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HOUSING FINANCE REFORM: ESSENTIAL ELEMENTS TO PROVIDE AFFORDABLE OPTIONS FOR HOUSING

HEARING

BEFORE THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE

ONE HUNDRED THIRTEENTH CONGRESS

FIRST SESSION

ON

EXAMINING RECOMMENDATIONS TO PROVIDE AFFORDABLE OPTIONS FOR HOME OWNERSHIP AND RENTAL HOUSING, AFFORDABLE MORTGAGE CREDIT IN RURAL AND UNDERSERVED COMMUNITIES, AND SOLUTIONS TO ADDRESSING THE COST BURDENS FACING MANY RENTERS

NOVEMBER 7, 2013

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C O N T E N T S

THURSDAY, NOVEMBER 7, 2013

WITNESSES

HOUSING FINANCE REFORM: ESSENTIAL ELEMENTS TO PROVIDE AFFORDABLE OPTIONS FOR HOUSING

THURSDAY, NOVEMBER 7, 2013

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
Washington, DC.

The Committee met at 10:04 a.m., in room SD–538, Dirksen Senate Office Building, Hon. Tim Johnson, Chairman of the Committee, presiding.

OPENING STATEMENT OF CHAIRMAN TIM JOHNSON

Chairman JOHNSON. I call this hearing to order.

Today with the help of our witnesses, the Committee will examine the importance of affordability in the housing finance system for both homeowners and renters. It is imperative that any new system meets the housing needs for all Americans, and this morning, we will explore the well-functioning elements of the current system that should be maintained to provide renters, low- and moderate-income families, and those who live in rural areas affordable options for housing.

Currently, Fannie Mae and Freddie Mac support affordable financing for multifamily lending and, prior to being placed in conservatorship, were authorized to provide funding for the Housing Trust Fund and Capital Magnet Fund to further target support for affordable housing to those families that need it most.

In addition, Fannie Mae and Freddie Mac's mission is to ensure a liquid market and stable access to mortgage credit in all communities, including rural and underserved markets. This mission cannot be scrapped in a new system.

As we consider winding down Fannie Mae and Freddie Mac and transitioning to a new structure, we must consider what worked and what did not work in the old system, and how the roles currently filled by the GSEs will be replaced in a new system.

While those who are opposed to the GSE's affordable housing goals often link the goals—last increased for the single-family market by the Bush administration in 2004—to the problems experienced in the housing market, even Dr. Holtz-Eakin's dissenting view in the Financial Crisis Inquiry Commission report found that the problems were complicated rather than solely focused on the GSEs.

And research conducted by the St. Louis Federal Reserve Bank determined that the affordable housing goals were not the cause of this subprime mortgage boom.

According to a recent report by the Harvard Joint Center for Housing Studies, home ownership is at its lowest level since 1976 for those ages 25 to 54. The statistics are equally troubling for affordable rental properties. As the home ownership rate decreased during the crisis, the demand for the rental stock exceeded the supply and the number of rent-burdened families increased as the supply of vacant rental housing declined to the lowest percentage since 2001.

Without a new system that includes a duty to serve all areas of the country, I am concerned that these levels could fall further and at the expense of rural and traditionally underserved markets like those in my home State.

I look forward to hearing our witnesses' recommendations to maintain and increase access to housing options that are affordable, and to ensure that all communities are served by any new secondary market structure.

Now I turn to Senator Crapo for his opening statement.

STATEMENT OF SENATOR MIKE CRAPO

Senator CRAPO. Thank you, Mr. Chairman.

Today we continue our important work examining essential elements of the housing finance system. I want to thank our witnesses for appearing today to present your thoughts on this important topic. For millions of Americans across the country, home ownership provides a source of security and a sign of responsibility.

There are undeniable benefits derived from home ownership for both the families who buy and the broader community as long as the purchase of that home is achieved through responsible, sustainable means. Five years after the financial crisis, affordability is still a major concern for prospective homeowners. As we address this important issue, we must not return to the flawed politics of the past.

Several prominent economists have criticized the affordable housing policies of the 1990s and the early 2000s as a significant contributor to the financial crisis. They argue mandatory affordable housing goals forced Fannie Mae and Freddie Mac to lower underwriting standards, reach into the subprime market, and ultimately take on more unsustainable risk.

During the height of the housing bubble, Fannie and Freddie began acting like highly leveraged hedge funds, purchasing as investments nearly 40 percent of the private label subprime securities. These combined actions harmed borrowers, homeowners, and taxpayers through the creation of unsustainable mortgages.

S.1217 aims to strike a delicate balance between making homes more affordable and protecting the American taxpayer. In exchange for a repeal of the flawed affordable housing goals the Government-sponsored enterprises were previously required to meet, the new framework would provide funding to expand access to affordable home ownership and rental housing.

Funds would be allocated to two existing programs, the National Housing Trust Fund and the Capital Magnet Fund. These funds would provide grants and other aid for States, housing entities, and other nonprofits to ensure broad access to affordable housing options.

I have heard a lot of positive feedback about the benefits of localized affordable housing policy and how it can provide more flexibility for tailored approaches. However, this new model still raises many questions. First, how would these funds interact with the myriad of other Federal affordable housing options already offered through HUD, Federal home loan banks, the USDA, and certain tax incentives?

According to a recent Government Accountability Office report, Federal housing assistance is fragmented across 20 different entities administering 160 programs, receiving tens of billions of dollars each year in Federal funding. The GAO report recommends several actions that can be taken to eliminate duplication and increase efficiency among these programs.

Second, is the five to ten basis point charge on guaranteed securities envisioned in S.1217 appropriate to capitalize these funds? Using today's secondary market size, many estimate that these funds would receive $2.5 billion to $5 billion per year in funding. To put that in perspective, the allocation to these funds would be roughly 10 percent the size of HUD's fiscal year 2012 budget.

How do we make sure that the funds are accountable and transparent to the American taxpayers and Congress? As we debate ways to increase affordability, it is imperative that we strive to make our policies responsible, accountable, and efficient.

We have an opportunity to achieve much needed reform in our housing finance system. In doing so, we must find a way to promote responsible housing policies without placing the American taxpayer at risk. The American taxpayer cannot be exposed to another GSE-like bailout as a result of deeply flawed policies.

Thank you, Mr. Chairman.

Chairman JOHNSON. Thank you, Senator Crapo.

Are there any other Members who would like to give a brief opening statement? If not, I would like to remind my colleagues that the record will be open for the next 7 days for additional statements and other materials. Before we begin, I would like to introduce our witnesses that are here with us today.

First, Mr. Hilary O. Shelton is the Washington Bureau Director and Senior Vice President for Policy and Advocacy at NAACP. Mr. Rick Judson is the current Chairman of the National Association of Home Builders, as well as a home builder from North Carolina. Dr. Sheila Crowley is the President and CEO of the National Low Income Housing Coalition.

Dr. Douglas Holtz-Eakin is the President of the American Action Forum. And finally, we have Mr. Ethan Handelman, Vice President for Policy and Advocacy at the National Housing Conference. We welcome all of you here today and thank you for your time.

Mr. Shelton, you may proceed with your testimony.

STATEMENT OF HILARY O. SHELTON, WASHINGTON BUREAU DIRECTOR AND SENIOR VICE PRESIDENT FOR POLICY AND ADVOCACY, NAACP

Mr. SHELTON. Thank you very much and good morning. Good morning, Senators Crapo, Johnson, esteemed members of this panel. My name is Hilary Shelton. I am Director of the NAACP's Washington Bureau, the legislative and public policy arm of our Nation's oldest and largest grassroots-based civil rights organization.

Owning a home remains the American dream. For many, it represents a degree of financial success as well as an opportunity to build and retain wealth. Our Nation, our communities, and our people all benefit from safe, affordable, secure housing, whether it be through home ownership or rental housing.

Furthermore, it has been established that housing markets currently generate more than $10 trillion per year in domestic economic activity. Yet, the communities served and represented by the NAACP have long been underserved by the housing market. We were, for decades, targeted by predatory lenders and, as a result, have been denied the opportunity to build wealth through housing.

Furthermore, many of our communities, in fact, a disproportionate number of communities of color continue to suffer from the foreclosure prices and continue to be neglected by too many mainstream financial institutions.

As Congress considers and debates the future of the housing market and the role to be played by the Federal Government, I cannot stress enough how important it is that any future housing finance system must affirmatively establish pathways to sustainable and affordable home ownership for a wide range of qualified buyers.

We must also make sure that any genuine reform of the secondary market will assure an adequate supply of safe and affordable rental homes. A 2008 burst of the housing bubble had repercussions which are still being felt today, especially in communities of color across the United States. An estimated 4.5 million homes have been foreclosed upon since the crisis began, and many more are still at risk of foreclosure.

Due largely to the targeted predatory lenders which have been going on for years in the communities of color, the rate of foreclosures is currently twice as high for borrowers of color when compared to white borrowers. In addition to the households actually facing prospects of foreclosure, the crisis has also impacted homeowners who live in neighborhoods with high levels of foreclosures, and again, racial and ethnic minority communities are disproportionately affected.

One study estimated that racial and ethnic minority neighborhoods will lose $1 trillion in home equity because of the impact that homes going through foreclosure process has had on overall neighborhood property values, fully half of all overall national total.

In my written testimony, I cite several studies which demonstrate that although mortgages made to low-income and racial and ethnic minority Americans were disproportionately predatory subprime loans, neither the borrowers nor the affordable housing goals, which many claim led to the—been extended the loans in the first place were not at fault for the 2008 housing crisis.

Nor was the housing crisis caused by compliance with the Community Reinvestment Act, as some of have tried to claim. In fact, studies show that loans made to low wealth homeowners as part of the banks' efforts to meet their CRA obligations have actually performed better than the rest of the subprime market.

Rather, the source of too many of our economic woes was the desire of Fannie Mae and Freddie Mac to make money for their private stakeholders and the willingness of the private label market to accommodate their desires.

Chairman Johnson, Members of the Committee, I do not need to tell you that the Americans' housing market is incredibly complicated and complex. Its needs and fortunes vary from region to region, income to income, and year to year. Nobody, including me, has all the answers of reform under the current system.

Yet, I do know that if we take steps to reform the housing market, we must do all that we can to ensure that every American has access to safe, affordable, sustainable housing. For low-income Americans, this means that we must ensure that there is an adequate stock of safe and affordable rental units throughout the country, and for qualified middle income Americans, this means that we must make sure that sustainable, affordable mortgages are available.

And the housing finance system must affirmatively establish affordable, sustainable pathways to home ownership for all qualified buyers. Ensuring that all Americans have access to fair and sustainable credit opportunities is crucial to a sustained economic recovery. The Federal Government is obligated to promote nondiscrimination, residential integration, and equal access to the benefits of decent and safe housing and ownership opportunities.

Therefore, any reform of the secondary market must require all lenders and scrutinizers receiving a guarantee of any kind to affirmatively market or offer credit in the manner that promotes equal opportunity in all neighborhoods.

Furthermore, without a duty to serve all communities, as is indicated by the Community Reinvestment Act, private capital will gravitate to the elite home buyers, those with traditional borrowing profiles, while middle class and first time home buyers, as well as purchasers of color, will be left without. This will result in the exacerbation of an unsustainable housing finance market in which qualified, but lower wealth and lower income buyers, especially minorities, will be underserved.

Sadly, this trend is already evident. The private market overwhelming caters to traditional borrowers in well-served locations, a fact that harms both borrowers and minority communities and whole housing sectors.

Let me wrap up by saying that the NAACP does not agree with any provisions in legislation proposed by—some of the provisions, not every provision, in legislation proposed by Senators Corker and Warner, especially provisions which would negatively and disproportionately affect racial and ethnic minorities, including the mandated 5-percent downpayment, and we will be quick to point out areas in which the proposed legislation is lacking.

We do congratulate them for moving the debate forward, however. Likewise, we are strongly encouraged by these hearings being held by Chairman Johnson and Ranking Member Crapo intended to look into the necessary elements of GSE reform. Members of this esteemed panel, I look forward to your questions and the ensuing debate regarding GSE reform, and to working with you to ensure that any reform will benefit all home buyers, renters, and our Nation as a whole.

I thank you very much for holding this hearing and look forward to your questions.

Chairman JOHNSON. Thank you. Mr. Judson, you may proceed.

STATEMENT OF RICK JUDSON, CHAIRMAN, NATIONAL ASSOCIATION OF HOME BUILDERS

Mr. JUDSON. Chairman Johnson, Ranking Member Crapo, and Members of the Committee, thank you for the opportunity to testify today. My name is Rick Judson. I am a builder/developer from Charlotte, North Carolina, and the Chairman of the Board of the National Association of Home Builders.

NAHB believes that an effective housing finance system must address liquidity as well as affordability. It is essential that the housing credit is consistently available on affordable terms regardless of domestic and international economic and financial conditions.

The U.S. housing finance system must be multifaceted, including private, Federal, and State sources of housing capital. To achieve this, it is important to reform and restructure the conventional mortgage market, but also to improve other parts of the housing finance system, including reform of the appraisal process.

We urge Congress to move comprehensive housing finance reform legislation that contains elements that contribute to affordability and availability of safe and soundly underwritten loans. Most importantly, to maintain affordable mortgage credit, NAHB believes strongly that a Federal backstop is needed to ensure the continued availability of mortgage credit, specifically, 30-year fixed-rate mortgages and reliable mortgage financing for multifamily rental housing.

The key to the sustainability of the 30-year fixed-rate mortgage is securitization outlet, because originators simply do not have the sufficient capacity to hold for such long-term assets. There are serious doubts as to whether a private housing finance system would be capable of supporting this type of product without some sort of Government guarantee.

At a minimum, the cost and terms of a 30-year fixed-rate mortgage would be significantly less favorable in a totally private system and fewer families would be eligible for such mortgages. NAHB believes that S.1217, the Housing Finance Reform and Taxpayer Protection Act introduced by Senators Corker and Warner, represents an important bipartisan step in the debate on housing.

NAHB believes that the—in particular, we support modifications to the Corker-Warner bill that would make the National Housing Trust Fund accessible. The future housing finance system must be viewed as more than a private conventional market. The array of Federal and State government programs that have been developed over the years are still essential elements of an affordable housing option.

FHA single family mortgage programs are unique and a vital component of the housing finance system. FHA is critical to providing home ownership opportunities, especially for first time home buyers, minorities, and those with limited downpayment capabilities. Similarly, FHA has historically played an important role in financing multifamily rental housing.

For our Nation's rural areas, programs operated by the USDA's Rural Housing Service have played an important role in providing mortgage credit in underserved areas. The VA Home Loan Guarantee Program is an integral component of housing finance for our Nation's service members, providing an outstanding example of how low to no downpayment programs can perform even in a difficult economic environment if they are properly underwritten.

Finally, builders continue to have a very difficult time accessing production credit from the traditional financial institutions. NAHB greatly appreciates the efforts of Senators Menendez and Isakson for introducing legislation, S.1002, that addresses several regulatory barriers currently inhibiting access to construction credit.

We hope this Committee will consider this legislation and other regulatory barriers to both construction and the broader, small business credit. NAHB looks forward to working with the Chairman and Ranking Member, and all Members of the Committee, to achieve comprehensive housing reform finance that maintains a proper level of Federal support necessary to provide the much-needed, long-term stability for this critical section of our economy.

Thank you for the opportunity to testify today.

Chairman JOHNSON. Thank you. Dr. Crowley, you may proceed.

STATEMENT OF SHEILA CROWLEY, PRESIDENT AND CEO, NATIONAL LOW INCOME HOUSING COALITION

Ms. CROWLEY. Chairman Johnson and Ranking Member Crapo and Members of the Committee, thank you so much for inviting me to testify today.

This Committee's extensive work that you are engaged in housing finance reform is focused on how mortgage financing should be structured and what role the Federal Government should play. The reason that the Federal Government should be involved at all is to make sure that the housing sector works for everyone, not just for the most fortunate.

I am here today to ask that you make sure that the least fortunate are included in your legislation, people for whom the housing market does not work at all and who cannot be reached through the existing low-income housing programs because the need far exceeds the resources.

To do so, I ask that you protect and fund the National Housing Trust Fund. We have led the National Housing Trust Fund campaign since the year 2000. This includes some 7,000 organizations in every Congressional district across the country. We celebrated when the Trust Fund was created in 2008 in the Housing and Economic Recovery Act, HERA.

We are very grateful to Senator Reed for his authorship of the Housing Trust Fund provisions in HERA, and to Senators Shelby, Crapo, Corker, Johnson, Schumer, Menendez, Brown, Tester, and Warner for supporting the Housing Trust Fund in 2008. We are also grateful to Senators Corker and Warner and the other cosponsors for including the Housing Trust Fund in S.1217.

All housing markets are local, but there is no community in our country that has a sufficient supply of decent rental homes that are affordable to extremely low-income families. In South Dakota, that is $18,784 a year. In Idaho, it is $16,932 a year, or less. These are people who labor in the low wage workforce and people who are elderly and disabled with incomes primarily from SSI.

There are 10.1 million extremely low-income renter households in the United States and only 5.5 million units renting at prices they can afford. It is the only income group for whom there is a shortage of homes. Nationwide, there are just 30 homes that are available and affordable for every 100 extremely low-income renter households.

And moreover, the shortage gets worse every year. HUD reports that the number of worst case housing needs increased by 43 percent between 2007 and 2011. That is why 6,500 people showed up last week when the East Providence Housing Authority, which only administers 330 vouchers and has none to give out right now, opened up its voucher waiting list to people who came the night before to camp out to be able to just put their names on a list.

These are data about families who have to choose between food or heat, coats or medicine, and get behind on their rent and lose their homes anyway. They move in with others or they sleep in cars. Next time you are at home ask a local principal about how many homeless children there are in their schools. We have 1.1 million homeless children enrolled in public schools in the United States now.

And though we have made progress in reducing the number of veterans and people with chronic illnesses who are homeless, there has been an explosion in the number of homeless families with children. There are over 20,000 homeless children in New York City alone.

The purpose of the National Housing Trust Fund is to end this housing shortage. The market will not do it on its own. The cost of building and operating rental housing is more than poor families can afford to pay in rent.

There would be no need for the National Housing Trust Fund—and let me be clear about this—if existing Federal housing programs were sufficiently funded and properly structured. But there is no existing Federal housing program that produces rental homes targeted specifically for extremely low-income households, and more critical, current programs are grossly underfunded.

HUD rent assistance only reaches 25 percent of the eligible population. All the HUD programs that serve low income people are part of domestic discretionary spending and are subject to sequestration. We estimate that 185,000 vouchers will be lost by the end of next year under sequestration. Given the constraints on appropriations today, it is inconceivable that the existing HUD programs will ever be enough.

We estimate that it would cost $30 billion a year for 10 years, that is $300 billion, to close this gap. That is why we need a National Housing Trust Fund, to produce, preserve, rehabilitate, and operate rental homes that these families can afford. It is modeled after housing trust funds created at the State and local level over the past 30 years. Those that are the most successful have robust, dedicated sources of funding.

The National Housing Trust Fund is supposed to be funded with a dedicated source of funding, and as you know, the initial source provided in HERA was an assessment on Fannie and Freddie. The statute also says that the Trust Fund can be funded by any other amounts that Congress may direct toward it.

Fannie and Freddie were taken into conservatorship soon after HERA was enacted. The conservator suspended their obligation. The story is well-known. We think that now that Fannie and Freddie are profitable again, that the suspension should be lifted. Given the current dire circumstances of so many poor Americans, it would be a Godsend if the conservator agreed with us, but unfortunately, he does not.

Our specific requests related to the Housing Trust Fund in your bill are detailed in my written testimony and my letter to you of October 11. The essence is that we ask that you preserve the Housing Trust Fund as enacted in HERA with the sole purpose of expanding rental housing that is affordable for extremely low-income households, and to maximize the funding provided to it through the dedicated sources of revenue that you are creating in this bill.

Thank you so much.

Chairman JOHNSON. Thank you. Dr. Holtz-Eakin, you may proceed.

STATEMENT OF DOUGLAS HOLTZ-EAKIN, PRESIDENT, AMERICAN ACTION FORUM

Mr. HOLTZ-EAKIN. Thank you, Mr. Chairman, Ranking Member Crapo, and Members of the Committee for the privilege of testifying today. I have a written testimony for the record and I will just make three brief points at this juncture.

First, in my view, housing finance reform is long overdue and I applaud the Committee for taking up the legislation that you are working on, and I encourage you to continue to try to push it across the finish line. That is something the Nation needs.

Second, in doing so, I think it is important not to replicate the affordable housing goals that were in the housing GSEs, and I want to thank the Chairman for noting my dissent in the Financial Crisis Inquiry Commission. I am now assured that the readership has reached one.

[Laughter.]

Mr. HOLTZ-EAKIN. But as you pointed out, I have never felt those affordable housing goals were central to the crisis that we experienced. It is a very complicated set of causes of that crisis. But they did not work either. They were poorly targeted. They tended to lag the market. And in my view, they also suffered from being off-budget and not subject to the appropriate scrutiny by the Congress.

And that brings me to my main point, which is that I do not think you will find any great disagreement about the need to help low-income Americans have adequate shelter. That is a laudable and important policy goal that the Committee should pursue. And as my written testimony makes clear, and the GAO report lays out, we have an enormous array of on-budget appropriated programs which are intended to meet that need.

