documentation and income verification; down payment and closing cost assistance; homeownership counseling; and proactive servicing. They employ the same kind of discipline in their multifamily housing underwriting and asset management.

The Administration and Congress clearly recognized the soundness of the HFA lending model when they entrusted to HFAs in recent years billions in housing recovery resources, on top of the substantial resources they already commit to them annually to create affordable housing opportunity in this country. They understood that HFAs have consistently achieved, in both strong and weak economies, successful and sustainable housing outcomes by combining public purpose and accountability with sophisticated lending practices. They knew HFAs had not and would not engage in subprime or other risky lending.

The Administration and Congress have turned repeatedly to HFAs for help in responding to the housing crisis, committing to them billions in federal resources through the tax-exempt Housing Bond program, the Low Income Housing Tax Credit Assistance and Exchange Programs, the Neighborhood Stabilization Program, and the Emergency Homeowners Loan Program. The Administration further demonstrated its confidence in HFA lending practices with the Treasury Department’s purchase of more than \$15 billion in state HFA Housing Bonds to help overcome the failure of the severely weakened private bond market to purchase Housing Bonds at rates that would allow HFAs to lend the proceeds affordably. Treasury also stood behind outstanding HFA bond issues, providing \$8 billion in liquidity to HFAs. More recently, Treasury has committed billions in TARP funding to HFA foreclosure mitigation efforts through its Hardest-Hit Housing Markets Fund.

NCSHA urges the Administration and Congress to again turn to the time-tested and consistently high-performing HFA delivery system to extend the reach of any future GSEs and to help them substantially achieve their affordable housing mission and mandates. We encourage you to direct GSEs to

prioritize their relationships with HFAs, to work closely with HFAs in the design of their affordable housing programs and products, and to rely upon HFAs to carry out those activities within reasonable flexible parameters that allow HFAs to respond most effectively to the diverse housing and community needs across the country and within their states.

In this reform effort, we caution you against overreacting to the housing crisis in a manner that will deny housing opportunities to deserving people and undermine the housing and economic recovery. We encourage you to require the GSEs to respect HFA expertise and experience by allowing them the flexibility to utilize their proven mortgage underwriting and servicing standards and procedures, which they have employed with great success for decades. We urge you not to impose on the GSEs, or allow them to impose on HFAs, rigid, one-size-fits-all mortgage standards that will severely limit if not shut down their first-time homebuyer lending programs. We appeal to you to strongly resist the suggestion from some to draw a tight mortgage box into which all homebuyers must fit, or you will dash the dream of homeownership for many worthy working families.

Overly prescriptive underwriting standards, for example, could prevent the kinds of high Loan-to-Value (LTV) mortgages HFAs have long made successfully to first-time homebuyers to help them overcome what is often the single greatest barrier they confront to homeownership—the down payment. With the rise of house prices in recent decades, it has become very difficult and sometimes impossible for families with qualifying incomes, strong employment history, good credit scores, and little or no debt, to jump the down payment hurdle. Yet, HFAs find families with this profile are the most likely to sustain homeownership over the long term, even after making no or a small down payment. In fact, HFA loans, most of which are high LTV loans, have historically consistently outperformed conventional market loans, with lower delinquency and default rates.

Even today's more affordable home prices will not eliminate the down payment obstacle for many. However, the high LTV loan products HFAs judiciously offer will allow more families to take advantage of this new affordability, giving a much-needed boost to both the first-time homebuyer and trade-up markets.

While it is important that GSE affordable housing programs and products support and complement federal housing assistance programs, it is also critical to keep in mind that income eligibility and other rules vary across federal housing programs and when applied in some markets, deny assistance to people with housing needs not being met by the private market. For example, in some especially low-income rural areas, a two minimum wage earner family's income exceeds the Housing Credit income limit but is insufficient to support a market-rate rent. We urge you to design sufficient flexibility into the GSEs' affordable housing mandates to allow HFAs to use the whole range of federal housing tools available to them in combination with GSE products and programs and to also respond to affordable housing needs not being met by such programs or the private market.

In addition, we urge you to ensure that GSEs partner with HFAs in meaningful and innovative ways that complement, augment, and expand HFA financing and development activities, rather than

compete or work at cross-purposes with them. To accomplish this, it is imperative that the GSEs work with HFAs to design a full array of financing tools, as affordable housing finance is complex and requires multiple executions.

