MEMORANDUM

September 6, 2019

TO: HFA Executive Directors
FR: Garth Rieman and Greg Zagorski
RE: Treasury, HUD Housing Finance Reform Proposals

Executive Summary

The U.S. Treasury Department and the Department of Housing and Urban Development (HUD) late yesterday sent to President Trump their respective proposals for reforming the housing finance system. Both plans, which respond to an executive memorandum issued by Trump in March, include a mix of legislative and administrative proposals for reform. This memorandum summarizes the plans and highlights key aspects of them. We are still assessing their potential impact on HFAs and how NCSHA will comment and respond in our advocacy activities.

Treasury's plan focuses on removing the government-sponsored enterprises (GSEs) Fannie Mae and Freddie Mac from conservatorship and establishing a new competitive secondary housing finance market. HUD's plan outlines potential changes to the Federal Housing Administration (FHA) and Ginnie Mae that HUD says will ensure the agencies responsibly meet their affordable housing missions. Included in HUD's plan are several proposals pertaining to down payment assistance provided with FHA-insured mortgages.

Combined, the plans include 116 different proposed policy changes (49 from Treasury, 67 from HUD). Many of the plans' more substantial provisions would have to be enacted by Congress, which appears unlikely this Congress. While there are many noteworthy changes the Administration believes could be enacted administratively by either FHA or the Federal Housing Finance Agency (FHFA), the plan does not specify if and when these agencies intend to carry out these proposals.

Ending Conservatorships and Establishing Private Guarantors

The crux of Treasury's proposal is similar to several plans advanced by lawmakers and outside experts in recent years. Fannie Mae and Freddie Mac would each be removed from conservatorship and become mortgage guarantors in the private sector. Fannie Mae, Freddie Mac, and any other private entity guarantors wishing to would then apply to the FHFA to purchase government insurance for qualified mortgage-backed securities (MBS) from Ginnie Mae. The

Ginnie Mae insurance would be largely the same as the insurance it currently provides on MBS composed of federal program loans. Treasury recommends that FHFA and Ginnie Mae identify what changes are necessary to enable Ginnie Mae to take on this role.

FHFA would regulate the guarantors, including chartering new guarantors, setting capital and liquidity standards, and approving pricing. Guarantors would be required to provide equal access to all originators, regardless of their size or loan volume, and would have to operate cash windows via which lenders could sell them individual loans that the guarantors would then securitize. They would be expected to operate as monoline insurers, and their business activities would be strongly restricted by Congress. Further, guarantors would have to offset some of the risk associated with the loans they guarantee through credit risk transfers in order to purchase the government guarantee.

While Treasury makes it clear it would prefer Congress act to pass reform legislation, it recommends that, pending legislation, FHFA take several steps unilaterally to better prepare the GSEs to be spun off from conservatorship. These include requiring the GSEs to build up additional capital and reviewing whether Fannie Mae and Freddie Mac should continue to guarantee certain loan products, including cash-out refinancings, higher principal balance loans, and loans for investment properties.

The plan also recommends FHFA and HUD evaluate the appropriate roles and overlap between GSE and FHA activities, including with respect to high loan-to-value (LTV) ratio lending and high debt-to-income (DTI) ratio lending, which would include eliminating the "QM Patch" that allows the GSEs to purchase high-DTI loans.

The plan also calls for Treasury to maintain its current commitment to backstop the GSEs' single-family and multifamily MBS until legislation is passed.

Support for Affordable Housing

The Treasury plan urges Congress to rescind Fannie Mae and Freddie Mac's affordable housing goals, which it argues are inefficient, lack transparency, and cause the GSEs to engage in risky lending. In their place, Treasury proposes the GSEs pay an assessment that Congress would appropriate to support HUD-administered multifamily and single-family affordable housing programs. In the absence of legislation, Treasury suggests that FHFA examine how the GSEs can more efficiently meet the housing goals.

Treasury does not propose any changes to the GSEs' Duty-to-Serve requirements or their contributions to the Housing Trust Fund and Capital Magnet Fund.

GSE Role in Multifamily Market

Treasury's report expresses concern about Fannie Mae and Freddie Mac's increased role in the multifamily mortgage market, which it says departs from the GSEs' primary purpose to support financing for rental housing affordable to low- and moderate-income families. The plan calls on Congress to limit eligibility for the government guarantee to MBS composed of affordable multifamily loans. It also suggests FHFA explore how it can further restrict Fannie Mae's and Freddie Mac's multifamily activities.

The report further suggests that FHFA consider reviewing the GSEs' multifamily lending underwriting criteria for properties located in jurisdictions that have adopted rent control laws.

HUD to Examine Pricing for Down Payment Assistance Loans

In its report, HUD notes that an increasing share of FHA borrowers are receiving down payment assistance. As it has previously, HUD says that loans with down payment assistance, including those provided through government programs, have demonstrated worse performance than FHA's portfolio as a whole and could pose a threat to the health of FHA's Mutual Mortgage Insurance Fund.

To address this issue, HUD recommends that FHA examine whether the premiums FHA charges for loans with down payment assistance adequately reflect the risks such loans pose. Further, it suggests that FHA establish a Homebuyer Sustainability Scorecard to measure the performance of FHA loans with various features, including DPA, and use such data to establish a tiered premium structure that would base a borrower's insurance premiums on their perceived risk. Finally, it proposes that FHA issue a rule clarifying the statutory prohibition on DPA providers that financially benefit from a transaction.

Other notable provisions of HUD's plan include:

- Restructuring FHA as an autonomous corporation within HUD;
- Lifting the 455,000-unit cap on the Rental Assistance Demonstration program;
- Separating the mortgage insurance function from rental subsidy administration within FHA; and
- Taking further action to clarify lenders' compliance obligations under FHA.

The Senate Banking Committee has scheduled a hearing for Tuesday, September 10, at 10:00 a.m. ET to examine the Administration's proposals. Treasury Secretary Steve Mnuchin, HUD Secretary Ben Carson, and FHFA Director Mark Calabria will all testify.

NCSHA will continue to examine both plans in more detail to determine how they will impact HFAs and affordable housing lending. Please reach out to us with any questions or comments you might have.