We have scrutinized tax expenditures which are run through the Finance Committee and are part of the budgetary process. I do not think it is appropriate to create a new program which is outside of the budget process, which does not require the Congress to annually look at the effectiveness of the program, to balance the tradeoffs between this policy objective and the others that you will face. They are unquestionably real and difficult.

And that in going forward with assistance to low-income shelter, the starting point ought to be to take the programs that exist and make them work better, target them more effectively, and if more resources are needed, put them in through the budget process, not through something which is a fee outside the budget process that does not enter into the regulatory tradeoffs that you face.

So I thank you for the chance to be here today and I look forward to answering your questions.

Chairman JOHNSON. Thank you. Mr. Handelman, you may proceed.

STATEMENT OF ETHAN HANDELMAN, VICE PRESIDENT FOR POLICY AND ADVOCACY, NATIONAL HOUSING CONFERENCE

Mr. HANDELMAN. Thank you very much, Mr. Chairman, Ranking Member Crapo, and all the Members of the Committee for bringing me here today to testify.

I particularly appreciate the constructive bipartisan manner that the Committee has been pursuing this exercise. It is essential to the future of America, and I think your efforts will certainly pay off in the system that is created.

I am particularly glad to see affordable options for housing in the title of this hearing because that should be a central goal of housing finance reform. The work of rebuilding the mortgage finance system cannot only be about making markets function well. That has to be part of it, but it must also be about shelter.

As the Federal Government creates new mechanisms for housing finance, deploys its full faith and credit, and encourages private entities to put capital to work, the social purpose of safe, decent, and affordable housing for all in America must guide those efforts.

The new housing finance system you are working hard to create must find ways to harness the creativity and energy of the private sector to provide homes for people across this country, that is in cities, suburbs, and rural areas in houses, apartments, in manufactured homes, for old and young, renters and owners, singles and families of all backgrounds.

To accomplish that, the housing system must, by design, serve as broadly as possible and then there must be specialized mechanisms to fill in the remaining gaps, and those must work together. You have heard a lot about the need for affordable housing and there is great consensus here. There is more in my written testimony about it, but I will not belabor it here.

What I will suggest, however, is that the urgency of mortgage finance reform stems both from the growing housing needs of Americans and the need to restore a reliable source of mortgage capital in the wake of the financial crisis. And there are several parts to that solution.

The first part of the Federal guarantee. You have heard several of my colleagues on the panel talk about that. Second is allowing multiple sources of capital, multiple channels, including specialized lenders like housing finance agencies, credit unions, community banks, and other smaller lenders to have access to the most efficient form of mortgage capital.

Third is safe and sustainable low-downpayment lending. You have heard a little bit about that on the panel. I am happy to talk more about it, but there are excellent studies that show that if properly structured, low-downpayment lending can be very safe and very sustainable, prime-like in its characteristics, and I would urge you to eliminate the overly rigid 5-percent downpayment restriction that is currently hard-wired into S.1217, and allow more flexibility to do safe and sustainable low-downpayment lending, consistent with safe underwriting.

Next is particularly important and, Mr. Chairman, you mentioned this in your opening statement, that the market needs to serve all qualified borrowers in all areas of the country. It is very difficult for either the primary market that originates loans or the secondary market that securitizes them to cause the other to broaden its parameters for what loans to provide because neither can act without the support of the other.

It is only by Government action using strong regulation consistent with safe and sound underwriting that we can make sure that all parts of the country are served and that the risk pooling that occurs through securitization does not just either cream the best loans or omit whole sections of the housing market from its service.

Fifth is financing affordable multifamily housing. This is a very important source of rental housing. It has already been the subject of a previous hearing by this Committee, so I will not belabor it here. It is not part of my written testimony. But we are recommending that the successful Fannie Mae and Freddie Mac multifamily businesses, which have been proven and profitable even throughout the crisis, be prepared for eventual spin-off and privatization as part of the new mortgage finance system.

The last part is filling in the gaps that the market leaves, that even with the best engineering, there will be parts of our country that are underserved, and you have heard some discussion of those areas.

The three mechanisms that we recommend for solving that, one is the Housing Trust Fund. You have heard an excellent presentation about that. Second is the Capital Magnet Fund which supports financing for the preservation, rehabilitation, or purchase of affordable housing for low-income communities, and also community service facilities. It leverages other funds at least ten to one and has proven in its single round of funding to be extremely effective.

The third is to create a market access fund which would help share the cost with the private sector of finding new ways through competitive research and development grants and temporary credit enhancement to more efficiently serve unmet housing need.

It is a way to cut through the far too common challenge where private sector entities say, Look we do not know how to serve certain sections. It is not profitable. And Government or advocates say, Well, you ought to, and the private sector says, Well, we just told you it is not profitable.

By helping to share the cost and risk of the research, of figuring out how to do it consistent with safe underwriting, doing it in sustainable and profitable ways, we can help to broaden access. And I think that is why, as we shift to a new system, the Market Access Fund is an important complement to those efforts.

I will close with two points. First really just a reference to my written testimony that talks about how addressing house need early and preventing homelessness, preventing foreclosure, preventing displacement and instability really does pay off in all sorts of ways that affect both Government revenue and economic activity.

And last, urge you to think holistically about this problem, that as you are reengineering the system, as you are putting all of the pieces together, recognize how they fit together, and that by making the market serve as broadly as is possible profitably and then filling in the gaps, we can do a better job of making sure that the needs of all in this country for safe, decent, and affordable housing are met.

Thank you very much.

Chairman JOHNSON. Thank you. And thank you all for your testimony. As we begin questions, I will ask the clerk to put 5 minutes on the clock for each Member.

A question for Mr. Judson, Mr. Shelton, and Mr. Handelman. Mr. Judson, do you believe that the new system should include a requirement to provide broad access to credit for qualified single family and multifamily credit in all geographies, including rural markets and market conditions?

Mr. JUDSON. The simple answer to that—sorry—the simple answer to that is yes, it has to be accountable, it has to be properly underwritten, which I think you have heard from the panel and, as you all well know, is the fundamental element in any underwriting process. It has to be properly underwritten.

We think it can be served, both the rural areas through some of the programs that are existing now at USDA. We think that the lower income markets can be served, again if they are properly underwritten. The key to all of it is have a program that is specifically addressing those components of geographic area, as well as the socioeconomic areas.

Chairman JOHNSON. Mr. Shelton, do you have any additional thoughts?

Mr. SHELTON. No, I strongly agree as well. The kind of economic support, these outlays, are extremely important as we move ahead.

Chairman JOHNSON. Mr. Handelman.

Mr. HANDELMAN. I would agree with my colleagues. The only point I would add is that as you think about securitization, it is largely an exercise in risk pooling and that without the requirement to serve very broadly, you get concentration of either very good credit risk or very bad credit risk in pools.

The very good ones, it is profitable, that gets done. If you concentrate the very—the worst credit risk, it does not get done and that is where you get underserving. So the requirement to serve broadly is part of making sure that the efficiency reaches all parts of the country.

Chairman JOHNSON. Dr. Crowley, from your area with some of the housing challenges faced by families in Indian country, how could a housing trust fund assist tribes in creating good quality, affordable housing?

Ms. CROWLEY. Thank you for that question, Senator Johnson. We are very fortunate the National Low Income Housing Coalition to have Pinky Clifford on our board who lives on the Pine Ridge Reservation, and is a member of the Oglala Sioux tribe. Pinky invited me out to Pine Ridge. I spent some days there with her. And it was a very eye-opening experience. The conditions, housing conditions there are quite extraordinary.

The Housing Trust Fund is specifically designed to provide rental housing for the very poorest people, and as it is currently structured, the grants would go to the Governors, and any able and willing provider within the State could apply for those.

We would certainly support any provision that you would like to offer about having a set-aside for tribes, which we think would be an important thing to do as well. I talked to Pinky yesterday and she got permission from a woman to tell you this story. She has been on the waiting list for housing there since 1995.

She lives in a trailer with no running water. She has an outhouse. And that she has been waiting. She has patiently put her name on the list, recertified every year, and she is now at the top of the list. But there is no housing for her to go to. She is still waiting and she said that she hopes that she gets a house before she dies.

So the situation is quite dire and the Trust Fund would be very important there.

Chairman JOHNSON. I know Pinky well.

Mr. Judson, this new legislation includes stricter underwriting such as a minimum downpayment. What impact would that have on the demand for new homes and how would that affect current home prices? Alternatively, should the regulator of the new system have the flexibility to adjust underwriting standards?

Mr. JUDSON. Thank you. As mentioned earlier, the underwriting standards are the key to the success with this. The downpayment is less of a factor. There are certainly qualified buyers out there, particularly the entry level or first time buyer who cannot accumulate the funds or some of the required downpayments that are being proposed, i.e., the 20 percent.

Five percent, 3 percent, whatever that number is, is supportable, again, if properly underwritten. You can look at the VA loans to substantiate that. The effect of having a lower downpayment would be that more people will be able to qualify, more people, specifically the first time buyer will be able to qualify to own their homes and begin that accumulation of their net worth and creating the social fabric that goes along with that home ownership.

Chairman JOHNSON. Senator Crapo.

Senator CRAPO. Thank you, Mr. Chairman.

Dr. Holtz-Eakin, in my opening statement, I noted that using the current funding mechanism in S.1217, the Housing Trust Fund and the Capital Magnet Fund would receive an estimated total of somewhere between $2.5 to $5 billion based on the current secondary market size, and this represents about 10 percent of HUD's annual budget.

What kind of safeguards do you think would be appropriate to ensure that these funds remain accountable to Congress and to the American taxpayer?

Mr. HOLTZ-EAKIN. Well, I think first and foremost, they should go through the appropriations process. I think that the notion of creating off-budget entities and dedicated funding for them violates the integrity of the Congressional budget process.

These are important policy goals, that is not in dispute, but the program should be reviewed on a regular basis to make sure that they are meeting their policy objectives. The funding for them should be traded off against funding for other objectives within the HUD budget, and, you know, the reality is many programs that are on the budget now could be improved or eliminated and those funds will be freed up for these objectives.

Taking it outside the budget process relieves both the scrutiny on the trust fund, but also the scrutiny on the programs in the HUD budget, and that is a disservice to the taxpayer.

Senator CRAPO. Thank you. And Dr. Crowley, your organization has been the leading supporter of the National Housing Trust Fund in the United States, I think, and Dr. Holtz-Eakin noted that the Appropriations Committees of Congress should have a role in these funds, as he has just testified.

If they are going to be funded in the manner as suggested in S.1217, do you believe a role for Congressional appropriations through committees is appropriate, and perhaps through review and approval would be a reasonable method to assure accountability in the management of these funds?

Ms. CROWLEY. Let me answer that by saying that there is nobody in the country who wants there to be more oversight and greater accountability in this program than me. We are extremely clear that the dollars need to be spent for precisely what it is that Congress has intended, and that there have to be very strong mechanisms for oversight for how the money is used, and how the housing is kept up over the years, and all the things that we think are important.

We have worked too long and too hard to get this done just to see any of the money misused or wasted. So we support the strongest possible oversight that Congress can conceive of for this program.

Having said that, I have real confidence that the Banking Committee can do that, and would encourage you to look at ways to expand the oversight that is possible here. We are certainly open to talking about anything that you would like to talk about. We do not want the funds in any way to be used for other purposes. Housing trust funds that have been built across the country have been done with dedicated sources of revenue and the ones that are most successful have housing-related sources of revenue.

So the housing market produces money in one way and then money is directed into the housing trust funds in order to solve unmet needs—solve problems. If we thought the appropriations process worked, and we do not think it does, and if we thought we could get the appropriated funds, as I said in my testimony, to solve this problem, then we would not need to have this conversation.

But it has not proved to be the case. And we are losing ground in the existing affordable housing programs that we have. As the sequestration continues, for the very first time, people with vouchers are going to actually lose their homes. That has never happened.

It is time for some creative outside of the box thinking. We cannot continue to try to solve this problem in the narrow constraints of what we have. And so, having the housing finance market, which is making a lot of money, pay some fee to support things that the market will not do, we think is highly appropriate and we urge you to seize this opportunity.

Senator CRAPO. Thank you, Dr. Crowley. I can assure you you are not the only one who thinks the appropriations process needs to be fixed. I think we could get some strong bipartisan agreement on that today. Thank you very much.

Chairman JOHNSON. Senator Reed.

Senator REED. Thank you very much, Mr. Chairman.

As an appropriator, Senator, I concur.

Senator CRAPO. You agree with that?

Senator REED. Yes, I concur.

[Laughter.]

Senator REED. Dr. Crowley, there has been discussion of the Housing Trust Fund, that it could accumulate to about $2.5 billion. My best guess of the housing market is about $5.5 trillion, roughly. So this is a very small fraction of resources that is going to a very compelling need, in my view, which is housing for low-income.

Even if we were able to effectively deploy all this money, how much of the gap will we fill in terms of affordable housing for Americans?

Ms. CROWLEY. A small portion of the gap. Our estimate is that it is, as I said, if we were to close this gap, we would need 30 billion additional dollars for 10 years. So we are not getting close to that in this program. But we think that this is a way to get started, and certainly it gives hope to people out there who are actually trying to do something about housing.

If you go out and talk to people, as you all do, in your communities about the work that they do to try to help people find housing, there is a real sense of desperation. And I go out and I spend time with people and they say, "I have got so many people that I cannot place, I have got so many people that we are just spinning our wheels."

And what you are offering in the Housing Trust Fund is a sense of hope, that we have something that may happen, that we may begin to be able to dig ourselves out of this deep hole. So that is what we are striving for.

Senator REED. The Trust Fund is aiming, as I understand it, for individuals and families with incomes below 30 percent——

Ms. CROWLEY. Right.

Senator REED. ——of the area median income. So essentially, these are working families.

Ms. CROWLEY. That is right.

Senator REED. These are families who are working and they make too much, in most cases, to qualify for public housing, you know, but they do not make enough to get to be able to afford decent rental housing. Is that fair?

Ms. CROWLEY. Well, I think that the eligibility for public and assisted housing is 30 percent of area median income.

Senator REED. So they would qualify, but——

Ms. CROWLEY. They would qualify, but it is totally insufficient, as I said in my testimony. You know, every time there is a waiting list that opens, there are thousands and thousands of people who come in. In East Providence this last week, our friends at the Rhode Island Coalition for the Homeless went and videotaped people in the line to find out what their stories were, and the stories are remarkable.

People who are struggling and all they get to put their names on a list. They do not get a voucher, they do not get housing. They are just trying to get their names on a list to maybe get it someday. So it is people who are working hard, it is often people who are working more than one job.

A story from Sioux Falls is about a woman who has a job in a grocery store and she has a second job in order to make ends meet. And she is being asked if she would like to be considered for a promotion at the grocery store which would require that she work more hours there, which would mean she would have to give up her second job.

And she is not sure she can afford that promotion because she is not sure that she would be able to afford her home if she did not get to a certain wage in that new job. And so, she is making extraordinarily complex calculations about how many hours she has to work per week at what wage in order just to make ends meet.

Senator REED. Thank you.

Mr. Handelman, you mentioned the Capital Magnet Fund. We have had one tranche of $80 million in 2010. Can you kind of elaborate on how effective it was and how it engaged, perhaps, other sources?

Mr. HANDELMAN. Sure. Thank you for the question, Senator Reed.

The Capital Magnet Fund has been incredibly effective. It has required a leverage ratio of ten to one, so a lot of times it is used as gap financing or as bridge financing, which can be repaid and then reused. Some of the examples I have seen, there is a project in Alaska. It was one of the ones I cited in my testimony. It is 66 townhome units for folks at 50 percent or 60 percent of area median income, funded by Volunteers of America through their Capital Magnet Fund grant.

The leverage on that was exceptional. It is already being paid back so it can be then—the money can then be used again for gap financing. It integrates well with the Low-income Housing Tax Credit and it is very effective at preserving Section 8 rental housing. So it works well with some of the existing insufficient resources to maintain the investments that the Federal Government has already made in affordable housing.

Senator REED. Thank you. Thank you, Mr. Chairman. Thank you.

Chairman JOHNSON. Thank you. Senator Corker.

Senator CORKER. Thank you, Mr. Chairman. I want to thank you again and Ranking Member Crapo for having these extensive hearings to touch on all topics, and I want to thank the witnesses for being here today.

I know, for what it is worth, and especially sitting on this side of the dias you might not expect this, but the only reason I am in the Senate today probably is because of an effort that I started as a civic leader, not as a business, to provide the opportunity for all Chattanoogans to have decent, fit, and affordable housing. And that effort led to about 10,000 families in our community having housing that otherwise would not.

So I very much appreciate this panel and appreciate the effort to try to solve this problem in an appropriate way. And the written testimony today touched on this more than we are actually touching on in the oral presentation. I do think that we have to figure out a way on the duty to serve that you do not end up in a situation where we create a finance system that allows wealthy people to have cheaper loans, on one end of the spectrum, and on the other end of the spectrum we push the duty to serve so much that we end up with predatory lending.

And so, I know that we probably will not resolve that here today in this hearing, but I do welcome you in our offices, I know many other people do, too, to try to figure out a way to address that issue appropriately, and I think you know we can easily around here get things out of balance over time. So I invite you to our office, and I know other people here that are working on this issue would like to hear some of that same kind of input.

I was really interested in Dr. Crowley and Dr. Holtz-Eakin talking about this trust fund. I actually heard some overlap and I would like to sort of tease that out a little bit if I could. I know that Doug does not like off-balance sheet funding and, candidly, a lot of people do not. On the other hand, Sheila, if I could, you want to make sure that there is some kind of funding stream that is in place.

I just wonder if the two of you all might talk a little bit about how we could accomplish appropriate oversight if there, in fact, ends up being—and when we complete this work—a dedicated funding stream. Is there a way to have that accountability that Doug wants to see, and at the same time, have the income stream, Sheila, that you would like to see? And I wonder if you all might talk about that a little bit.

Ms. CROWLEY. Well, the first thing that comes to mind is that what we should look at is what has happened at the State and local housing trust funds. And I am not an expert on those—we have experts who we work with very closely on that—to see precisely how they have answered that question. How is that State legislatures have answered that question to see what their processes are? The States are the laboratories for how we figure out new ideas and then we bring them to the Federal level.

So I would be certainly willing to search through and look at that and see what that looks like and see what the recommendations would be from our friends who have worked on those State and local housing trust funds to see precisely what the accountability mechanisms are.

Senator CORKER. OK.

Mr. HOLTZ-EAKIN. So I have several concerns, obviously. The first is simply that—you know, Dr. Crowley is a tremendous advocate for this cause. It is a legitimate cause and there is going to be all sorts of advocacy. If the response of the Congress in every instance is to create a special outside-the-budget funding mechanism, then the admittedly broken appropriation and budget process will only be worse.

It will become a Balkanized, unbalanced set of efforts. And I am concerned about that. As the former CBO director in me, I am deeply concerned about the quality of the budgetary process that we have now. Steps like this go in the wrong direction, in my view.

What could one do? Well, first is——

Senator CORKER. Let me just say this. At the end of the day——

Mr. HOLTZ-EAKIN. It would not just be housing. It would be everything.

Senator CORKER. I understand. But we are talking about this.

Mr. HOLTZ-EAKIN. No, no, I hear you.

Senator CORKER. And I do think that—I mean, I think the reality of the situation is that a bill that likely passes the U.S. Senate—anyway, I do not know what happens on the House side—will likely fund the trust fund. I think that is likely to occur.

So my question is, is there a way to have appropriate oversight so that you can continue to play a role in understanding and making sure that there is accountability that ought to take place?

Mr. HOLTZ-EAKIN. Do not delegate too much authority to an independent regulator to set such a fee and fund such a trust fund. That should be something that is done within the Congress. Make it a mandatory spending program. If you do not like the appropriations process, I understand that. Have a mandatory spending program which has standard oversight by the authorizing committee and bring it through the budget process.

The key policy error would be to put it outside the regular review and budgetary tensions that the Congress faces, and I know it is going to get funded. It is a legitimate policy goal. There is no dispute about that, I hope. The question is, how do you, in this instance and in many others that arise, meet that policy goal without completely undercutting the objective of good use of the taxpayers' funds.

Ms. CROWLEY. My understanding is that it is structured as a mandatory fund on the permanent side of the budget and it is subject to the oversight of this Committee. Maybe I should just talk a minute about how the trust fund actually would work.

Senator CORKER. So the Chairman does not get too mad at me, make it a half a minute.

[Laughter.]

Ms. CROWLEY. It is set up, so the regulator does not have a lot to say about it. It is set up as a trust fund, as a block grant that is housed at HUD, so the money that Congress would direct to it would go to HUD. There is a formula that is in the HERA that says this is how much money goes to each State. That formula has been developed. It is based on need.

The Governor of each State would decide which agency would run it. It would usually be the housing finance agency. So that is all done. There is nothing optional there. That is all taken care of. And then the Governor has the responsibility to develop a plan for how to allocate those funds within the confines of what the trust fund is supposed to do, which is primarily rental housing for extremely low-income people.

The Governor can say, I am going to dedicate these dollars to funding my plan to end homelessness, which every State has. Or the Governor can say, We are going to use these dollars to respond to our requirement that we provide community-based housing for every disabled person in our State.