NCSHA feels strongly that effective fulfillment of their public purpose mandates will require future GSEs to integrate wholly within their business cultures and throughout their operations a dedication to affordable housing and underserved market financing. These activities should be pursued by these entities broadly and consistently, not as side or niche businesses. The GSEs must fully devote themselves, across all of their business lines, to bringing about affordable and sustainable housing outcomes, especially in areas where market forces fail.

Though important and welcomed activities, the capitalization of housing trust funds, grant-making, and charitable giving should not alone fulfill these entities' public-purpose responsibilities. Not only would these activities be subject to the vagaries of congressional action and other uncertainties, they would also not have nearly the impact of a national secondary market system designed to support affordable housing finance in a myriad of ways.

The GSEs should make low-cost capital available to support a broad range of affordable housing financing needs, including affordable homeownership lending; rental housing development; predevelopment, site acquisition, and construction lending; subordinate lending; small property financing; and mixed-income and mixed-use financing. They should provide support in a variety of ways, including through the purchase and securitization of mortgages, lines of credit, and bond and loan guarantees, all with reasonable rates and terms. They should invest in the Housing Credit and Housing Bonds to stabilize and improve pricing in those markets and refrain from selling such investments in a manner that will have destabilizing effects on those markets.

It is critical that the GSEs be given broad authority and flexibility, within prudent standards of safety and soundness, to practice innovation in carrying out a wide array of affordable housing and underserved market strategies, which may include subsidizing lending for these purposes. These entities must be able to respond quickly and nimbly to changing housing markets and conditions and to take measured risks.

Finally, we want to stress that HFAs should play a key role in the strong governance of the GSEs. We suggest HFAs be at the regulatory table, not only to help ensure that these entities meet their affordable housing mandates, but also to inform those efforts and evaluate their success.

Why Should HFAs Be the GSEs' Preferred Affordable Housing Partner?

State HFAs play an indispensable role in the provision of affordable housing in our country today. They bring statewide perspective and focus, along with a deep understanding of the needs of their local markets. They are in an unparalleled position to ensure that resources are integrated with other public investments in our physical, economic, and human infrastructure.

HFAs combine tough business acumen with a mission-oriented public purpose to harness private capital to provide affordable housing. They possess sophisticated financing, underwriting, and asset management capacity and a multi-decade record of responsibility, effectiveness, accountability, and success in administering tens of billions of dollars of federal housing assistance.

In strong and weak economies, HFAs have been a constant, reliable source of flexible, affordable mortgage money for lower-income first-time home buyers, anchoring the first-time home buyer market. HFA loan performance is strong, with delinquency and foreclosure rates well below those in the conventional market, even in today's troubled economy.

HFAs never turned to subprime mortgage products, offering largely 30-year, fixed-rate mortgages. Through a combination of low-cost financing, prudent underwriting, home buyer counseling, down payment assistance, and aggressive servicing, HFAs have proven over many decades that homeownership is not only possible for lower-income families, it is sustainable.

Using single-family Housing Bonds or, as they are commonly known, Mortgage Revenue Bonds (MRBs), HFAs have made nearly 3 million families first-time homeowners. They add another 100,000 families to their ranks each year.

Recognizing that not everyone is ready for or interested in homeownership, HFAs and their partners have produced more than 2 million affordable rental homes with equity provided by the Housing Credit. Nearly half of these homes are multifamily Housing Bond-financed. HFAs have financed nearly another 1 million affordable rental homes with Housing Bonds alone. Using Housing Bonds and the Credit, HFAs add another 150,000 homes to our country's affordable rental housing inventory each year.

HFAs engage in a broad range of other affordable housing activities, including home rehabilitation and weatherization, rental housing preservation, tenant rental assistance, housing for the elderly and persons with special needs, and homelessness assistance.

What Are State HFAs?

HFAs are state-chartered housing agencies that operate in every state, the District of Columbia, New York City, Puerto Rico, and the U.S. Virgin Islands. Though they vary widely in their characteristics,

including their relationship to state government, HFAs have in common their public-purpose mission to provide affordable housing to the people of their states who need it.

What Is NCSHA?

NCSHA is a national nonprofit, nonpartisan Washington, DC-based association that represents the interests of state HFAs before the Administration and the Congress. In addition to its policy and advocacy work, NCSHA provides HFAs education and training and facilitates best practice exchange among them.