And then there are all sorts of prohibitions, things you cannot do with the money that are very clearly laid out in the statute. There are all sorts of requirements that if a Governor of a State does not spend its money in a certain amount of time, that HUD reclaim that money and distribute it to another State.

The statute is full of very strong protections that I think are probably quite extraordinary compared to what other programs are. And I am happy to come here every month and tell you what I know about it.

Senator CORKER. You are talking about the statutes that are actually in S.1217?

Ms. CROWLEY. S.1217 basically repeats what is in HERA, and all those things are in HERA. And so we have been down this road. We have thought about this a lot, and so, it does not seem to me that there is a lot of questions about accountability at this point.

Senator CORKER. I am going to thank you so much. And also, I have a hearing starting myself. Thank you so much. I appreciate it. Thank you all of you for your testimony.

Mr. HOLTZ-EAKIN. Mr. Chairman, without penalizing Senator Corker, can I add one thing quickly?

Chairman JOHNSON. Yes.

Mr. HOLTZ-EAKIN. A suggestion I would make is do not fund it with a G fee, which is what 100 percent gives it this dedicated function. Fund it out of general revenues. All the fee is going to do is raise mortgage costs, so that goes against affordability anyway, and then the program competes on a legitimate basis for funding in the policy process.

Chairman JOHNSON. OK. Thank you. Point well-taken. Senator Tester.

Senator TESTER. Yes, thank you, Mr. Chairman, and I want to echo what many have said. Thank you for having this hearing, as well as Ranking Member Crapo. I appreciate it. We all know how important affordable housing is; that is why we are here today. I want to thank our witnesses.

Unfortunately, I think, over the past several years, we have seen many mechanisms to provide more affordable housing, many of them get defunded. I want to talk a little bit about what we have been talking about and that is the Market Access Fund as envisioned in S.1217 that provides dedicated funding to the National Housing Trust Fund, as well as the Capital Magnet Fund.

These programs are going to be funded by five to ten basis points for folks using—for securities use a common securitization platform. To be honest with you, as we hear the discussion here today, I think I would like—this would give a dedicated stream of funding, and I think that is the real advantage. I think when you get into the appropriations process, and I like Senator Reed and Senator Johnson, are all appropriators and it is not working very well right now. It is not working very well at all.

And so, consequently, it puts at risk that dedicated funding stream. Because I think you are both going to agree on this, could you tell me how important that dedicated funding stream is for affordable housing? If the amount of money has a lot of peaks and valleys in it, what does that do to affordable housing? Both of you, either one go first, second.

Mr. HOLTZ-EAKIN. I guess what I would say lovingly to the appropriators is that it is time for you to get your act together. The solution is not to bypass this. It is time to do it right.

Senator TESTER. I understand that. But we are where we are for a number of reasons and——

Mr. HOLTZ-EAKIN. Well, the second point would be, I believe it was a mistake to make permanent reforms on temporary current conditions. We should design a program that we want in 2013, '23, '33. And third, I think dedicated funding is better than these cycles up and down.

Senator TESTER. And why?

Mr. HOLTZ-EAKIN. It allows a planning process. Housing is a durable asset and you have to plan. The local planning process with the environment regulations and the community planning objectives requires lead time and funding security. I mean, all those are legitimate parts——

Senator TESTER. Cost effectiveness, would it have any impacts on things that we do not like to spend money on like admin?

Mr. HOLTZ-EAKIN. Yes.

Senator TESTER. And those would be negative consequences?

Mr. HOLTZ-EAKIN. Yes. A clearly planned funding stream is superior, there is no doubt about that.

Senator TESTER. Cool. Would you like to comment on that at all, Ms. Crowley, Dr. Crowley?

Ms. CROWLEY. I just want to be really practical at this point.

Senator TESTER. Sure.

Ms. CROWLEY. And that the notion that we are creating a program to respond to temporary conditions seems pretty outrageous. These are not temporary conditions. We have had a housing shortage for extremely low-income people for many years in this country. It has not always been that case. In 1970, we had a small surplus. But we have been consistently losing ground in this area. We have had growing homelessness and it is unacceptable.

Senator TESTER. From your perspective, does S.1217 address the issues you are concerned about?

Ms. CROWLEY. S.1217 creates a very good dedicated funding stream and we certainly would support that.

Senator TESTER. Do you think that is adequate at five to ten basis points?

Ms. CROWLEY. No, but we are not asking for more——

Senator TESTER. All right.

Ms. CROWLEY. ——at this point. It is not adequate to solve the housing problems of the very poor. We would like to see the Trust Fund maximized in S.1217. We are concerned about the way that the bill is structured, that the funds are jumbled together instead of held separate. We would like to see them be separate.

Senator TESTER. OK. Mr. Handelman, in your testimony, you highlighted some of the ways that the Market Access Fund has envisioned S.1217, support innovation, promote home ownership. Briefly, could you talk more specifically about the areas where there are opportunity for innovation that could lead to home ownership?

Mr. HANDELMAN. Sure. Thank you for the question, Senator. I will highlight some examples and then—recognize that the point of the Market Access Fund is to do a bunch of experiments, so it is not just what I can think up sitting here at this table. It is going to be a whole lot of other people, much smarter about it than me, coming up with different things to try.

But some of the examples I highlight in the testimony, one is about energy efficiency and underwriting. Right now household energy costs in the country are about $230 billion annually and they make up 15 percent of the total cost of home ownership for average families.

So if we can find ways to encourage lending that encourages energy efficiency, there can be savings throughout and make housing more affordable. Thus far, we have not found great ways to lend against that efficiency. So this is where research and development and testing and process improvement can really make a difference.

Another great example is reserve funds for home ownership success. Rather than asking a family to really stretch and put all of their savings into a downpayment, if you can take a portion of that, separate it into a reserve fund to take care of the needs of the home, right, when the roof leaks or the boiler breaks, there is some funds to fix it, that could actually really improve the success rate of those borrowers and be better for the lender, be better for the community, be better for the homeowner.

So these are just examples and there are many more, but that is the point of trying to share the cost of R&D.

Senator TESTER. Well, thank you. And I want to thank all the folks on the panel. Very quickly, this is not a question, this is just, with your indulgence, a thank you. To Mr. Judson, I want to take a minute to thank you for your group's impacts on the appraisal system.

It is a broken system in Montana. Your members in the State have stepped up in a big, big way, and hopefully, we can continue to work with your input on how we can improve that appraisal process. With that, thank you all for your testimony. I very much appreciate it.

Chairman JOHNSON. Senator Johanns.

Senator JOHANNS. Let me also say thanks to the panel. If I could just comment, a word of thanks to the Chair and the Ranking Member. We have been going through a series of hearings on 1217. I am one of the cosponsors, truly a bipartisan bill. I think these have been excellent. I think the witness panels have been good; this is no exception to that and we have learned a lot.

I came to the Senate having done a lot of different things. Started out in county government and went to city government to then the Governor's office and then came out in the Bush administration to head up the USDA. So I have been in affordable housing really all of my public life. Here is a couple of things that I would offer about 1217, and I think it is really important to keep this in mind.

Number one, I think there is real urgency here. Yes, the market is improving and maybe some would think that takes the pressure off. It should not take the pressure off. We have got to fix this system and we have yet to have a witness come in here and say, Do not touch anything, I love the system. We all know it is a system waiting for the next crash, to be another real calamity.

The second thing I would say is that the only way this bill is going to pass is it has to be bipartisan. You know, if I were king for a day, which is not going to happen, I would probably write this bill differently. I think we all probably would write this bill differently and we would be more insistent on, I want it my way and there is no other way, but at the end of the day, we are going to have to get Democrats and Republicans to sign onto this bill and get it across the finish line.

So I would not argue that this is perfection, but I would argue that it is a gigantic step in the right direction in a whole bunch of areas. Here is what I am thinking about when I think about this bill. On one hand, we have a real estate finance system that is really a mess and we have got to fix it and I think this bill takes a giant step in that direction.

On the other hand, everybody here wants to do something about housing and affordable housing. I do, my colleagues on the other side do. I do not think there is a lack of heart here, but I would like your comment. I am going to start, Sheila, with you. My experience in affordable housing, and Rick, I will ask you to weigh in on this, too.

My experience in affordable housing is this: It is one of the most complicated endeavors you could possibly imagine. When we are in session, we have a place out here and the community where our place is at has this ongoing discussion about affordable housing. And I am thinking, My goodness, this is the worst place in the world for affordable housing because it is so danged expensive to live here. Land is expensive, development costs are expensive. Everything is expensive. How do you get affordable housing out of that?

Well, I think one opportunity with the Trust Fund—and if I were the Governor looking at this and it was funded, I would bring all my housing people together and I would say, OK, is this a program that we can fill some gaps? And maybe this is the bridge money that makes the project work that would not otherwise work, because at the end of the day, it has got to make economic sense or it is not going to come out of the ground.

Am I thinking of all of this in the right way? Sheila and then Rick, I would like your thoughts on that.

Ms. CROWLEY. Absolutely, Senator. The beauty of the structure of the Trust Fund—and we owe this to Senator Reed and the folks who worked on this before—is that it is a program where the money goes to the Governors who figure out how best to use those dollars in the markets in their States. Every market is different. Every community is different.

And you would bring together the experts in the State and say, "How can we deploy these dollars in the best possible way to do what we want to do, which is to lower that gap?" We can tell you what the gap is in Nebraska and we want to say that after a certain period of time, we will have fewer extremely low-income households who do not have affordable housing. And we are going to be able to count that and see how we get to that.

And it does include saying, "Where do we need to put money into other deals so that we can have certain units that are affordable to people in this income group." We would see these dollars being coupled with low-income housing tax credits.

We would see them being coupled with any number of other kinds of resources that create new housing or preserve housing, but where there is not the money to be able to write it down to be affordable for people at that lowest income level, and that is the whole idea.

Senator JOHANNS. Rick, thoughts?

Mr. JUDSON. Yes. Your point is very well taken and I think there are two things that jump to my mind, is the incorporation of low-income housing tax credits, which are private money, which are revenue-neutral to the Government, we will say, but provide a service to the community. So it is a win-win proposition, to incorporate that right balance between the low-income housing tax credits and the need for the community for affordable housing.

The other would be zoning issues, which are probably more locally driven, which may allow for greater density opportunities if there is an affordable housing component involved. So the balance—I think we are all talking about the balance and the accountability. The economic balance is to provide service needed for low-income housing, and yet, to do it at the least possible cost to achieve the greatest result.

I think that is not going to be simply a dole from public coffers, but a combination of set-asides, a combination of incentives, fees, a number of components that will fuel that end result.

Senator JOHANNS. Thank you, Mr. Chairman.

Chairman JOHNSON. Senator Warner.

Senator WARNER. Thank you, Mr. Chairman. Again, I want to thank you and Ranking Member Crapo for continuing to hold these hearings.

I want to start where Senator Johanns left off and thank him and the cosponsors of 1217 because you are right. We would have written it all differently, but we wrote something that I believe actually advances the ball on a lot of fronts, including the affordability function, because, you know, one of the things is—and I think we kind of went for a long time with a system that worked relatively well.

But when we think back from a policy standpoint, who would have ever designed a system where we combined the function of private sector money making, a profit-making entity with this also quasi-role of an implicit Government. Immediately you have got some conflict there. And then on top of that, we layer a very, I believe, very important social function on these entities. Let us face it, they were damned if they do, damned if they do not.

We have lots and lots of folks on the progressive side who said the GSEs never did enough. We have lots of folks on the conservative side who feel like those very goals brought about the crisis. Now, I reject that notion, but there are people who have those strongly held views.

The idea of saying, first of all, do no harm, so whether it is low-income housing credits, whether it is Section 8, whether it is all the other pieces that make affordable housing, and particularly when you get to multifamily, without those, we would have no multifamily at all, and then say, let us maintain.

I again want to thank my Republican colleagues for working with this. Let us say, let us make sure we still promote this function, but let us charge for it in an appropriate way, let us set it off, let us put appropriate oversight, and let us take great things like the Housing Trust Fund that has been set up.

It is a great idea, but never had any money. And, you know, the dollars are in many, many billions a year that could actually help us achieve these goals. And I know, you know, one of the concerns—I missed and I apologize. We were at a budget conference. You may recall we have had this shut-down problem in the past. We are trying to avoid that going forward.

You know, I know there are questions about, Well, somehow if we take this out of the budget process, I would argue that if you have got the appropriate oversight, and I am going to get to a question here. If you take it out of the budget process, but you have the appropriate oversight that has representatives from the low-income housing community, from home builders, others on this board, and we have got this steady flow, do we not actually—and I will even ask Doug to comment on this as well—is, do we not actually create a countercyclical balance by having this funding source that is not subject to the budgetary constraints so that in these downturns, this fund that is still going to be stable actually could help us achieve our goals?

So if we could speak to the countercyclical protection nature, and love to have anybody on the panel address that. If you want to go down the line, that would be fine. Anybody want to start? Doug, do you want to start first? Go at it.

Mr. HOLTZ-EAKIN. I do not, but I will. I do not think there is anything about this structure that dominates the ability of the U.S. Treasury to borrow against cycles. So there is nothing, I think, supremely countercyclical. And indeed, the base, which is a securitization of underlying mortgages, has been traditionally a very cyclical part of our economy. So I do not think its cyclical properties are a virtue, quite frankly.

Senator WARNER. What I am saying, though, is that the ability to have a steady stream of income that is not subject to the budgetary constraints, I actually believe, helps us in that countercyclical. Sheila, if you want to comment?

Ms. CROWLEY. Precisely, and that is one of the things that is attractive about it from the perspective of people who are trying to solve housing problems on the ground, is that it would be a predictable stream of funding. Now, it does not mean it is going to be the same amount every year and hopefully it will, as the housing market is robust, then that money will, in fact, increase.

But it is a predictable stream of funding which they do not have now at all through the HUD programs. It is just really critical to understand that we have put most of our money in the HUD programs to maintain the housing that we have. We put very little into doing anything new.

And the money that we have put into doing anything new, the HOME Program, has been slashed dramatically over the past couple of budget cycles. So what it is that people can predict, that they can rely on. They can rely on the low income housing tax credit program, but it is highly competitive. It is not deeply targeted. There is a little bit of money for the Affordable Housing Program in the Federal Home Loan Banks, but that is highly competitive.

There is just nothing out there and this would be a Godsend to people who are trying to solve these problems.

Senator WARNER. I am running out of time, but if anybody wants to make a quick comment, if you could include Godsend in your comment, that would be helpful as well.

[Laughter.]

Mr. HANDELMAN. I will not use the word Godsend, but I will add that, you know, I think the countercyclical nature of it from an economic standpoint is probably somewhat limited, but by creating additional supply of homes affordable to extremely low-income folks, it helps to cushion against the impact of cycles on those households.

A lot of what we saw, and this is some of what our Center for Housing Policy found, both in renters and homeowners is that even as the cost of housing fell somewhat, because housing values fell and housing costs fell, incomes fell much worse. So that is part of the countercyclical nature of this, too.

Chairman JOHNSON. Senator Warren.

Senator WARREN. Thank you, Mr. Chairman.

I am going to pick up with Senator Warner's note, that a lot of people claim that Fannie and Freddie's affordable housing goals caused the 2008 crisis, but there is no evidence to back that up. In fact, the data studied by the Financial Crisis Inquiry Commission and the Federal Reserve show that the affordable housing goals had no impact on either the subprime loans, the number of the subprime loans, or on the price of those loans.

And, in fact, that the data showed that the underlying cause of the crisis was subprime lending in the private label market, not with Fannie and Freddie. But that is not to say that the affordable housing goals had no impact. They did have a powerful impact. They helped millions of families purchase homes.

According to data from Fannie and Freddie, from 2002 to 2007, between 6 million and 12 million families each year benefited from the affordable housing goals. That is millions of creditworthy, lower income or rural families that are building up savings even today thanks to those goals.

So before we all conclude that we are throwing out the affordable housing goals on the basis of some myth, I think we need to look carefully at what we would be giving up. And I would like to just get a single statement on the record here, if I can. Mr. Shelton, if the affordable housing goals are eliminated, what do you estimate would be the impact on home ownership rates in minority neighborhoods?

Mr. SHELTON. Well, it would be devastating. Quite frankly, we depended on that kind of support for years and years to make sure that we have access. You have seen what happened with the housing crisis. Over 52 percent of African Americans lost their homes.

They lost all their wealth and everything else that was so important to looking at the future and everything that we do with our homes, from educating our children to planning for our retirement.

Senator WARREN. Thank you. And, Dr. Crowley, could I ask you, would eliminate affordable housing goals, could you describe the impact on rural communities?

Ms. CROWLEY. Well, I think that it would be horrible because rural communities are where lenders are not likely to go unless there is some encouragement, incentive, requirement that they go there. I think that this Committee really needs to look at making sure that whatever is passed has something that holds the system accountable for getting lending into every single geography. We are talking about inner cities, but we are also talking about the most remote parts of the country.

And that is what your job is, is to figure out how to make sure that the system is fair and accessible to everybody.

Senator WARREN. So I want to just see if we can then wrap this into the next piece of it. I want to say, I commend Senators Warner and Corker for the work they have put into S.1217 and how you have moved this debate forward. But I am concerned about S.1217's elimination of the affordable housing goals.

We have all been talking about the strip of five to ten basis points on the Government-backed securities for the Housing Trust Fund, and I think the estimate is it would be about—produce about $2.5 to about $5 billion annually, is the estimate.

But the question I want to ask, Dr. Crowley, in your views, will $5 billion a year substitute for the benefits that the affordable housing goals provide for lower-income and rural communities?

Ms. CROWLEY. No way, no way. Let me just say that the affordable housing goals, which are very important, they did not reach poor people. And so, the Housing Trust Fund is—the reason that we established it is so that we, in fact, have a way to come up with a dedicated revenue source to get to rental housing for extremely poor people.

And so, we would like a good portion of that to have the $5 billion to go to the Housing Trust Fund, which is not going to do the kinds of things that we need to do to create access to home ownership for middle income families.

Senator WARREN. So the point I just think I wanted to make sure that we are clear on, one is not a substitute for the other?

Ms. CROWLEY. No, no.

Senator WARREN. And we have got to look at both of these independently. I see that I am running low on time and the Chairman has been so gracious to let me go over so many times. I will quit now, but I do have a question for the record about duty to serve and how we make sure that that reaches rural communities and low-income communities. So I will add that as a question. Thank you.

Chairman JOHNSON. Senator Heitkamp.

Senator HEITKAMP. Thank you, Mr. Chairman, and thanks to the Ranking Member. I think these are have been extraordinarily helpful, especially for some of the newer Members who have not been in the trenches for years and years, kind of looking at housing struggles, and certainly affordability is one of the biggest challenges we have as we look forward.

Arguably, one of the biggest challenges we have today in North Dakota is housing. We have a huge economic boom, and which you can all say are you not lucky, but the person who is working at the grocery store making $15 an hour who cannot afford to live and is living in their car do not feel so lucky.

And so, one of the questions that I have is how we define affordability, and a lot of this is based on national standards on, you know, taking a look at what housing costs are. When you tell people in Dickinson, North Dakota, half-a-million-dollar house does not buy you much, you might all look at me like I am crazy, but it is the truth.

And so, my question is, do you think there is enough flexibility in this effort to accommodate for regional variances and for, you know, kind of boom times, which really have a huge affordability impact on those who are not getting—opening up their mailbox and getting a $1,000 check every week from the oil industry. I would ask anyone on the panel to respond.

Mr. HANDELMAN. Sure. So I will start. I would say one of the strengths not just of the trust fund, but the Capital Magnet Fund, but of the way affordable housing is, in general, delivered is that it is tied to area median income, which is imperfect, but pretty good at addressing some of the challenges you identified.

If there is a local boom in income, which then pushes up rent and pushes up housing costs, both of those can be captured. There is sometimes a lag, right, because Government data take awhile to work through the machine. But the way different programs are structured, so, for instance, HUD Section 8 program is tied to the fair market rent, which is a survey everywhere.

Senator HEITKAMP. Right.

Mr. HANDELMAN. Imperfect, but it gets to some of that variation.

Senator HEITKAMP. If I can just interrupt you there?

Mr. HANDELMAN. Sure.

Senator HEITKAMP. Section 8 has become irrelevant in western North Dakota. Those vouchers have been moved east because they do not accommodate the increased housing costs. Now we are in the third or fourth year of this and they have not caught up. And so, not to belabor this point, but this is something that I want to kind of lay down the marker on that. We need to have more flexibility for other parts of the country.

Dr. Crowley, I really appreciate your response on Native American housing, and I want to ask this question and I know that it is not necessarily directly related to this bill itself. The Income Tax Credit Program, which is a program that States have the ability to allocating those resources, have you seen those income tax credit programs work effectively in Indian country throughout the United States?

Ms. CROWLEY. You mean the Low-Income Housing Tax Credit Program? My understanding is that it has not reached Indian country very well, and part of the problem is that the people who live in Indian country are too poor to be able to afford the minimum rents that are required in tax credit properties.

For tax credit properties, the rent is set at a flat amount and they are not required to be targeted to the very poorest people. So unless you have other subsidies, tax credits are not very useful in Indian country.

Senator HEITKAMP. So this very significant program across the country is not particularly responsive. The other thing I would tell you is that you need someone who wants to use those credits, who is willing to come to Indian country and do the development, and that has also been a problem.

Finally, and following up on Senator Warner's line of questioning, we have tried to find some kind of actual economic verification of the impact of the affordable housing goals, you know, actually quantified. Can I just—you do not need to respond to this now, but can I ask that, to the extent that you have actual data, hard data on the impact as we have discussed here, that you could provide it, certainly to my office and maybe any other Member who would interested in seeing that?

Because we are having this discussion about the affordable housing goals, and I think it is really important that we operate on not emotion, but on fact. And so, I would appreciate if you would submit that information for the record and provide it to my office.

Ms. CROWLEY. OK.

Senator HEITKAMP. Thank you.

Chairman JOHNSON. Senator Hagan.

Senator HAGAN. Thank you, Mr. Chairman. Thanks for Senator Johnson and Crapo for hosting—holding this today.

I want to start out by welcoming Rick Judson to the panel. Rick is a North Carolinian. He is a home builder who has been in the industry building single family, multifamily, commercial projects for 30 years, and he is the owner of the Evergreen Development Group in Charlotte. So, Mr. Judson, thank you for joining us today on the panel.

I wanted to start off with a question for you. Talking about access and affordability of the housing. In your testimony, you highlighted the shift that is taking place today as children of the baby boom generation are beginning to form households. These are the young adults today that were born in the 1980s and the 1990s, primarily.

So can you talk about this demographic shift that is playing out, not only in North Carolina, obviously with your background, but also how this demographic shift is actually impacting access and affordability in the housing market? And do you believe that housing finance reform can help alleviate some of these affordability concerns for this cohort group of the echo boomers?

Mr. JUDSON. I will answer that question—thank you—with an example, a specific example, and it is typical of what exists across the country. I have a project in Charlotte that is an infill project, 190-unit townhome project. The profile of the buyer is all the same: Young, first-time professional buyers, my children, our children, that era.

The community was selling very robustly until the market tanked a few years ago. The same profile buyer is now renting in that project. They are afraid to buy. It is not that they cannot qualify, it is not that their social fabric has changed. Their income is still good. It is the uncertainty of the market. Are they concerned about their jobs? Yes. Are they concerned about rising interest rates? Yes.

They are equally concerned about what they have heard for 3 years about qualifying for a loan. They are of the mentality that they have to put down 20 or 25 percent when, in fact, there are programs and should be programs that support a qualified buyer to purchase a home, that first home.

The adage in our industry is if you do not buy the first home, you will certainly not buy the second or the third. And it is that first-time buyer that represents 35, almost 40 percent, in some cases, of the housing stock in this country, which is 17 percent of the GDP.

So long story short, the financial reform will help the market. It will help stabilize the market. It will create certainty for the market and it will create a sense of confidence in that first-time buyer who is a qualified buyer. This is not a no-doc loan or some of the things that got us in trouble in the past, but it is a legitimately well underwritten product.

Senator HAGAN. Do you see things changing now? Are things getting better?

Mr. JUDSON. The market is improving because the confidence of the general consumer is improving. They are finding there is opportunity. There is a supply/demand scenario that is moving people off the fences and out of our basements into purchasing their own home because they feel better and brighter future opportunity as we move through this.

Senator HAGAN. Thank you. Dr. Crowley, in North Carolina 32 percent of the households, as Mr. Judson was saying, are renters, and we have got close to 300 households that have extremely low income, meaning a family of four with income less than $17,300. So over 75 percent of those families spend more income on housing cost than—on housing cost and utilities. They spend more than 75 percent of their income on their housing and utilities.

Would you agree that providing a dedicated source of funding for the National Housing Trust Fund in GSE reform could help to alleviate the affordable housing strains that we are seeing, at least in my State in North Carolina, and how exactly would the Trust Fund actually accomplish that?

Ms. CROWLEY. The answer is yes, and I do agree with that, and the specifics is that the Trust Fund is dollars that would be distributed to the Governors and the Governor would develop a plan for how to use those dollars. There is a great deal of flexibility in what they can do with the dollars, except that the dollars primarily have to benefit precisely the population that you are talking about.

Ninety percent of the dollars have to be for rental housing; at least 75 percent have to benefit extremely low-income households. But how they do that, if they build new housing, if they want to rehabilitate housing, if they want to create operating subsidies to go along with Trust Fund-funded housing, those are the things that the legislation allows them to do in a way that fits local markets.

Senator HAGAN. Thank you, Mr. Chairman.

Chairman JOHNSON. Thank you again to all of our witnesses for being here with us today. I also want to thank Senator Crapo and all of my colleagues for their ongoing commitment to examine this topic in detail. This hearing is adjourned.

[Whereupon, at 11:37 a.m., the hearing was adjourned.]

[Prepared statements and responses to written questions supplied for the record follow:]

PREPARED STATEMENT OF HILARY O. SHELTON

WASHINGTON BUREAU DIRECTOR AND SENIOR VICE PRESIDENT FOR POLICY AND ADVOCACY, NAACP

NOVEMBER 7, 2013

Good morning, Senator Johnson, Senator Crapo, and esteemed members of this panel. Founded more than 104 years ago, in February of 1909, the National Association for the Advancement of Colored People, the NAACP, is our Nation's oldest, largest, and most widely recognized grassroots based civil rights organization. We currently have more than 2,200 membership units across the Nation, with members in every one of the 50 States.

My name is Hilary Shelton, and I am the Director of the NAACP Washington Bureau and the Senior Vice President for Policy and Advocacy. I have been the Director of the NAACP Washington Bureau, our Association's Federal legislative and political advocacy arm, for over 16 years.

Owning a home remains the American dream. For many, it represents a degree of financial success as well as an opportunity to build and retain wealth, which in turn can be passed down to future generations, used as collateral for college tuition, or used as a nest egg in one's senior years. Our Nation, our communities, and our people, all benefit from safe, affordable, secure housing, whether it be through home ownership or rental housing. Furthermore, it has been estimated that the housing market currently generates more than $10 trillion per year in domestic economic activity. Given that our Nation's overall economic activity is estimated at roughly $17 trillion, we all have a vested interest in a healthy housing market.

Yet the communities served and represented by the NAACP have long been underserved by the housing market; were, for decades targeted by predatory lenders; and, as a result have been denied the opportunity to build wealth through housing or worse yet have had their wealth stripped from them because they, like almost every other person in our Nation, were chasing the American dream. Furthermore, many of our communities, in fact a disproportionate number of communities of color, continue to suffer from the foreclosure crisis and continue to be neglected by too many mainstream financial institutions.

As Congress considers and debates the future of the housing market and the role to be played by the Federal Government, I cannot stress enough how important it is that any future housing finance system must affirmatively establish pathways to sustainable and affordable home ownership for a wide range of qualified buyers as well as assure an adequate supply of safe and affordable rental homes. It is vital that the Federal Government uses its authority and its might to ensure that the secondary market serves all borrowers in a fair and equitable manner, and that some of the profits from the housing market be reinvested in the American people and in our economy through the construction, renovation, and preservation of safe and affordable rental housing.

The Origins and the Impact of the Housing Crisis on Communities of Color

The 2008 "burst" of the housing bubble had repercussions which are still being felt today, especially in communities of color across the United States. An estimated 4.5 million homes have been foreclosed upon since the crisis began, [1] and many more are still at risk of foreclosure. Due largely to the targeted predatory lending which had been going on for years in communities of color, the rate of foreclosures is currently twice as high for borrowers of color when compared to white borrowers. [2]

In addition to the households actually facing the prospect of foreclosure, the crisis has also impacted homeowners who live in neighborhoods with high levels of foreclosures. This so-called "spillover" effect has reduced property values and home equity for many homeowners, including a large number of homeowners of color. One study estimated that racial and ethnic minority neighborhoods will lose $1 trillion in home equity because of the impact that homes going through the foreclosure process has on overall neighborhood property values, fully half of the overall national total. [3] Furthermore, too many homeowners have found that as a result of unscrupulous loans and the "spillover" effect their homes are now "underwater," whereby they owe more than their home is currently worth.

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[1] *http://www.nasdaq.com/article/1-in-5-predicted-to-default-cm95228*

[2] Center for Responsible Lending, "State of Lending in America", December 2012, available at: *http://www.responsiblelending.org/state-of-lending/reports/3-Mortgages.pdf.*

[3] Center for Responsible Lending, August, 2013, available at: *http://www.responsiblelending.org/mortgage-lending/research-analysis/2013-crl-research-update-foreclosure-spillover-effects-final-aug-19-docx.pdf.*

One result of this disproportionate impact of the foreclosure crisis on communities of color has been that they have, in recent times, suffered a disproportionately extreme loss of wealth. Between 2007 and 2010, African Americans lost an estimated 31 percent of their wealth; Hispanic families lost 44 percent of their wealth; and White families lost 11 percent.[4]

A study by the Federal Reserve Bank of San Francisco found that CRA-eligible loans made in California during the subprime boom were half as likely to go into foreclosure as loans made by independent mortgage companies (Laderman and Reid, 2008).

Despite the disproportionately devastating impact the housing burst and foreclosure crisis has had on communities of color across the United States, there is strong evidence to indicate that we neither profited from the calamity nor did we cause it.

According to the Financial Crisis Inquiry Commission, the crisis was triggered by the rapid growth in the origination and securitization of subprime loans in the private-label market.[5] Furthermore, according to a careful analysis of the housing crisis released just last year by the Federal Reserve Bank of St. Louis, Fannie Mae and Freddie Mac's affordable housing goals were not to blame for the rapid increase in subprime originations. Although Fannie and Freddie purchased securities backed by subprime loans, and some of those purchases helped fulfill their affordable housing goals, the study's authors found that the housing goals had no impact on either the number of subprime loans originated or the price of those loans in the private-label market.[6]

In short, while the communities served and represented by the NAACP have suffered disproportionately from the housing crisis and subsequent recession, they were not caused by laudable affordable housing goals. Nor was the housing crisis caused by compliance with the Community Reinvestment Act, as some have tried to claim. In fact, studies show that loans made to low-wealth homebuyers as part of banks' efforts to meet their CRA obligations have actually performed better than the rest of the subprime market.[7]

Rather, the source of too many of our economic woes was the desire of Fannie and Freddie to make money for their private stakeholders, and the willingness of the private-label market to accommodate their desires. To quote an esteemed member of this panel, the gracious and brilliant Senator from Massachusetts, who happens to be a former professor at Harvard specializing in bankruptcy law and who helped create the Consumer Financial Protection Bureau, "Affordable housing goals have been scapegoated by those who have been itching to get rid of the goals for a long time, but I think it's time to drop that red herring."[8] The NAACP could not agree more.

Necessary Elements of Genuine Reform

Chairman Johnson, Members of this Committee, I do not need to tell you that the American housing market is incredibly complicated and complex; its needs and fortunes vary from region to region, income to income, and year-to-year. Nobody, including me, has all the answers to reforming the current system, ensuring that all the housing needs of the American people are met, and reducing if not eliminating the risk to tax payers of another bailout and another recession.

Yet I do know that as we take steps to reform the housing market we must do all that we can to ensure that every American has access to safe, affordable, sustainable housing. For low income Americans, this means that we must ensure that there is an adequate stock of safe and affordable rental units throughout the country, and for qualified, middle income Americans this means that we must make sure that sustainable, affordable mortgages are available.

Nationwide, there are currently approximately 7.1 million American households for whom even a modest rental home is unaffordable and unavailable. Families in

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[4] Signe-Mary McKernan, Caroline Ratcliffe, C. Eugene Steuerle, and Sisi Zhang, "Less Than Equal: Racial Disparities in Wealth Accumulation" (Washington, DC: The Urban Institute, 2013).

[5] Financial Crisis Inquiry Commission, "The Final Crisis Inquiry Report", January 2011.

[6] Ruben Hernandez-Murillo, Andra C. Ghent, and Michael T. Owyang, Federal Reserve Bank of St. Louis, "Did Affordable Housing Goals Contribute to the Subprime Securities Boom?" (Aug. 2012), at *http://research.stlouisfed.org/wp/2012/2012-005.pdf.*

[7] In an analysis of CRA-motivated loans sold to CRL's affiliate Self-Help, a community development financial institution (CDFI), Ding, Quercia, Ratcliffe, and Li (2008) found that the default risk of these loans was much lower than subprime loans made to borrowers with similar income and credit risk profiles.

[8] Senator Elizabeth Warren, Speech Before the Mortgage Bankers Association, Washington, DC, October 29, 2013.

this situation find themselves making impossible choices between food, clothing, medicine, and rent. When illness, job loss or other tragedy strikes, they often become homeless. The NAACP has long been a strong supporter of the National Housing Trust Fund (NHTF) and as such, we are extremely pleased to see the current debate focusing on how to best ensure that it is fully and adequately funded, not if it should be funded at all.

In short, a solid stock of safe and affordable rental housing, such as that which could be supplied by the NHTF, is sufficiently important to the NAACP that we were pleased when the original source of funding for the NHTF was a dedicated source of revenue, namely contributions from Freddie Mac and Fannie Mae. In these days of sequestration and other budgetary cuts, this meant that the NHTF would not be subjected to the annual budget process. Furthermore, we felt strongly that the NHTF should never compete with existing HUD programs. Yet as history has shown us, the GSE funding stream proved to be unstable, and as a result, crucial funding for the NHTF has been suspended.

With this history in mind, and given that at least 90 percent of the funds set aside for the NHTF must be used for the production, preservation, rehabilitation, or operation of rental housing, and that it is intended to help extremely low income and very low income households, I will reiterate the NAACP's support for an inclusion of a consistent, adequate funding stream for the NHTF in any GSE reform. The NAACP is confident that the NHTF, once fully funded, will go a long way towards addressing many of our Nation's most urgent housing needs. The NAACP is dedicated to working with Members of Congress, the Administration, and private nonprofit groups at the local, State, and Federal levels to ensure that consistent, adequate funding for the NHTF is included in any GSE reform.

In addition to ensuring adequate, affordable rental stock, the future housing finance system must also affirmatively establish affordable, sustainable pathways to home ownership for all qualified buyers.

Allow me to back up a little, to the late 1990s and the early 2000s. As I have previously stated, targeted predatory lending—offering mortgages to people which were much more expensive than what they qualified for and which they could not afford—was rampant in the communities of color across the United States. These subprime loans were driven by greed, pure and simple, and they played upon the desire of people to live in their own homes. These nefarious loans were abetted and often encouraged by legal policies and practices such as steering and yield spread premiums.

Every time the NAACP or other, like-minded groups spoke out in opposition to these predatory policies and practices we were told that making them illegal would be contrary to "Preserving access to credit." It took the financial crisis of 2008 to get to the point at which our words sank in. In 2010, we were finally able to pass legislation, the Dodd/Frank Wall Street Reform bill, to curb many of these abuses. The NAACP strongly supported the enactment of Dodd/Frank, and we continue to support the strong regulations which are resulting from it; regulations which we believe will strengthen the underlying market.

Ensuring that all Americans have access to fair and sustainable credit opportunities is crucial to our sustained economic recovery. The Federal Government is obligated to promote nondiscrimination, residential integration, and equal access to the benefits of decent and safe housing and ownership opportunities. Therefore, any reform of the secondary market must require all lenders and securitizers receiving a Government guarantee of any kind to affirmatively market and offer credit in a manner that promotes equal opportunity in all neighborhoods.

The receipt of Federal support, including insurance and guarantees, invokes the mandate to affirmatively further the objectives of the Fair Housing Act. Therefore, the delivery of Government-supported mortgage credit or rental financing cannot be withheld from any geographic location or neighborhood. Instead, the delivery infrastructure must make deliberate provisions for the flow of credit to all qualified borrowers and neighborhoods. Moreover, the infrastructure must include a mechanism for monitoring and enforcing compliance, both by the Government and the public. Simple, transparent, and timely data must be made publicly available to measure the market's progress in providing fair, sustainable capital to underserved people and communities.

Furthermore, without an obligation to serve all markets, communities of color in particular will find it extremely difficult to access mortgage credit. Without a duty to serve all communities, as is dictated by the Community Reinvestment Act, private capital will gravitate to the elite homebuyers—those with traditional borrowing profiles—while middle class and first time homebuyers, as well as purchasers of color—will be left without. This will result in the exacerbation of an unsustainable housing finance market in which qualified but lower-wealth and lower-income buyers, especially minorities, will be underserved. Sadly this trend is already evident; the private market overwhelmingly caters to traditional borrowers in well-served locations.[9]

This trend does not just harm borrowers in minority communities, but rather the whole housing sector. Although African Americans and Hispanics are already significant segments of the housing market, they are projected to be an even larger portion of the market over the next 10–20 years. According to the Joint Center for Housing Studies at Harvard, minorities will account for 70 percent of net new households over this period and 33 percent of all households by 2020. These households will be younger than traditional borrowers and will likely have lower incomes and less credit history. These new borrowers will therefore need access to affordable housing credit. Without affordable access to credit for these prospective buyers, there will be a large supply of housing stock left unsold, leading to decreasing prices and wealth.[10]

Thus, it behooves all of us to ensure the availability of safe, sustainable, credit access and affordability for all homeowners and prospective homeowners alike. Reforming our Nation's current housing finance system requires a great balance. Reform must facilitate a stable, liquid secondary market—accessible to small and large lenders alike—which will extend credit and capital on an equitable basis to all qualified borrowers and in all communities. While the NAACP does not agree with every provision in the legislation proposed by Senators Corker and Warner (especially provisions which will negatively and disproportionately affect racial and ethnic minorities, including the mandated 5 percent downpayment), and we will be quick to point out areas in which the proposed legislation is lacking, we do congratulate them on moving the debate forward. Likewise, we are strongly encouraged by these hearings, being held by Chairman Johnson and Ranking Member Crapo, intended to look into necessary elements of GSE reform.

Members of this esteemed panel, I look forward to your questions, to the ensuing debate regarding GSE reform, and to working with you to ensure that any reform will benefit all homebuyers, renters, and our Nation as a whole. Thank you again for holding this hearing and for seeking the perspective of the NAACP.

PREPARED STATEMENT OF RICK JUDSON

CHAIRMAN, NATIONAL ASSOCIATION OF HOME BUILDERS

NOVEMBER 7, 2013

Chairman Johnson, Ranking Member Crapo, and Members of the Committee, I am pleased to appear before you today on behalf of the National Association of Home Builders (NAHB) to share our views on housing finance reform and the essential elements needed to provide affordable options for housing. My name is Rick Judson, and I am a builder/developer from Charlotte, North Carolina, and NAHB's 2013 Chairman of the Board.

NAHB represents over 140,000 members who are involved in building single family and multifamily housing, remodeling, and other aspects of residential and light commercial construction. NAHB's members construct approximately 80 percent of all new housing in America each year, and many of our builders rely on the programs of the Department of Housing and Urban Development (HUD), (most involving the Federal Housing Administration, FHA) and the U.S. Department of Agriculture's Rural Housing Service (RHS) to help provide decent, safe, and affordable single family and multifamily housing to many of our fellow citizens.

We believe that an effective housing finance system must address liquidity as well as affordability and that those two elements are very closely related. Therefore, while it is important that the system provide housing credit at affordable terms as well as address specific housing needs, it is also essential that credit is consistently available on those terms regardless of domestic and international economic and financial conditions.

NAHB is a strong proponent of housing finance system reform and feels significant changes should occur in the conventional mortgage market, where Fannie Mae and Freddie Mac currently account for almost all activity. NAHB supports steps to

[9] Bhutta, Neil, and Glenn B. Canner. 2013. "Mortgage Market Conditions and Borrower Outcomes: Evidence From the 2012 HMDA Data and Matched HMDA-Credit Record Data", Federal Reserve Bulletin. *http://www.federalreserve.gov/pubs/bulletin/2013/pdf/2012_HMDA.pdf.* Accessed on October 25, 2013.

[10] Joint Center for Housing Studies of Harvard University. 2013. "The State's of the Nation's Housing", Harvard University. *http://www.jchs.harvard.edu/sites/jchs.harvard.edu/files/son2013.pdf.* Accessed on October 25, 2013.

increase the role of private capital but does not believe the market can rely exclusively on private sources. Recent experience demonstrates that private players are unwilling or unable to participate in periods of extreme economic and financial distress.

NAHB also believes that the future housing finance system must be viewed as more than the private conventional market. The array of Federal Government programs that have been developed over the years in response to identified needs are essential elements in ensuring that there are affordable options for providing housing. Thus, this testimony includes NAHB's position on how those programs contribute to the national housing finance system.

Demographic and Economic Overview

The underlying demographics of the U.S. forecast a continuing rise in demand for housing over the next two decades. A combination of record births and past immigration will produce over four million people moving into prime household formation ages every year for at least the next 20 years. These young people, primarily the children of the baby-boom generation, will form their own households as they age into the 25- to 34-year old cohort. These younger households were among the hardest hit by the economic recession, reducing household formation rates by more than most other age groups.

While older households have largely recovered from household arrangement setbacks, younger households are still struggling to return to prerecession headship rates. And despite having lower headship rates than older segments of the population, these younger households are expected to add 2.4 million units to total housing demand over the next 10 years. Given their economic vulnerability, affordability will be key to recovery for these households.

Most newly formed households are just beginning their employment career and will not have large downpayments or lofty credit scores. Current extra tight underwriting standards have made mortgage attainment even more difficult for younger families. Student debt responsibilities and lower starting salaries and wages compound the ability for younger individuals to transition to home ownership without access to affordable opportunities.

In addition to the oncoming demand, NAHB estimates that two million households did not form during the recession and represent an additional pent up demand that will come to the housing market as the economy improves and hiring returns to more normal levels. Many young and not so young individuals either did not launch into an independent household or returned to live with their parents, relatives or friends after losing their job or experiencing a significant reduction in income. NAHB expects these individuals to establish their own home and be in the market for an apartment or owned home as the economy expands.

Providing affordable homes will also present a challenge to home builders as the cost of ingredients rises. Builders are paying more for labor, land, and building materials. As discussed later, builders continue to have difficulty accessing production credit from the traditional financial institution sources and have turned to nontraditional equity and debt sources that cost more.

Land development for homes ceased to take place during the Great Recession and building that capacity and process back up has taken time. In many revived and reviving markets, lots for single-family homes are very scarce, and prices have been bid up beyond what could be supported by current selling prices of completed homes. Construction workers found other sources of employment during the building collapse and can only be attracted back to home building with higher wages. Building material prices are back to or near the levels of 2005 when production was at two million homes. Production currently is less than one million, but while waiting for the material-producing industries to get back to capacity, prices have risen for the major building products like lumber, plywood, and drywall.

Current Restrictions and Gaps in the Market

The ability of the home building industry to meet the demand for housing, including addressing affordable housing needs, and contribute significantly to the Nation's economic growth is dependent on an efficiently operating housing finance system that provides adequate and reliable credit to home buyers and home builders at reasonable interest rates through all business conditions.

At present, home buyers and builders continue to confront challenging credit conditions weighed down by strict underwriting requirements and an uncertain future regulatory environment. For home buyers, while mortgage rates have fallen to record lows, access to mortgage credit is limited to those with pristine credit histories who can qualify for Government-backed programs. Presently, FHA, VA, Fannie Mae, and Freddie Mac (the Enterprises) account for more than 90 percent of mortgage originations.

Credit Overlays

Lender overlays in the mortgage credit process have been flagged as a major element in the greater difficulty potential home buyers are having in obtaining financing as lenders are imposing credit underwriting standards that are more restrictive than FHA, VA, Fannie Mae and Freddie Mac require. These credit overlays are employed due to heightened lender concerns over forced loan buy-backs on mortgages sold to Fannie Mae and Freddie Mac and/or greater required indemnifications on FHA-insured and VA-guaranteed loans.

While FHA and the Federal Housing Finance Agency (FHFA), which regulates Fannie Mae and Freddie Mac, have announced efforts to encourage lenders to refrain from excessive mortgage credit requirements, lender concerns about how Federal agencies will implement repurchases and indemnifications continue to constrain credit availability. This is evidenced by the sharp increase in average credit scores for new Enterprise loans from about 720 in 2006 to 760 in 2012. For FHA loans, average credit scores have jumped from around 650 in the early 2000s to 756 in 2012. According to the 2013 State of the Nation's Housing Report, these trends largely reflect the evaporation of loans to borrowers with weaker credit histories. "In 2007, borrowers with credit scores below 620 accounted for 45 percent of FHA loans. By the end of 2012, that share was under 5 percent." [1] Similar trends are evidenced in the share of first-time home buyers which accounted for 28 percent of home sales in September 2013, well below the historical average of about 40 percent.

Regulatory Constraints

The regulatory environment for mortgage lending is undergoing significant changes as regulators implement new rules mandated by the Dodd-Frank Act. Uncertainty about the eventual regulatory landscape is another key factor that has tightened access to mortgage credit. Attempts by lawmakers and regulators to prevent a repeat of the housing boom/bust and the financial crisis by purging risk from mortgage lending has further tightened the credit box.

NAHB supports steps to ensure that mortgage lending occurs in a safe and sound manner, with appropriate underwriting, prudent risk management and sound consumer safeguards and disclosure. NAHB believes that loans should be carefully underwritten and adequately disclosed. NAHB also believes that it is critical that mortgage lending reforms are imposed in a manner that causes minimum disruptions to the mortgage markets, while ensuring consumer protections.

The release of the final Ability to Repay (ATR) standard by the Consumer Financial Protection Bureau (CFPB), which will take effect on January 10, 2014, has alleviated some of the regulatory uncertainty by defining new requirements and liabilities on lenders, but will undoubtedly create new hurdles for borrowers. The ATR rule establishes standards for complying with the ability-to-repay requirement by making a "qualified mortgage" (QM). The CFPB included a safe harbor in the definition of a QM that would provide some assurance to lenders that they will not be subject to increased litigation if they use sound underwriting criteria. The safe harbor would apply to lower-priced loans that are typically made to borrowers who pose fewer risks. However, the CFPB also included a "rebuttable presumption of compliance" for higher-priced loans typically for consumers with insufficient or weak credit history. Additionally, the QM includes a 3-percent cap on points and fees, which is a new calculation that has to be incorporated into the mortgage approval process.

The ATR provides a new framework for all mortgage lending. To the extent that lenders will remain cautious during the transition and beyond, creditworthy borrowers may not have access to affordable mortgage credit, or may be left out of the credit box all together. Reports also are surfacing about the challenges that lenders are experiencing in preparing their systems for operation under the ATR and QM regulations.

NAHB was pleased in August when the six Federal agencies responsible for implementing the credit risk retention requirements mandated by the Dodd-Frank Act reissued a proposed rule with a revised definition of a "qualified residential mortgage" (QRM) that would equate with the definition of the QM. Aligning the QRM with the QM has many benefits. Establishing one streamlined regulation, instead of having two separate sets of underwriting criteria, will alleviate confusion in the marketplace and will provide clarity and transparency for home buyers, lenders, in-

[1] Joint Center for Housing Studies of Harvard University, "State of the Nation's Housing 2013", p. 19.

vestors and other housing market participants. Additionally, the underwriting criteria and product limitations contained in the QM will promote more prudent lending and will provide investors with an assurance that the loans are sustainable.

NAHB is supportive of ensuring safe, well documented, and soundly underwritten loans without limiting the availability, or increasing the costs of credit to borrowers. Aligning QRM with QM levels the playing field, promotes liquidity in the mortgage market and allows access to credit for a diverse range of home buyers, particularly first-time and low- to moderate-income home buyers. If the QRM is too restrictive, this important group of home buyers will have to rely on Government programs or potentially risky mortgage products for low-downpayment options. Encouraging private capital to provide mortgages with reasonable terms to a broad range of home buyers is imperative to support a sustained housing market recovery.

Commercial Real Estate

The proposed credit risk retention rule also sets forth the underwriting standards for a "qualified commercial real estate loan" (QCRE), which is presumed to be a low-risk loan. In the revised proposed rule, the agencies made modifications to their originally proposed criteria.

NAHB appreciates and supports the agencies proposed modifications. However, NAHB remains concerned that the regulators did not make distinctions among the different asset types included in CRE loans (hotel, retail, multifamily, office, etc.) in setting underwriting standards, except for the debt service coverage and amortization period of the loan. NAHB believes that it is not appropriate to apply the same standards to different classes because there are significant differences in property features, lease structures, tenant characteristics, etc., that affect how a CRE property is underwritten.

NAHB believes the QCRE is an important component of the credit risk retention requirements and setting an appropriate QCRE standard will be key to minimizing the impact on borrower financing costs for multifamily borrowers. To the extent that risk retention requirements raise multifamily financing costs, there will be an impact on rents. Higher rents have an immediate impact on renter households' budgets. For aspiring homeowners, higher rents also mean that it will take longer to save for a downpayment on a home. In addition, for other types of commercial properties, higher rents affect companies' ability to grow, and thus negatively impact job creation.

NAHB is concerned that, if not properly implemented, the credit risk retention regulations will further restrain credit to the multifamily housing sector. In addition to the adverse impact on families seeking affordable rental homes, such disruptions in the market have the potential to slow down the job creation and monetary contributions to the economy that are currently fueled by multifamily construction.

Importance of Federal Government Backstop

As stated earlier, NAHB's priority in housing finance system reform is ensuring liquidity for the housing sector in all markets throughout the economic cycle. This is only possible if market participants know there is a Federal Government backstop that will maintain stability in catastrophic circumstances. While NAHB agrees that the current degree of Government intervention is unsustainable, an ongoing, though more limited, Government role must be maintained to avoid future interruptions in the flow of credit to mortgage borrowers.

NAHB recommends establishing a new securitization model for single family and multifamily mortgages where Fannie Mae and Freddie Mac would be transitioned to private housing finance entities that would aggregate mortgages into securities for sale to investors worldwide.[2] Private capital from mortgage originators and securities issuers would be in the first loss position but the principal and interest for investors in the mortgage-backed securities would be guaranteed through a privately capitalized, federally backed insurance fund. Only mortgages with reasonable and well understood risk characteristics would be eligible to serve as collateral for Government-backed mortgage securities, and the system would be overseen by a strong and independent regulator.

The new housing finance system envisioned by NAHB is similar to that proposed in the Housing Finance Reform and Taxpayer Protection Act of 2013 (S.1217, Corker-Warner bill) which NAHB largely supports. In contrast, NAHB opposes the House Financial Services Committee-passed bill, H.R. 2767, the Protecting American Taxpayers and Homeowners Act of 2013 (PATH Act), which removes Govern-

[2] The full details of NAHB's housing finance system recommendations are contained in "A Comprehensive Framework for Housing Finance System Reform", published by NAHB on February 9, 2012.

ment support to the conventional mortgage market. While NAHB agrees that private capital must be the dominant source of mortgage credit, the future of the housing finance system cannot be left entirely to the private sector. The historical track record clearly shows that the private sector is not capable of providing a consistent and adequate supply of housing credit without a Federal backstop.

NAHB believes Federal support is particularly important in continuing the availability of the affordable 30-year fixed-rate mortgage (FRM), which has been a staple of the U.S. housing finance system since the 1930s. These loans are geared toward affordability; 30-year terms lock in low monthly payments, allowing households with average incomes to comfortably budget for their home loan. Knowing their monthly housing costs will remain the same year in and year out regardless of whether interest rates rise provides households with a sense of financial security and also acts as a hedge against inflation. Many young buyers know that as their incomes rise, their housing costs will stay constant and become less of a burden, enabling them to prepare for other long-term obligations, such as college tuitions and retirement savings. In most instances, all of the interest and property taxes borrowers pay in a given year can be fully deducted from their gross income to reduce taxable income. These deductions can result in thousands of dollars of tax savings, especially in the early years of a 30-year mortgage when interest makes up most of the payment.

The key to the sustainability of the 30-year FRM is a securitization outlet because originators (banks and thrifts) do not have the capacity to hold such long-term assets which are funded with short-term deposits. Currently, Fannie Mae and Freddie Mac provide the securities vehicle along with a Government guarantee for investors. There are serious doubts on whether a private housing finance system would be capable of supporting this type of product without some Government backing. At a minimum, the cost and terms of 30-year FRMs would be significantly less favorable under a totally private system.

A Government role is also essential for multifamily mortgage programs which also play a critical role in the overall health of the U.S. housing finance system. More than one-third of Americans live in rental housing and demand for rental housing in the future is expected to increase. As discussed further below, the multifamily sector performed much better than the single family housing market during the recent downturn. Multifamily loans held or guaranteed by Fannie Mae and Freddie Mac have very low default rates and the multifamily segments of both Enterprises are profitable. FHA also provides support to the multifamily market through the FHA multifamily mortgage insurance programs. Private market financing is not readily available for all segments of the multifamily market. Thus, there is a need to maintain a viable, liquid and efficient secondary market for multifamily rental financing where the Federal Government continues to play a role.

Future Cost of Housing Credit

In a future housing finance system, where several layers of private capital stand in front of a Government backstop for catastrophic circumstances, the relative cost of housing credit would increase from current levels as home buyers ultimately bear the charges needed to attract the private capital and cover the cost of the Government guarantee. However, NAHB believes that such a system would entail lower housing credit costs than one that relied exclusively on private players. Also, as mentioned previously, a completely private system likely would be subject to inconsistent credit availability.

With the prospect of higher mortgage borrowing costs, NAHB believes it is extremely important to make every effort to ensure that mortgage interest rates and fees do not increase more than is absolutely necessary to safely sustain the new system. The requirement in S.1217 (Corker-Warner bill) that first-loss capital providers hold capital of 10 percent of their risk exposure is excessive and would unnecessarily increase mortgage borrowing costs. A capital cushion of 4 to 5 percent would have been sufficient for Fannie Mae and Freddie Mac to sustain all of their losses during the recent decline in home prices and their current, more restrictive, book of business would require only a 2 to 3 percent capital under such a drop in collateral values. [3]

Guarantee fees or insurance premiums for the catastrophic Government backstop could be subject to similar inflation. It is important to base Federal guarantee/insurance charges on the universe of mortgage products and underwriting requirements that will be in place in the future rather than on products and protocols that are no longer in existence. Careful study should be undertaken to determine the level

[3] Laurie S. Goodman and Jun Zhu, "The GSE Reform Debate: How Much Capital Is Enough?" Urban Institute Housing Policy Center Paper, October 23, 2013.

of private capital and Federal guarantee/insurance charges that are needed for a safe, sound, and sustainable future housing finance system.

A Multifaceted Housing Finance System Is Needed

NAHB believes that the U.S. housing finance system should be multifaceted with both competing and complimentary components, including private, Federal, and State sources of capital liquidity. To ensure all markets are served, broad market participation should be encouraged. Barriers to entry to the secondary market should be a low as possible while balancing safety to the system. Compliance with regulatory requirements should not be more burdensome for smaller lenders—recognizing the unique role many small lenders have carved out for their communities.

To-Be-Announced (TBA) Market

The to-be-announced (TBA) market plays a critical role in maintaining a liquid secondary market for mortgage-backed securities (MBS). Fannie Mae, Freddie Mac, and Ginnie Mae securities make up the TBA market, and liquidity in these agency mortgage-backed securities is key to an efficient marketplace and affordable interest rates. Agency MBS are comprised of relatively homogenous mortgage loans with known underwriting criteria and standard documentation.

This well-defined marketplace supports the necessary fungibility to allow investors to buy and sell without the due diligence applied to non-TBA market securities and leads to the liquidity that is vital. TBA securities allow mortgage originators to lock-in interest rates to consumers by using the TBA securities to hedge their exposure to an increase or a decrease in interest rates before the mortgage loans close.

Reforms to the secondary market system should take into account the potential impact on the securitization of mortgage loans and the issuance and trading of MBS to insure the liquidity of the TBA market is not negatively affected.

Federal Home Loan Bank System

The Federal Home Loan Bank System (FHLBank System) is composed of 12 member-owned regional cooperatives chartered by Congress to provide reliable funding for housing and economic development to their members. Membership in the FHLBank System includes community banks, thrifts, credit unions, insurance companies and Community Development Financial Institutions (CDFIs). Each day the Federal Home Loan Banks (FHLBs) lend billions of dollars to member institutions through secured loans called "advances" to support the credit and financial needs of their members. Combined, the FHLBank System has 7,600 member institutions.

NAHB believes the Federal Home Loan Banks should continue to exist and provide their member institutions access to housing credit and liquidity. The FHLBs offered the housing market significant stability during the mortgage credit crisis when many banks were unwilling or unable to provide mortgage credit. NAHB has advocated for the FHLBs to capitalize on their acknowledged solid performance and risk management strength and seek to expand their role in housing finance as housing finance reform is considered.

Currently, the FHLBs can purchase mortgage loans from their member institutions but have only limited leeway to manage the resulting portfolios. NAHB believes the FHLBs would benefit from being allowed to aggregate loans from their members for sale to investors. A statutory change to allow the FHLBs to issue conventional mortgage-backed securities would significantly increase their value to members seeking enhanced access to the secondary market. In particular, small lenders would benefit from increased options for selling their loans to FHLBs rather than selling to large aggregators that may be less responsive and more expensive.

In fact, NAHB was very pleased to see the recent announcement by the Federal Home Loan Bank of Chicago that it will begin issuing Ginnie Mae securities backed by mortgages originated by its member institutions. This is extremely innovative and will provide the access to the secondary market that many of its member institutions currently lack.

Reform to the housing finance system must carve out a role for the FHLBs. NAHB would support an expanded role as long as any new lines of business, new mortgage programs, or statutory changes to the FHLB charters are considered carefully in order to avoid unintended consequences that might conflict with the FHLBs' existing authorities and primary activity of providing advances to members.

As we think about ensuring affordability in a reformed housing finance market, the Federal Home Loan Banks should continue to support affordable housing through their Affordable Housing Program (AHP). Since 1990, each FHLBank has been required by statute to put aside 10 percent of its net income each year toward grants for affordable housing. The AHP is designed to be local in nature. It is administered regionally by each FHLBank through its financial institution members and each member's community-based partners to insure the programs are designed to meet the specific needs of local neighborhoods.

Access by Community Banks

While not having the dominant share of mortgage originations, community financial institutions originate a significant volume of mortgage loans. During the first quarter of 2013, $435 billion of mortgages were originated nationwide. Community banks and thrifts with less than $10 billion in total assets originated $55 billion of residential mortgage loans during the first quarter of 2013.[4]

As the name implies, community banks offer financial services designed to meet the specific needs of their unique local markets. They are known particularly for serving rural areas and traditionally underserved markets. In the current environment of increased regulatory compliance requirements, tighter underwriting standards, and overall less availability of mortgage credit, it is important to be vigilant about the impact of housing finance reform on community banks and the mortgage borrowers they serve. Meeting the needs of their communities can mean these institutions are not originating standard products that can be sold in the secondary markets. This inability or difficulty to sell their loans to the secondary market can restrict their primary market activity.

Over the years, community banks have sold their loans to large aggregators, including Fannie Mae and Freddie Mac, and have paid higher fees based on smaller volumes. In a new housing finance system, access and pricing should not be based on the volume of business or size or geographic location of the selling institution.

Recently, community banks have been increasing their secondary market activity. Loans delivered to Fannie Mae and Freddie Mac by community banks have increased significantly from 2007 to 2012. For example, in 2007, only 3.6 percent of loans delivered to Freddie Mac came from outside the top 100 lenders. In 2012, this increased to 15.1 percent of all loans at Freddie Mac.[5] Access for community banks should be a priority when considering housing finance system reform.

The Corker-Warner bill acknowledges the importance of providing access to the secondary mortgage market to community banks. As proposed, Corker-Warner would create the Federal Mortgage Insurance Corporation (FMIC) which would be required to ensure that credit unions and community and midsized banks have equal access to the common securitization platform. The FMIC is authorized to create the Mutual Securitization Company to purchase, pool and securitize loans from insured depositories having less than $15 billion in assets or a nondepository mortgage originator having a minimum net worth of $2.5 million. NAHB supports Corker-Warner's provision to create a Mutual Securitization Company, which would be an approved issuer. However, as an issuer purchasing from small entities, its ability to compete with larger issuers should be carefully monitored to ensure a level playing field.

Housing Finance Agencies

NAHB believes State and local housing finance agencies should play an expanded role in providing housing funds. These agencies have proved critical in helping communities meet the needs of consumers who have faced hardships in the face of tight credit conditions.

State and local housing finance agencies utilize tax-exempt and taxable bonds as well as State and Federal resources to offer a range of single family and multifamily housing programs. These agencies are uniquely positioned to assess community housing needs and should play an even more prominent housing finance role through the development of new programs for new, for-sale housing and multifamily rental homes. This should include partnering with Federal and private providers of housing capital.

Single Family Housing

Retain Capacity of FHA To Meet Its Vital Housing Mission

The FHA single-family mortgage programs are a unique and vital component of the housing finance system, providing access to home ownership for underserved communities, primarily first-time homebuyers, minorities, and those with limited downpayment capabilities. During the recent mortgage crisis, FHA demonstrated how invaluable its countercyclical role was in providing mortgage market liquidity

[4] ABA Federal Home Loan Bank Member Insights, October 10, 2013, Vol. 4, No. 1.

[5] Statement of Sandra Thompson, Deputy Director for the Division of Housing Mission and Goals, Federal Housing Finance Agency; Subcommittee on Securities, Insurance, and Investment, U.S. Senate Committee on Banking, Housing, and Urban Affairs, July 23, 2013, pp. 4–5.

as FHA's share of the market jumped from 3 percent during the housing boom to a high of almost 30 percent early in the crisis. Nearly 80 percent of FHA's purchase loans have been to first-time home buyers. This dramatic shift is evidence that FHA is performing its mission of providing the Federal backstop to ensure that every American has access to a stable mortgage product. In times of crisis, private sources of mortgage credit have demonstrated they are unable or unwilling to meet housing capital needs.

NAHB supports efforts to reform FHA and understands that this is not a simple undertaking. However, reform must be approached with caution. Since 2010, FHA has implemented a series of policy changes, including higher mortgage insurance premiums, tighter underwriting requirements, stricter mortgage lender enforcement, and improved risk assessment, all intended to strengthen the performance of the Mutual Mortgage Insurance Fund (MMIF) and rebuild the capital reserve ratio. These changes are the most sweeping combination of reforms to credit policy, risk management and lender enforcement in FHA history. Further changes to FHA's programs cannot be separated from the larger discussion of reforming the complex housing finance system to ensure homebuyers have affordable financing solutions.

NAHB urges Congress to proceed carefully and not significantly alter FHA's role of providing affordable single family financing. We are concerned that several of the provisions in H.R. 2767 (PATH Act) would greatly reduce the scope and reach of FHA's programs. In particular, NAHB opposes provisions in the PATH Act that would limit FHA's single family programs to first time or low- and moderate-income home buyers, increase downpayments, and reduce the minimum FHA mortgage limit or floor. These proposals would have a detrimental impact on FHA's ability to serve its mission and facilitate the flow of mortgage credit to its targeted borrowers.

Provide a Reasonable Menu of Conventional Mortgage Products

America's future housing finance system must be designed to ensure that creditworthy borrowers have access to a reasonable menu of conventional mortgage products that are prudently developed and appropriately underwritten. While standardized product features and underwriting requirements are necessary to ensure liquidity, these mortgage products must also have practical flexibilities to meet the diverse financial needs of first-time homebuyers, minorities, buyers with limited downpayment capabilities, and move-up buyers.

Research suggests that the greatest obstacle faced by potential first-time homebuyers, especially low-income, minority individuals and families, is not the ability to make monthly mortgage payments, but rather the ability to assemble enough funds to pay the downpayment and closing costs. Because of the financial downturn, many more potential homebuyers will have the ability-to-repay but will need affordable downpayment conventional mortgage products.

Maintain Role of Mortgage Insurance Industry

Private mortgage Insurance (MI) companies provide a vital component of our country's residential mortgage finance system by protecting mortgage investors from credit losses. Mortgage insurance also benefits home buyers by helping them achieve home ownership earlier with low-downpayment loans.

Mortgage investors require healthy counterparty risk mortgage insurance partners, and both will need to continue to form strong partnerships to serve borrowers with well underwritten, competitively priced and flexible MI programs to ensure the availability of 95 percent loan-to-value (LTV) mortgage products.

Another benefit to this type of counterparty risk arrangement is that the loan is underwritten by both the mortgage investor and the MI company. This due diligence helps to ensure the consumer's ability-to-repay. MI companies are also providers of homeowner assistance programs that go well beyond the initial purchase of their home.

Preserve Rural Housing Service and Veteran's Administration (VA) Loan Programs

The Federal Government historically has played an important role in providing mortgage credit to rural areas. The National Housing Act of 1949 authorized the Farmers Home Administration to issue mortgages for the purchase and repair of single family homes in rural areas and to provide financing and rental assistance for multifamily rental housing. Later legislation moved this function to the Rural Housing Service (RHS), which is part of the U.S. Department of Agriculture (USDA).

Section 502 housing loan guarantee programs provide well underwritten loan programs to low- and moderate-income individuals and families without having to make a downpayment because they may borrow up to 100 percent of the appraised value of the home. Since a common barrier to owning a home for many is the lack of funds to make a downpayment, this program makes the possibility of owning a home a reality for many Americans in rural communities.

The VA home loan guarantee program is an integral component of housing finance and is an outstanding example of a how a low- to no-downpayment program can perform even in difficult economic markets. The VA attributes its track record of success to strong principles of underwriting loans and high-touch service for its veterans throughout the mortgage process.

Appraisal System Reform

The current residential appraisal system is impaired due to inconsistent and conflicting standards and guidance; inadequate and uneven oversight and enforcement; a shortage of qualified and experienced residential appraisers; and, the absence of a robust and standardized data system. NAHB believes these problems must be addressed in order to restore confidence in the residential real estate market and to establish a foundation for sustainable growth of the U.S. economy. This can only be accomplished through sound valuation practices, policy, and procedures that produce more credible valuations under all economic circumstances.

In 2012, NAHB formed an Appraisal Working Group (AWG), consisting of home builders and representatives from the financial and appraisal sectors, to develop recommendations for comprehensive appraisal reform and produced a White Paper with specific recommendations.[6] In this process, there was extensive dialogue with all stakeholders in the residential appraisal process. The AWG continues to meet and discuss the importance of appraisal reform and below are their key recommendations:

- Reform the regulatory framework for real estate valuation to more effectively oversee standards, guidance, and enforcement.

The goal is to better integrate and streamline the jumble of existing entities to ensure the valuation of collateral in housing finance transactions occurs in a coordinated and effective manner. This would contribute to uniform and consistent standards and avoid the current multitude of conflicting and confusing requirements. In particular, urgent steps should be taken to improve the effectiveness and consistency of State appraisal oversight.

- Develop and build a real estate data superhighway with a national real property registry and supporting networks.

The development of a real estate database would facilitate the safe and efficient transfer of real property. The reformed regulatory system would be responsible for the establishment of standards for data, methodology and practice. Stakeholders would be able to view all valuations, and secondary market participants would have access with proper rights established. Access rights would be granted to any registered purchaser, securitizer, or servicer.

- Establish a single, consistent set of rules and guidelines for appraisers and appraisals and set standards to ensure the engagement of an appraiser who has the training and experience necessary for the assignment.

The establishment of a single set of rules and appraisal forms should be incorporated as a high priority as part of housing finance system reform. Currently, Fannie Mae and Freddie Mac impose de facto appraisal authority through the guidelines they have established for appraisals on the mortgages they purchase and the forms they use to collect appraisal information. These Enterprise appraisal rules tend to restrict appraisers' ability to pursue approaches that could result in more accurate valuation. In addition, confusion arises in how to interpret the Enterprise appraisal guidelines in relation to the rules established by The Appraisal Foundation (TAF) in the Uniform Standards of Professional Appraisal Practice (USPAP) and the appraisal regulations of the banking regulators.

In addition, there have been reports of appraisal problems due to appraisers not being familiar with the area in which the subject home is located and not having experience in valuing the type of property in question. This is a particularly acute issue for builders and purchasers of newly constructed homes, which normally require more extensive analysis and research. Standards and processes should be established to ensure appraisers have the training and experience needed to provide an accurate property valuation.

- Develop a workable process for appealing inaccurate or faulty appraisals.

[6] "A Comprehensive Blueprint for Residential Appraisal Reform", National Association of Home Builders, February 2013.

It is extremely important to establish a timely value appeals process that is fair, balanced, and appropriate to allow all parties of the transaction to appeal appraisals that do not meet USPAP standards or are based on inaccurate data or assumptions.

Today's residential appraisal system remains in a state of uncertainty. The current patchwork system cannot continue indefinitely. A key consideration must be to establish stability and restore confidence in the system that determines the value of mortgage collateral. NAHB remains committed to residential appraisal reform and looks forward to working with industry stakeholders to address the problems and implement solutions to the current U.S. residential appraisal system.

Multifamily Housing

Future Conventional Multifamily Finance System

NAHB and several of the most prominent trade associations representing multifamily developers, owners, property managers, and lenders have prepared a set of principles under which we believe the future multifamily finance system should be framed. (The set of principles accompanies this statement.)

Key principles include:

- The Nation's multifamily housing finance system should rely primarily on private capital.
- The Federal Government is the only entity that can ensure the availability of liquidity in all market cycles, and the appropriate mechanism to do that is through a catastrophic backstop role.
- The Government guarantee-related market should be subject to strong and independent regulatory oversight and risk-based capital requirements.
- Policy makers should protect and preserve existing resources, as well as support greater transparency, during the transition to an overhauled housing finance system.

NAHB cautions against overreaching in regard to reforming the multifamily finance system. This component of the Nation's housing finance system has performed, and continues to perform, very well. NAHB does not believe it is necessary to take draconian steps that are not needed to "fix" an unbroken system. Such steps would include setting income or rent restrictions on loans as a condition of access to a Federal Government backstop, standardizing products, or requiring only one securitization platform. Again, NAHB believes that the critical consideration in a new system is broad and continued liquidity during all economic cycles and for all geographic areas.

Preserve Successful Infrastructure, Products, Programs From Conventional Market

As noted earlier, in spite of the crisis affecting single family housing, the multifamily sector has performed well. Multifamily loans held or guaranteed by Fannie Mae and Freddie Mac have very low default rates, and both businesses are profitable. Both of the Enterprises' multifamily businesses involve risk-sharing with private capital, and both businesses have practiced disciplined underwriting. In addition, because of the range of products and business lines employed by the Enterprises, a wide range of multifamily rental properties that provide housing for very-low to middle income households can be financed in the conventional market. NAHB strongly supports retention of the successful infrastructure, products and programs that have been built over the years by the Enterprises and which are used as the core of most of the major financial institutions providing multifamily debt financing.

NAHB is thus alarmed at recent actions taken by FHFA related to the Enterprises' multifamily businesses. In an August 2013 press release, FHFA stated it was seeking input on strategies for reducing the Enterprises' presence in the multifamily housing finance market in 2014. FHFA's Strategic Plan for Enterprise Conservatorships, released in February 2012, included a goal to contract the Enterprises' presence in the market while simplifying and shrinking certain operations. The 2013 conservatorship Scorecard included reducing their volume of new multifamily business by 10 percent relative to 2012. FHFA expects this reduction to be achieved this year through a combination of increased pricing, more limited product offerings and stronger underwriting standards. FHFA stated its intention to continue a path of gradual contraction of the multifamily businesses while awaiting a legislative resolution to the conservatorships.

It is disturbing to NAHB that FHFA is taking these steps in the absence of direction from Congress. NAHB believes that the FHFA's directive to the Enterprises to reduce their multifamily businesses is arbitrary and unnecessary. In fact, NAHB strongly believes that it is critical that the Enterprises retain their ability to provide broad liquidity to the market, which includes having a diversified line of products and the ability to address financing for a large range of multifamily property types.

This critical aspect of the Enterprises' mission—to provide liquidity during all economic cycles—should not be regulated by the conservator; that is the job of Congress. To lose any of the successful products or business activities at this point in time—before decisions are made by Congress as to the future of the multifamily housing finance market—means they may have to be rebuilt at a future point. NAHB has urged FHFA not to take unwarranted actions that will result in damage to the multifamily market now and in the future, and NAHB urges members of Congress to convey the same message to FHFA.

Private Market Participants Are Selective Investors

It is important to understand that not all private market sources of capital for multifamily financing are available for all segments of the multifamily market. Each has strength in specific niches and markets and thus moves in and out of the market as economic conditions and their investment goals change. Life insurance companies typically target low-leverage, high-quality deals in the strongest markets (usually urban) and typically serve the highest income households. Once they meet their own portfolio investment targets, life insurance companies retract their lending. Banks do not provide long-term financing and are subject to significant restrictions in terms of capital requirements. Banks also have significant exposure to regulatory pressure that influences their lending decisions, including obligations under the Community Reinvestment Act (CRA). While the commercial mortgage backed securities (CMBS) market was significant at one time, it has not recovered from the financial crisis and is not expected to resume its past levels of volume.

These facts point to the need to maintain a viable, liquid and efficient secondary market for multifamily rental financing where the Federal Government continues to play a role. In addition, the secondary market must be structured to ensure that the appropriate range of products is available to provide the capital needed to develop new and to preserve existing rental housing, as well as to refinance and acquire properties. An adequate flow of capital will ensure that demand for rental housing is met and that affordable options are available for a range of households and communities.

Legislative Proposals

NAHB appreciates that S.1217, the Housing Finance Reform and Taxpayer Act of 2013, introduced by Senators Corker and Warner, recognizes the importance of the Enterprises' multifamily businesses. The bill would transfer both multifamily businesses to the newly created Federal Mortgage Insurance Corporation (FMIC). However, NAHB does not believe it is practical for the regulator to absorb and run the multifamily businesses. A more practical option is to transition the Enterprises' multifamily businesses to private entities, which would then be allowed access to the Federal Government guarantee through FMIC.

The House Financial Services Committee-passed bill, H.R. 2767, the Protecting American Taxpayers and Homeowners Act of 2013 (PATH Act), does not address the multifamily conventional market at all, which is a major omission.

Maintain FHA's Multifamily Capacity

FHA historically has played an important role in the financing of multifamily rental housing, and it was especially important during the economic crisis. FHA provides an explicit Federal Government guarantee on multifamily loans for which borrowers pay a mortgage insurance premium set by HUD. The FHA multifamily loans have performed well with low default rates (as published by HUD in May 2013), and the programs generate significant revenue to the Federal Government in the form of a negative credit subsidy, generating positive cash flow to the U.S. Treasury.

In 2008, FHA endorsed just over $2 billion in multifamily loans (excluding health care programs), which grew to $18.3 billion (excluding health care programs) in FY2013. This unprecedented increase in FHA multifamily loan volume occurred as other private market sources of multifamily financing withdrew from the market when economic conditions worsened. FHA, along with Fannie Mae and Freddie Mac, became the primary sources of multifamily financing as the recession deepened. Like in the single family market, the FHA multifamily mortgage insurance programs are fulfilling the function and mission for which Congress originally intended.

NAHB has long-supported these programs, notably Section 221(d)(4) and Section 223(f), which have enabled the construction of new affordable and market rate rental housing units, as well as the acquisition, refinance, and rehabilitation of the Nation's existing stock of rental housing. Of importance, FHA financing is often used in smaller markets where Fannie Mae, Freddie Mac and other market participants are less active, and FHA has filled the niche that local banks and thrifts have retreated from in recent years.

Risk Management Protocols

It is important to note that over the last 3 years, HUD has instituted new risk management protocols for the FHA multifamily mortgage insurance programs. The new protocols tightened underwriting requirements, created a national loan review committee, and strengthened policies related to large loans, sponsor creditworthiness, and experience. There is closer scrutiny on market strength and FHA presence than before the economic crisis. In 2012, for the first time in 10 years, HUD raised the mortgage insurance premiums (MIPs) for programs in the General Insurance/ Special Risk Insurance (GI/SRI) fund. All of these actions were intended to strengthen risk management practices related to the FHA multifamily mortgage insurance programs, ensure the health of the GI/SRI fund, and attract high quality borrowers, without taking market share from the private sector or endangering taxpayers.

HUD's most recent step towards increasing efficiency and standardizing policies across field offices was the announcement of a major restructuring of the Office of Multifamily Programs. The restructuring in the Office of Multifamily Programs will consolidate its program Hubs and field offices and reorganize the offices within its headquarters in Washington, DC. The goal of the restructuring is to allow more consistent, efficient processing of loans and servicing of existing assets.

NAHB has testified previously that, as important as these steps have been towards increasing risk management, the FHA multifamily field offices continue to struggle because of inadequate staffing and resources. NAHB is supportive of HUD's efforts to address these difficult issues, and we urge members of Congress to ensure that the department has the resources it needs to safely and properly manage its large portfolio and to ensure that the programs remain strong and viable.

Commitment Authority

NAHB recently expressed strong concern to members of Congress that the uncertainty related to the availability of commitment authority for the FHA multifamily programs creates the potential for major disruptions in financing much needed affordable and market-rate rental properties, as well as health care facilities, which are also included under the GI/SRI fund. FHA exhausted its commitment authority for FY2013 in mid-September, which forced borrowers to wait until new authority became available before they could be assured of a loan commitment. As a result, affordable housing construction and other related jobs have been delayed, and in some cases, may not even go forward. The Government shutdown only made the situation worse, as the queue of loans waiting for commitment authority accumulated rapidly and is now in excess of one-half billion dollars.

NAHB suggests that an area of reform for the FHA multifamily and health care insurance programs is to consider giving FHA multiyear commitment authority, as is the case with the FHA single family programs. Another option would be to devise an automatic trigger of additional commitment authority if certain conditions are met to ensure the uninterrupted operation of the programs during all economic cycles.

Legislative Proposals—The PATH Act

NAHB is concerned about proposals to more narrowly limit FHA's current mission. The PATH Act would allow FHA to provide mortgage insurance for residential properties having five or more dwelling units—multifamily rental housing—subject to occupancy and rent restrictions applied during the life of the mortgages. The bill restricts occupancy to families having incomes no greater than 115 percent of area median income (AMI). It allows for higher income limits (up to 150 percent of AMI) in high cost areas. The bill gives FHA the discretion to establish lower occupancy, income and rent restrictions.

NAHB does not support setting occupancy and rent restrictions based on AMI for the FHA multifamily mortgage insurance programs. The Census Bureau's 2012 Rental Housing Finance Survey shows that an overwhelming majority of tenants in properties with FHA-insured mortgages have incomes of 115 percent or less of area median income. However, the FHA multifamily mortgage insurance program is also a key source of liquidity, so the imposition of income limits would impede that portion of FHA's mission, particularly in higher-cost markets.

The FHA multifamily mortgage insurance programs are subject to statutory mortgage loan limits, which effectively serve to focus the provision of FHA multifamily mortgage insurance on affordable and workforce rental housing. Imposing burdensome provisions that require developers, lenders, and property managers to track and document incomes and rents on unsubsidized properties is costly and unnecessary, given that the proposed targeted population is already being served by the programs.

The PATH Act also requires the Director of FHFA to set capital reserve requirements for the GI and SRI funds. The bill does not specify target reserve ratios. Currently, there are no statutory requirements for capital ratios for either the GI or SRI funds. While NAHB understands that members of Congress and the Administration are focused on strengthening the risk management practices for both the single and multifamily FHA programs, NAHB strongly urges that an in-depth analysis is conducted to determine any impact on the mortgage insurance premiums for the FHA multifamily programs before any reserve requirements are considered. NAHB does not believe that it is appropriate to use the type of capital reserve ratios used for the MMIF for the GI/SRI fund, because the nature of the multifamily portfolio is significantly different from the single family portfolio insured under the MMIF.

The implementation of a capital reserve on the GI/SRI funds could have significant impacts on MIPs. Higher MIPs will lead to higher costs for borrowers and renters who are served by the FHA multifamily programs. A key example is the Section 221(d)(4) program where a higher MIP will raise the required borrower debt service and/or equity contribution, resulting in a lower mortgage amount at a higher rate of interest. These higher costs would be passed along in the form of higher rents to the low- and moderate income families who reside in rental units financed through the program or could result in properties not being built or rehabilitated because of the higher equity contribution required.

Need To Address Rural and Small Rental Projects

Over the years, NAHB has discussed with FHA and the Enterprises the need to develop more options for small multifamily financing (typically defined as 5 to 49 units) and to address credit needs in rural areas. According to HUD, almost a third of the Nation's renters, more than 20 million households, live in small, unsubsidized housing. These properties tend to be owned by individuals (mom-and-pop owners), as well as small businesses. Rents charged at such properties are typically more affordable to low- and moderate-income families.

Owners of small multifamily properties do not have many options for financing acquisitions and/or rehabilitation work. Many lenders view such loans as high risk, and the costs of underwriting the loans are more expensive for both the lender and borrower. In addition, servicing costs for such loans are high, reducing lenders' incentive to make them. Small loans are not easily securitized, as it takes too long to accumulate the volume needed to issue a security.

The Enterprises have struggled with this type of loan, and FHA has not been successful at developing a viable small loan program. Although many local commercial banks are active in lending for small multifamily properties, the availability of financing is not very consistent. Large banks without a presence in rural areas have no Community Reinvestment Act (CRA) incentive to invest in such properties. Some State housing finance agencies address this need through set-asides for rural areas, where many small multifamily properties are located. A few NAHB members have been successful in refinancing a small portfolio of properties into one loan, which helps reduce costs.

HUD is currently exploring an expansion to its FHA risk-sharing program that would allow mission-based financial institutions to enter into risk-sharing arrangements with FHA to provide acquisition and rehabilitation financing for small multifamily properties. HUD is seeking a legislative change that would allow Ginnie Mae to securitize such loans. NAHB believes there is potential in this effort and has participated in several discussions with HUD and other stakeholders. NAHB urges Congress consider the legislative changes that are needed to develop a viable program.

As mentioned previously, the Corker-Warner bill acknowledges the importance of providing access to the secondary mortgage market to community banks. The proposed Federal Mortgage Insurance Corporation could provide opportunities for small multifamily lending.

Reform and Adequately Fund HUD's Rental Assistance Programs

HUD provides rental assistance to over five million households. Sixty-five percent of HUD-assisted households are elderly or disabled, and HUD-assisted families had an average income of $12,500 in 2012. Just one in four families that needs rental assistance is able to receive it because there are not enough resources to help everyone. The rental assistance programs have been under stress due to rising costs and the difficult economy. There are many potential areas for reform, yet agreement on how to proceed remains elusive. A major problem is the whipsaw of funding levels, which creates great stress on property owners, public housing agencies and residents.

Section 8 Housing Choice Voucher Program

NAHB has long supported the Section 8 Housing Choice Voucher program, which provides rental subsidies to approximately two million very-low income households who obtain housing in the private rental market. The program, which is intended to broaden the range of housing choices for families seeking affordable housing, has proven to be effective in helping low income families find decent, safe, and affordable housing. In addition, the rental vouchers can be leveraged to build or rehabilitate additional affordable housing, a necessity in today's tight rental markets.

In recent years, the program has been the subject of policy discussions because of its growing costs and strain on the HUD budget. Funding levels have fluctuated, causing public housing agencies (PHAs) to struggle to maintain assistance to current tenants. A major reform bill first introduced in 2004 has been revised and debated without moving to passage. The goals of the most current House version, the Affordable Housing and Self Sufficiency Improvement Act of 2013 (AHSSIA), are to reduce taxpayer costs within HUD's rental housing programs and facilitate greater private-sector participation in affordable housing. Streamlining aspects of the program will reduce costs and improve the delivery of services to the households seeking affordable housing. Private property owners will be more amenable to participating in HUD's affordable housing programs, as well, as the administrative burdens are eased and costs to participate are lowered.

NAHB, along with a large group of industry stakeholders, has identified a core set of reforms to the program. Included are reforms that would streamline various processes, including: unit inspections; rent calculations; income determinations; and tenant screening. Other reforms would improve the voucher funding allocations to make them more stable and predictable while still permitting appropriators to set overall annual funding levels. While some additional improvements could be included, NAHB and stakeholders agree that it is important to move forward quickly on these consensus reforms.

Section 8 Project Based Rental Assistance Program (PBRA)

The Section 8 Project Based Rental Assistance Program (PBRA), which provides rental subsidies directly to property owners for specific properties, is at risk due to inadequate funding while costs are rising. The budget sequester that became effective on March 1, 2013, resulted in a cut of $470 million for the PBRA program in FY2013. HUD had to issue a letter to owners outlining its plans to manage the program due to the reduced funding, which included providing less than 12-months of funding to owners with expiring contracts. The shortfall becomes worse in FY2014 when 15,900 contracts (1.1 million units) will be up for renewal. HUD acknowledges that all contracts will be have to be less than 12-month funding due to an anticipated shortfall of over $1 billion.

The consequences of this funding uncertainty every year are many: property owners may stop participating in the program because of the uncertainty revolving around appropriations; property owners who continue may have to defer needed maintenance or reduce contributions to reserves, which means residents may lose good quality housing; lenders may be reluctant to provide financing for the rehabilitation of these properties because of the uncertain revenue stream. NAHB strongly supports adequate and predictable funding for the PBRA program.

USDA Rural Housing Service (RHS) Multifamily Programs

The USDA administers multifamily housing programs that help finance rental housing in rural areas. The Section 515 direct loan program provides long-term, low interest loans to nonprofit and for-profit developers to support the construction, acquisition and rehabilitation of multifamily housing for low- and moderate-income renters. The program has financed over 15,500 properties with 443,150 units, with the average property consisting of 28 units. The USDA's Section 521 Rental Assistance (RA) program is project-based and provides rental subsidies to properties that were financed through USDA's Section 515 multifamily direct loan program. The majority of residents living in these properties are elderly, and average annual incomes are below $11,000.

Yet this valuable source of affordable rental housing for low-income rural families is in jeopardy of being lost. Section 515 funding has been cut drastically; the Section 521 RA program is experiencing a shortfall of funds due to sequestration, causing some property owners to have to take drastic steps to find funds to cover the shortfall for FY2013. It is very possible another shortfall will occur in FY2014, absent Congressional action. Property owners will not be able to maintain their properties without the RA funds and may be forced at some point to exit the program.

NAHB believes it is critically important that Congress take action to provide the funding needed to preserve this important portfolio of rural rental housing and to ensure that residents will continue to have affordable, decent and safe housing. However, funding is not the only issue; legislative action is needed to authorize a viable preservation program for the portfolio, as well as to consider what steps need to be taken to ensure the RA program can be sustained over the long term.

National Housing Trust Fund and Other Government Funding Programs

Housing Trust Fund

S.1217 includes provisions to fund the National Housing Trust Fund (HTF) and to make some modifications to its purpose and eligible uses. The HTF was first created by the Housing and Economic Recovery Act of 2008 (HERA) and was to be funded by the Enterprises. However, the Enterprises went into conservatorship shortly after passage of HERA, and the conservator determined it was not in the interests of safety and soundness to allow the Enterprises to transfer funds to the HTF.

S.1217 imposes fees on single and multifamily securities accessing the Federal guarantee through the proposed Federal Mortgage Loan Corporation (FMIC), which would be transferred to the HTF. Eligible activities would include grants and loans that support sustainable home ownership and rental housing for households for a range of households. S.1271 also includes a provision to ensure rural areas get proportionate shares of money and that States give priority to nonentitlement areas (population less than 20,000).

These provisions are consistent with NAHB's position on the purposes and uses of a national housing trust fund. NAHB believes that the purposes of a HTF should be broadly defined to include allowing a significant spectrum of eligible activities and with income targeting requirements that allow grantees and grant recipients to meet the fullest range of critical housing needs. It is important that the funds also meet the needs in rural and underserved areas. Also, NAHB believes that the statutory and regulatory framework of the HFT must allow for the effective and efficient use of trust fund monies in conjunction with other Federal and State housing programs, particularly the HOME Investments Partnership Program and the Low Income Housing Tax Credit (LIHTC) program.

Finally, NAHB strongly believes that eligible recipients must include both for-profit and nonprofit developers, and all recipients must be able to demonstrate that they have the necessary experience and capacity to carry out proposed projects. Adequate standards of experience and capacity for grant recipients should be required, along with results-focused allocation criteria, to ensure the best possible use of these valuable resources.

Role of the Home Investment Partnerships Program and Community Development Block Grants

NAHB has long supported the HOME Investment Partnerships Program and Community Development Block Grant (CDBG) programs. These two programs provide invaluable support to cities, counties, and rural areas in meeting their affordable housing and community development needs. The HOME program has been essential in providing gap financing for affordable rental housing financed with Low Income Housing Tax Credits, as well as for home ownership for first-time and low-income homebuyers. CDGB funds may be used to provide needed infrastructure that supports housing, such as sidewalks and streets, but also community centers, day care centers, and other important community assets.

Both programs have suffered deep budget cuts. NAHB has consistently supported adequate funding for both programs and has also supported reforms that would ensure the funds are spent efficiently and effectively. NAHB has also supported efforts to streamline the use of HOME funds with other Federal housing programs, especially those administered by State housing finance agencies (such as the LIHTC) and the USDA RHS.

Low Income Housing Tax Credit Program

The Low Income Housing Tax Credit (LIHTC) is the most successful affordable rental housing production program in U.S. history. It was created as part of the Tax Reform Act of 1986 as a more effective mechanism for producing affordable rental housing. Since its inception, the LIHTC has produced and financed more than two million affordable apartments. As LIHTC properties must generally remain affordable for 30 years, they provide long-term rent stability for low-income households around the country.

However, the demand for affordable housing is acute and exceeds the availability of financing through the LIHTC program. According to the most recently available annual survey released by the National Council of State Housing Agencies (NCSHA), State housing finance agencies generally receive $2 in requests for every $1 in LIHTCs available. At the same time, the supply of private, affordable housing stock is rapidly shrinking. Of the 6.2 million vacant or for-rent units with rents below $400 in 1999, 11.9 percent were demolished by 2009. Upward filtering to higher rent ranges, conversions to seasonal or nonresidential use, and temporary removals because of abandonment added to the losses. On net, more than 28 percent of the 1999 low-cost stock was lost by 2009.[7]

NAHB strongly urges Congress to maintain this critical affordable rental housing program.

Importance of a Reliable Supply of Affordable Acquisition, Development, and Construction Credit

A significant factor in the availability and cost of home ownership and rental housing is the cost and availability of the credit required to produce such housing. This credit is referred to as land acquisition, development, and construction (AD&C) financing. Affordable housing needs cannot be met by solely through utilization of the existing housing stock. This is particularly true if affordability is defined to include the cost of operating a home. Builders of new housing are required to meet increasingly stringent energy efficiency standards, which make new homes considerably less expensive to live in than older existing units. Also, new home construction occurs to satisfy consumer demand driven by lifestyle and location preferences such as urban living, multigenerational homes, and fifty-plus communities. Therefore, significant levels of production of new homes will be needed to meet future housing needs in choices.

Since the affordability of newly constructed homes is affected by the availability and cost of AD&C loans, it is important to ensure that this form of financing is available at reasonable rates and terms. The home building industry is predominantly made up of small businesses and, currently, these companies are having difficulty in obtaining AD&C loans. These home building companies have traditionally relied on community banks for AD&C loans, but those institutions have been under severe regulatory pressure to curb their AD&C lending and reduce the concentration of such loans in their portfolios.

NAHB appreciates the efforts of Senator Robert Menendez (D-NJ) and Sen. Johnny Isakson (R-GA) for introducing The Home Building Lending Improvement Act of 2013 (S.1002) that would address several of these regulatory barriers to sound construction lending. NAHB looks forward to working with this Committee to advance regulatory reform in this area. Going forward, it does not seem likely that community banks will again resume the levels of AD&C lending previously undertaken unless some form of secondary market outlet is created to allow these institutions to sell their AD&C output and obtain liquidity for additional lending.

Conclusion

NAHB thanks the Committee for the opportunity to submit its views on essential elements to provide affordable options for housing. Whether they rent or own, Americans want to choose where they live and the type of home that best meets their needs. Given the significant role that housing plays in the economy, we urge Congress to take a long-term, holistic approach to housing finance reform. NAHB also urges Congress to carefully consider the differences between the single family and multifamily market and not apply solutions to one piece of the market that are not appropriate for the other. NAHB thanks the Committee for its leadership on this important issue, and stands ready to work with you to achieve such reforms and provide much-needed stability for this critical sector of the economy.

PREPARED STATEMENT OF SHEILA CROWLEY

PRESIDENT AND CEO, NATIONAL LOW INCOME HOUSING COALITION

NOVEMBER 7, 2013

Chairman Johnson, Ranking Member Crapo, and Members of the Committee, thank you for the opportunity to testify today on the issues of affordability in housing finance reform and in particular on the National Housing Trust Fund.

I am Sheila Crowley, President of the National Low Income Housing Coalition (NLIHC). NLIHC is dedicated solely to achieving socially just public policy that

[7] "America's Rental Housing: Meeting Challenges, Building on Opportunities", Joint Center for Housing Studies of Harvard University, 2011. P. 6. *http://www.jchs.harvard.edu/publications/rental/rh11__americas__rental__housing/AmericasRentalHousing-2011.pdf*

assures people with the lowest incomes in the United States have affordable and decent homes.

Our members include nonprofit housing providers, homeless service providers, fair housing organizations, State and local housing coalitions, public housing agencies, private developers and property owners, housing researchers, local and State Government agencies, faith-based organizations, residents of public and assisted housing and their organizations, and concerned citizens. We do not represent any sector of the housing industry. Rather, NLIHC works only on behalf of and with low income people who need safe, decent, and affordable homes, especially those with the most serious housing problems, including people who are homeless. NLIHC is funded entirely with private contributions.

We organize our work in service of three overarching goals for Federal housing policy:

- There will be no further loss of federally assisted affordable housing units or Federal resources for affordable housing or access to housing by extremely low income people.
- The Federal Government will increase its investment in housing in order to produce, rehabilitate, and/or subsidize at least 3,500,000 units of housing that are affordable and accessible to the lowest income households in the next 10 years.
- Housing stability in the neighborhood of one's choice, which is foundational to good health, employment, educational achievement, and child well-being for people with the lowest incomes, will be the desired outcome of Federal low income housing programs.

The Committee's work on housing finance reform has largely focused on how home mortgage financing should be structured and what role the Federal Government should play. These are thorny, complex issues of great importance to the American economy and to all facets of the housing and lending industry. But the reason that the Federal Government should be and is involved in the housing finance system is to make sure that the U.S. housing sector works for all people in our country, not just for the most fortunate.

I am here today to ask that you provide for the least fortunate in the legislation under consideration, people for whom the housing market does not work, people who cannot be reached through existing publicly funded low income housing programs because the need far exceeds the resources. Specifically, I ask that you protect and fund the National Housing Trust Fund in your bipartisan bill.

Since 2000, NLIHC has led the National Housing Trust Fund campaign, a movement of more than 7,000 national, State, and local organizations located in every Congressional district. We celebrated when the National Housing Trust Fund was created in 2008 as part of the Housing and Economic Recovery Act (HERA). We are grateful to Senators Corker and Warner and the other cosponsors for including the Housing Trust Fund in S.1217, just as we are grateful to Senator Reed for his authorship of the Housing Trust Fund provisions in HERA and to Senators Shelby, Crapo, Corker, Johnson, Schumer, Menendez, Brown, Tester, and Warner for their support of the Housing Trust Fund as part of HERA in 2008.

Each of us knows how important home is to us, to every aspect of our well-being. We only have to imagine what it would be like to be displaced even for a few days to realize how essential our homes are to our health and happiness. Imagine what it would be like to be without a home, or to be afraid you will lose your home, or to be consigned to a home that was cold or dangerous. Then imagine trying to care for your children under those circumstances. Imagine being a child growing up without a secure and safe home.

There is a growing body of research that validates what we all tacitly understand: home matters to who we are, how we learn, how we feel, and how we perceive the world around us. I have a picture in my office of a 9-year-old child who, when asked what home means to her answers, "home is important as water and air."

If it is the business of this Congress to look out for the well-being of all your constituents, and I believe it is, then you are obligated to do everything within your power to make sure everyone in our country has a decent and affordable home in which to grow up, in which to raise a family, from which to go out from and return to each day, and in which to grow old with dignity.

Why We Need a National Housing Trust Fund

All housing markets are local, but there is one fact that is true in every community in the country. No community has a sufficient supply of decent rental homes that are affordable to extremely low income families, defined as having incomes at or below 30 percent of the area median.

Thirty-one percent of the households in South Dakota [1] are renters; the average renter in South Dakota has income of $20,176 a year. The annual household income needed to afford a modest two-bedroom rental home in South Dakota is $26,665. An extremely low income family in South Dakota has an annual income of $18,784 or less. [2]

In Idaho, 29 percent of all households are renters and the average renter earns $21,902 a year. The minimum income needed to afford a modest two-bedroom rental is $27,593 a year, but extremely low income in Idaho is $16,932 or less. [3]

Who has incomes that low? They are service workers—retail clerks, day care workers, home health care aides—the people on whom the rest of us depend to get our jobs done. They are waitresses, day laborers, farm workers, and office cleaners. They are people who are elderly or with disabilities, whose income is primarily Supplemental Security Income (SSI). The annual income of an SSI recipient in South Dakota is $8,556; in Idaho, it is $9,012. South Dakota and Idaho are among the 21 States that supplement the Federal SSI level. [4]

In 2011, there were 10.1 million extremely low-income renter households in the United States and only 5.5 million homes renting at prices they could can afford. This is the only income group for whom there is an absolute shortage of homes. Worse, many of the homes renting in the price range that an extremely low-income family could afford are in fact occupied by higher-income people. The real shortage for this income group is 7.1 million units. Nationwide, there are just 30 homes that are available and affordable for every 100 extremely low-income renter households. [5]

The most important thing to know about the housing shortage for poor Americans is that it gets worse each time it is measured and the number has skyrocketed in the Great Recession. HUD reports that the number of households with worst case housing needs (households with incomes less than 50 percent of the area median and who pay more than half of their income for their homes) increased by 43 percent between 2007 and 2011. [6]

These findings are confirmed by everyone who studies the housing gap. Other recent analyses that I recommend the Committee review are by the Joint Center on Housing Studies of Harvard, [7] the Bipartisan Housing Commission, [8] and former FHA Commissioner John Weicher. [9]

These data tell the story of families in your communities who have to choose to pay for food or heat, coats or medicine, and often get behind on the rent anyway and lose their homes. Then they have to move in with someone else or end up sleeping in their cars. I just heard from a service provider in rural Michigan about families living in deer blinds. Next time you are home, ask a local principal how many homeless children are enrolled in his or her school.

Homelessness is the most tragic manifestation of this housing shortage. In this very dangerous game of musical chairs, the people who are most likely to end up with no housing at all are those who are the poorest, the most vulnerable, those with the weakest support systems and the fewest coping skills. Although, we have made progress in reducing the number of veterans and people with chronic illnesses who are homeless, there has been an explosion in the number of homeless families with children in this recession. There are over 20,000 homeless children in New York City alone. Surely, we can do better than this.

The people who conceived of and have advocated for the National Housing Trust Fund see its purpose as ending this shortage, closing this gap. We think this is a proper role for Government. This is a shortage of a good that is fundamental to human well-being; housing is not an optional expense. It is clear that the market will not fill this gap. The cost of building and operating rental housing simply exceeds what can be paid in rent by extremely low income households.

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[1] Note: Housing and income data in SD may not reflect the total Native American population.

[2] Bravve, E., Bolton, M., and Crowley, S. (2013). "Out of Reach 2013". Washington, DC: National Low Income Housing Coalition.

[3] Ibid.

[4] Cooper, E., O'Hara, A., Singer, N, and Zovistoski, A. (2013). "Priced out in 2012". Boston, MA: Technical Assistance Collaborative, Inc.

[5] National Low Income Housing Coalition. (2013). "America's Affordable Housing Shortage and How To End It". *Housing Spotlight* 3(2). Washington, DC: Author.

[6] U.S. Department of Housing and Urban Development. (2013). "Worst Case Housing Needs 2011: Report to Congress". Washington, DC: Author.

[7] Joint Center for Housing Studies of Harvard University. (2013). "The State of the Nation's Housing 2013". Cambridge, MA: Author.

[8] Bipartisan Housing Commission. (2013). "Housing America's Future: New Directions for National Policy". Washington, DC: Bipartisan Policy Center.

[9] Weicher, J. (2012). "Housing Policy at the Crossroads: The Why, How, and Who of Assistance Programs". Washington, DC: The AEI Press.

You may and should ask why we need another low income housing program. What about all the HUD programs? What about the Low Income Housing Tax Credit? The answer is that there would be no need for the National Housing Trust Fund if the existing Federal programs were differently structured and sufficiently funded. However, no existing Federal housing program produces rental homes specifically targeted for extremely low income households, precisely the program that is most needed.

More critical, the existing programs are grossly underfunded. HUD rent assistance programs only serve 25 percent of eligible households. While we have had periods of modest growth in HUD programs in the last 30 years, more typically, the programs have been held flat or reduced. All HUD low income housing programs are part of domestic discretionary spending and thus subject to sequestration. Given the incredible constraints on appropriations that show no sign of abating, it is inconceivable that existing HUD programs will ever be enough.

We estimate that it would take $30 billion a year for 10 years to close the gap. That is why we need the National Housing Trust Fund.

How the National Housing Trust Fund Will Work

The primary purpose of the National Housing Trust Fund is to produce, preserve, rehabilitate, and operate rental homes that extremely low income households can afford. At least 90 percent of the funds must be used for rental housing and up to 10 percent can be used for home ownership activities. At least 75 percent must be used for extremely low income households and up to 25 percent can be used for households with incomes between 30 percent and 50 percent of the area median (very low income).

The National Housing Trust Fund is modeled after the over 600 housing trust funds created at the State and local level over the past 30 years, all of which help to supplement Federal funds for affordable housing. By 2013, 47 States and the District of Columbia had at least one State housing trust fund, for a total of 57 State housing trust funds. Five new trust funds have been established since 2011 in North Dakota, Virginia, Alabama, Colorado, and South Dakota.

Housing trust funds are run by a Government agency guided with priorities and programs established in the enabling legislation. Most commonly, trust fund resources are used for new construction, rehabilitation, preservation of affordable housing, as well as land or property acquisition for affordable housing development. Some trust funds also focus on the development of housing for individuals with special needs, including permanent supportive housing. Other activities include providing matching funds for Federal programs, predevelopment loans, emergency rental assistance, weatherization, and downpayment assistance. Although income targeting varies, many trust funds target the lowest income households.

Housing trust funds receive revenue from a wide range of sources, including general funds, but the preferred model is dedicated sources of revenue. For example, Nebraska has a documentary stamp tax, New Jersey has a realty transfer tax, and Ohio and Oregon have document recording fees. The most successful housing trust funds as those with robust dedicated revenue sources as they offer a predictable revenue stream.

It is important to note that at their peak in 2011, the combined value of State and local housing trust funds was approximately $1 billion.[10] They have lost ground since then. It is not realistic to think that State and local housing trust funds, even combined with other State and locally funded low income housing assistance, can ever get to the scale needed to solve the housing shortage.

The National Housing Trust Fund is structured as a block grant that is housed at HUD. Funds are to be distributed to the States and territories by a formula that is based on need, primarily need for rental homes affordable for extremely low income families. The funds will go to governors who will designate a State agency to administer the program. In most cases, we expect the National Housing Trust Fund to be run by State housing finance agencies that now administer the Low Income Housing Tax Credit program.

The State has to design an allocation plan and create performance goals. States can choose to use their National Housing Trust Fund dollars to address specific goals, such as ending homelessness or providing community based housing for all people with disabilities. States could use some of their allocation to preserve existing low income housing.

The State can use the funds to develop housing itself or can establish a grant making process to allocate the funds to subrecipients. The statute requires that a

[10] To learn more about State and local housing trust fund, go to *http://housingtrustfundproject.org.*

subrecipient has experience relevant to the activity it proposes and demonstrates financial expertise and experience.

The State is responsible for assuring that all funds are used properly and for assuring that any funds that are not properly used are reimbursed. HUD can reduce future grants to States that are not reimbursed for improperly used funds.

Funds cannot be used for advocacy, lobbying, political activities, travel, counseling, or preparing of tax returns. The State can use up to 10 percent of its allocation to administer the program, but no funds can be used for outreach or other administrative activities by the State or subrecipients.

HUD is required to recapture any funds that a State has not committed within 2 years and reallocate the funds to other States.

HUD has developed the regulations for implementation of the National Housing Trust Fund. They have been published for public comment, comments have been received, and final regulations are expected to be ready soon.

How the National Housing Trust Fund Should Be Treated in Housing Finance Reform

The National Housing Trust Fund has never been funded. It is intended to be funded with dedicated sources of revenue, such that it is not subject to the vicissitudes of the annual appropriations process and does not compete for funding with existing HUD low income housing programs. The initial source of funding provided for in HERA was an assessment on Fannie Mae and Freddie Mac. The statute also says that the National Housing Trust Fund can be funded by "any amounts as are or may be appropriated, transferred, or credited to such Housing Trust Fund under any other provisions of law."

As you well know, Fannie and Freddie were taken into conservatorship soon after HERA was enacted and the conservator suspended their obligation to fund the National Housing Trust Fund. That suspension continues to this day. Our analysis is that now that Fannie and Freddie are again profitable, this suspension should be lifted. Given the dire housing circumstances of so many poor Americans, it would be a godsend if the conservator agreed with us, but unfortunately he does not.

As you develop your legislation on the next generation of Federal housing finance policy, please include the following provisions related to the National Housing Trust Fund.

- Preserve the National Housing Trust Fund as enacted in HERA as a standalone program housed at HUD that provides grants to States for the core purpose of expanding rental housing that is affordable for extremely low income households. Do not change or add to its purposes or eligible activities unless doing so would strengthen this core purpose. This means the proposed Market Access Fund should be a separate program, not added to the Housing Trust Fund, as is done in S.1217. We also object to the segregation of the rental housing and home ownership activities in the National Housing Trust Fund as is the case in S.1217.
- Preserve the principle established in HERA that the U.S. housing finance system, which benefits from its affiliation with the Federal Government such as the explicit Federal guarantee that you contemplate, should make financial contributions to support housing activities that address housing needs that the market will not, specifically those of the poorest households.
- The financial contributions called for above should come from at least a 10 basis point annual user fee, i.e., a "strip," assessed on all mortgage backed securities (MBS), not just guaranteed securities. This includes both single family and multifamily MBS. Further, we support an additional fee on multifamily MBS for properties with rents geared to households with incomes over 150 percent of the area median.
- Maximize the amount of funding to the National Housing Trust Fund from these financial contributions, recognizing that even a 10 basis point annual user fee on all MBS would not generate sufficient funding to address the shortage of rental housing affordable for extremely low income households. Continue to provide for other funding to go to the National Housing Trust Fund in "any amounts as are or may be appropriated, transferred, or credited . . . under other provisions of law" as does HERA.
- Maintain the National Housing Trust Fund as a permanent fund on the mandatory side of the budget. We strongly urge that the Banking Committee retain and, if necessary, strengthen its oversight duties and responsibilities for the National Housing Trust Fund. If the funds generated by the user fee called for above are made available for appropriations, there is no way to assure that all

(or any) of the funds would be used for the National Housing Trust Fund or even for low income housing.

- Assure payments are made to the National Housing Trust Fund during the transition period from Fannie Mae and Freddie Mac to the successor entity and immediately upon establishment of the new housing finance system.

Thank you for the opportunity to testify today. I look forward to your questions.

PREPARED STATEMENT OF DOUGLAS HOLTZ-EAKIN

PRESIDENT, AMERICAN ACTION FORUM

NOVEMBER 7, 2013

Chairman Johnson, Ranking Member Crapo, and Members of the Committee, thank you for the opportunity to appear today. In this testimony, I wish to make three basic points:

- The legislation being worked on by this Committee represents a necessary and long-overdue effort to address damaging weaknesses in the U.S. housing finance system. The status quo is unsustainable and undesirable. I applaud the Committee for moving forward;
- While helping low-income households afford necessary shelter should be a policy priority, and such support should be appropriated by Congress and on the budget. Budgetary integrity requires that Congress balance the full range of policy priorities; and
- The affordable housing goals imposed on the housing GSEs were flawed, and should not be repeated.

The Need for Reform

Housing finance was at the center of the 2008 financial crisis that visited substantial economic stress on Americans and spawned dramatic Government intervention. Yet, over 5 years later the central actors in the crisis and response—Fannie Mae, Freddie Mac, and the Federal Housing Administration (FHA)—remain essentially unchanged. While the task is politically daunting and mechanically difficult, I applaud the Committee's desire to undertake these reforms.

Fannie Mae and Freddie Mac

Fannie Mae and Freddie Mac need to be wound down and closed as a matter of both policy and politics. From a policy perspective, the Government-sponsored enterprises were central elements of the 2008 crisis. First, they were part of the securitization process that lowered mortgage credit quality standards. Second, as large financial institutions whose failures risked contagion, they were massive and multidimensional cases of the too big to fail problem. Policy makers were unwilling to let them fail because financial institutions around the world bore significant counterparty risk to them through holdings of GSE debt, certain funding markets depended on the value of their debt, and ongoing mortgage market operation depended on their continued existence. They were by far the most expensive institutional failures to the taxpayer and are an ongoing cost.

There is vigorous debate about how big a role these two firms played in securitization relative to "private label" securitizers. There is also vigorous debate about why these two firms got involved in this problem. In the end, this debate need not be fully resolved to recognize that while Fannie Mae and Freddie Mac did not by themselves cause the crisis, they contributed significantly in a number of ways.

The mortgage securitization process turned mortgages into mortgage-backed securities through the Government-sponsored enterprises, as well as Countrywide and other "private-label" competitors. The securitization process allows capital to flow from investors to homebuyers. Without it, mortgage lending would be limited to banks and other portfolio lenders, supported by traditional funding sources such as deposits. Securitization allows homeowners access to enormous amounts of additional funding and thereby makes home ownership more affordable. It also can diversify housing risk among different types of lenders. If everything else is working properly, these are good things. Everything else was not working properly.

There were several flaws in the securitization and collateralization process that made things worse. Fannie Mae and Freddie Mac, as well as Countrywide and other private label competitors, all lowered the credit quality standards of the mortgages they securitized. A mortgage-backed security was therefore "worse" during the crisis than in the preceding years because the underlying mortgages were generally of poorer quality. This turned a bad mortgage into a worse security. Mortgage originators took advantage of these lower credit quality securitizations standards and the easy flow of credit to relax the underwriting discipline in the loans they issued. As long as they could resell a mortgage to the secondary market, they didn't care about its quality.

In addition to feeding poorly originated mortgages into the system, Fannie Mae and Freddie Mac proved to be so deeply interconnected with the broader financial system that policy makers were forced to step in to prevent their failure. In September 2008, the Federal Housing Finance Agency (FHFA) put Fannie Mae and Freddie Mac into conservatorship. Policy makers in effect promised that "the line would be drawn between debt and equity," such that equity holders were wiped out but GSE debt would be worth 100 cents on the dollar.

They made this decision because banking regulators (and others) treated Fannie and Freddie debt as equivalent to Treasuries. A bank cannot hold all of its assets in debt issued by General Electric or AT&T, but can hold it all in Fannie or Freddie debt. The same is true for many other investors in the United States and around the world—they assumed that GSE debt was perfectly safe and so they weighed it too heavily in their portfolios. Policy makers were convinced that this counterparty risk faced by many financial institutions meant that any write-down of GSE debt would trigger a chain of failures through the financial system. In addition, GSE debt was used as collateral in short-term lending markets, and by extension, their failure would have led to a sudden massive contraction of credit beyond what did occur. Finally, mortgage markets depended so heavily on the GSEs for securitization that policy makers concluded that their sudden failure would effectively halt the creation of new mortgages. All three reasons led policy makers to conclude that Fannie Mae and Freddie Mac were too interconnected with the system to be permitted to fail.

As a matter of politics, Fannie Mae and Freddie Mac are extremely unpopular and the public supports winding them down. (This section draws on a poll commissioned by the American Action Forum.[1]) The polling shows that a large majority of the voters have a "hard ID" of Fannie and Freddie. They are viewed favorably by only 20 percent and unfavorably by 52 percent.

This is related to another finding, namely that 52 percent of the voters said that their greatest concern is either no accountability of banks and Wall Street or that Wall Street banks are so big that if they fail the taxpayers will have to bail them out again. By a small margin (11 percent) voters are still unfavorable toward the bank bailouts and TARP. Likely for this reason, a majority favor (52 percent) phasing out both Fannie and Freddie.

Greater information sharpens these views. When informed that Fannie and Freddie played an instrumental role in the housing bubble and received nearly $200 billion in a bailout, voters' opposition to Fannie Mae and Freddie Mac moves to 59 percent. Additionally, the notion that Fannie and Freddie could require more public money in future bailouts is unacceptable to a sizable majority of the voters.

Using Housing Reform To Address Affordability

As the Committee considers housing finance reform, the affordability of shelter naturally arises as a policy concern. How should this be addressed? First, the affordable housing goals of Fannie Mae and Freddie Mac were both unsuccessful and dangerous, and should not be repeated. The Housing Finance Reform and Taxpayer Protection Act (S.1217), being considered by this Committee, does not authorize HUD to set similar goals, but it does aim to preserve them in other ways.

Affordable Housing Goals. Previously, HUD was the mission regulator of the GSEs, setting minimum percentage-of-business housing goals for mortgage purchases. The goals were set to support low-income lending and lending in underserved geographic regions. Specifically, the GSEs had three annual affordable housing goals:

1. Low- and Moderate-Income Goal: targets borrowers with income no greater than area median income (AMI)
2. Special Affordable Goal: targets very low-income borrowers (less than 60 percent of AMI) and low-income borrowers (less than 80 percent of AMI) living in low-income census tracts
3. Geographically Targeted or Underserved Areas Goal: targets low-income and high-minority neighborhoods

[1] American Action Forum, "AAF Releases New Poll of Public Attitudes on Fannie, Freddie Mac, and Housing Reform", (July 2013); *http://americanactionforum.org/topic/aaf-releases-new-poll-public-attitudes-fannie-mae-freddie-mac-and-housing-reform.*

Overall, Freddie Mac consistently lagged the conventional market in funding the three groups targeted by HUD's housing goals. Fannie Mae, while performing better than Freddie Mac, performed on average below market levels except over the 2001–03 period when it only lagged the market in funding underserved area loans.[2] [3] Yet despite failing to meet their goals, HUD added subgoals and consistently raised the purchase percentages of existing goals to ever-higher levels.

Though inclusion of affordability goals did not singularly undermine the GSEs' profitability or cause their demise, the goals complicated their mission, blurring public purpose and pursuit of private profits. More importantly, the goals were not successful. Evidence shows the other lenders were buying more loans that met the goals than the GSEs themselves. Furthermore, if the purpose of the goals was to provide shelter, it did not have to take the form of owner-occupied homes. If the goal was to promote home ownership, the GSEs failed by concentrating more on homebuyers with homes already (not first-time homebuyers) and on homeowners refinancing.[4]

Funding the National Affordable Housing Trust Fund. Provisions under Title IV of the proposed legislation would replace the failed affordable housing goals of the GSEs with a user fee of 5–10 basis points on FMIC-insured securities to fund the Housing Trust and Capital Magnet Funds. Instituting that surcharge presents three main problems:

- The cost of contributions may be passed on to mortgage borrowers, raising the cost of mortgage rates even further than the proposed legislation likely will already. That is, it works against the goal of affordable mortgage finance;
- Fund advocates have an increased incentive to encourage the FMIC to grow beyond its chartered purpose; and
- Revenues from the surcharge and the effectiveness of the ways they are spent will not be subject to the scrutiny and approval inherent in the budget and appropriations process.

Advocates for a national affordable housing trust fund—e.g., the National Low Income Housing Coalition—have stated the importance of "[a] dedicated source of funding not subject to the annual appropriations process."[5] Why? Despite the woes of the congressional budget process, it would fundamentally diminish the accountability of the Housing Trust and Capital Magnet Funds to which the fee is allocated if they stay outside of the regular appropriations process. A fundamental lack of transparency and accountability underscored the GSE model and continues to trouble the FHA. It would be a core policy error to make a similar mistake in the funding of these trusts included in the proposed legislation.

Preserving Support for Small Institutions and Underserved Communities. Support for all geographic regions of the country, whether an underserved rural or urban community, has been a mainstay of bipartisan proposals for housing finance reform. Additionally, equal access to the secondary market for institutions of all sizes is important to widespread availability of affordable credit.

S.1217 contains several provisions that aim to preserve support for small institutions and underserved communities. First, the legislation mandates in Title II that the FMIC "help ensure all geographic locations have access to mortgage credit." The FMIC is also charged with facilitating securitization for credit unions and community and midsize banks. In developing products, structures, contracts, etc., the FMIC must take into account how their actions would affect small financial institutions, the availability of credit, and equitable access to secondary mortgage market financing for lenders of all sizes and locations including those in rural communities. The legislation also requires fee uniformity for institutions purchasing insurance from the FMIC regardless of location or size of the institution. Finally, if concerns exist about the viability of those aforementioned duties, those concerns must be submitted in a report to Congress.

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[2] Bunce, Harold L., Office of Policy Development and Research, U.S. Department of Housing and Urban Development, "Working Paper No. HF-018. The GSEs' Funding of Affordable Loans: A 2004–2005 Update", (June 2007); *http://www.huduser.org/portal/publications/pdf/workpapr18.pdf.*

[3] FHFA, "Mortgage Market Note 10-2—The Housing Goals of Fannie Mae and Freddie Mac in the Context of the Mortgage Market: 1996–2009," (February 2010); *http://www.fhfa.gov/webfiles/15419/Housing_Goals_1996–2009_02-01.pdf.*

[4] John C. Weicher, "The Affordable Housing Goals, Home Ownership and Risk: Some Lessons From Past Efforts To Regulate the GSEs", Conference on "The Past, Present, and Future of the GSEs", Federal Reserve Bank of St. Louis, (November 2010); *http://research.stlouisfed.org/conferences/gse/Weicher.pdf.*

[5] National Low Income Housing Coalition, "National Housing Trust Fund"; *http://nlihc.org/issues/nhtf.*

Reforming the FHA. Housing finance reform, whether S.1217 or another piece of legislation, should consider undertaking needed reforms to FHA. While the GSEs supported affordable housing through goals sets by HUD, those goals worked to undermine the housing finance system. Following the housing bust and entry of the GSEs into conservatorship, significant market share shifted to FHA, causing unprecedented financial losses for the agency.

Some of the potential reforms—for example, as embodied in the PATH Act—would narrow FHA's mission to support only low-income and first-time homebuyers. With a mix of income-based borrower requirements and revised loan limits, the FHA would more adequately address a demonstrated need among low-income communities and first-time homebuyers while also enhancing the role of the private market. Addressing FHA in conjunction with the wind down of the GSEs is preferable because of how easily misaligned prices, limits, and standards can shift market share between Government-backed programs. S.1376, the FHA Solvency Act of 2013, considered by this Committee, does not include similar income-based borrower requirements, fundamental changes to the administration of FHA, fair-value and GAAP accounting requirements, or tightened loan limits present in the House legislation.

The Dodd-Frank Act and Affordability. Housing finance reform must also take into account how Dodd-Frank regulations deeply affect affordability. Eligible mortgages under the S.1217 are limited to qualified mortgages (QM) as defined by regulators. A recent analysis of Home Mortgage Disclosure Act (HMDA) data by economists at the Federal Reserve found that 22 percent of borrowers in 2010 had debt-to-income ratios above the 43 percent standard set by the QM rule.[6] Seventy percent of borrowers above that threshold had FHA, VA, or RHS insured loans. Those borrowers with debt-to-income ratios above 43 percent were also most likely to be lower-income, black, or Hispanic-white. This exemplifies just how easily regulations enacted from the Dodd-Frank Act can severely can impact affordability among lower-income communities and communities of color. Under the new regulatory regime, it will be either costly or impossible for private capital to back high LTV or non-QRM lending to fill the Government's role.

AAF previously estimated that the bottom line effects of proposed Dodd-Frank and Basel III regulations may include 20 percent fewer loans, resulting in 600,000 fewer home sales. In turn, the resulting tightened lending and reduced sales were estimated to cost up to 1,010,000 housing starts, 3.9 million fewer jobs, and a loss of 1.1 percentage points from GDP growth over the next 3 years.[7] While some of those regulations have been revised, the reality of tightened credit and its potential effect on the economy remain largely the same.

Another study by the National Association of Realtors estimated that Dodd-Frank regulations could raise mortgage rates by 75–125 bps for non-QRM, high LTV borrowers and Basel III could raise rates by 80 bps.[8] These estimates of the effect regulations have on mortgage rates are equivalent or higher than the effect economist Mark Zandi estimated S.1217 would have on mortgage rates.[9] To not take into account how Dodd-Frank regulations affect affordability in a future system would be a mistake.

Redundant Government Support for Affordable Housing

The Federal Government provides multiple avenues of support for the construction of affordable housing and assistance for low-income renters and homebuyers. While the success of these programs can be debated, support exists and does so in many forms; primarily the Federal Government provides appropriated funding through more than 30 programs within the Department of Housing and Urban Development (HUD), tax credits and deductions for both corporations and individuals, housing programs for veterans through the Department of Veterans' Affairs (VA), rural housing programs through the Department of Agriculture (USDA), the mortgage insurance programs of the Federal Housing Administration (FHA), and Government corporation Ginnie Mae. In attempting to overhaul the housing finance sys-

[6] Neil Bhutta and Glenn B. Canner, Division of Research and Statistics, Federal Reserve, "Mortgage Market Conditions and Borrower Outcomes: Evidence From 2012 HMDA Data and Matched HDMA-Credit Record Data", (September 2013); *http://www.federalreserve.gov/pubs/bulletin/2013/pdf/2012_HMDA.pdf.*

[7] Douglas Holtz-Eakin, Cameron Smith and Andrew Winkler, "Regulatory Reform and Housing Finance: Putting the 'Cost' Back in Benefit-Cost", (October 2012); *http://americanactionforum.org/sites/default/files/Regulation_and_Housing.pdf.*

[8] National Association of Realtors, "Recent Lessons for the QRM", (December 2011); *http://economistsoutlook.blog.realtor.org/2011/12/08/recent-lessons-for-the-qrm/.*

[9] Mark Zandi and Cristian deRitis, "Evaluating Corker-Warner", (July 2013); *http://www.economy.com/mark-zandi/documents/2013-07-08-Evaluating-Corker-Warner.pdf.*

tem, it would be wise to address the issue of affordability through the reform or increased support of existing programs and not through legislation addressing the mechanics of the Government's role in the secondary market.

Last year the Government Accountability Office (GAO) concluded that the Federal Government "incurred about $170 billion in obligations for Federal assistance and estimated forgone tax revenue in fiscal year 2010." [10] The GAO found housing assistance fragmented across 160 programs and activities. Table 1, which does not include any tax expenditures, provides an example of the number of programs that exist across agencies. (Note: housing programs are not limited to those in Table 1.)

According to the Joint Committee on Taxation, tax expenditures subsidizing housing, for individuals and corporations, will cost the Federal Government $868 billion in foregone taxes from 2012 to 2017 (see Table 1). While many of these credits, deductions, and exemptions favor owner-occupied housing over rental housing, that problem can and should be addressed through tax reform.

The redundancy of Federal support of housing calls into question the efficiency and effectiveness of Government efforts to assist low-income renters and homebuyers and maintain affordability. Tackling affordability requires both a dedication to greater job and wage growth, as well as a renewed look at what improvements can be made to existing Federal housing programs.

The effects of reform legislation on affordability will ultimately depend on the system put in place; whether the new system has many players, maintains the flow of mortgage credit and protects taxpayers from liabilities is more important than any fund or single program. The most important components of housing finance reform are the mechanics of a new system and how to transition to it.

Thank you. I look forward to answering your questions.

[10] Government Accountability Office, "Housing Assistance: Opportunities Exist To Increase Collaboration and Consider Consolidation", (August 2012); *http://gao.gov/assets/600/593752.pdf.*

TABLE 1. FEDERAL SUPPORT FOR HOUSING, 201 BUDGET *(In Millions $)*		
	BUDGET AUTHORITY	OUTLAYS
DEPARTMENT OF HOUSING & URBAN DEVELOPMENT		
Tenant Based Rental Assistance	18,264	17,952
Project-Based Rental Assistance	9,340	9,244
Community Development Fund	3,407	6,794
Public Housing Operating Fund	3,962	4,220
Public Housing Capital Fund	1,875	2,719
Homeless Assistance Grants	1,901	1,954
Home Investment Partnership Program	1,000	1,781
Housing for the Elderly	375	862
Housing Certificate Fund	(200)	834
Native American Housing Block Grant	651	751
Other Assisted Housing Programs	(231)	445
Housing Opportunities for Persons with AIDS	332	334
Housing for Persons with Disabilities	165	226
Emergency Homeowners' Relief Fund	-	189
HOPE VI	-	129
Self-Help Homeownership Opportunity Program	54	63
Indian Housing Loan Guarantee Fund Program Account	26	28
Rural Housing & Economic Development	-	11
Permanent Supportive Housing	-	10
Manufactured Housing Trust Fund	6	7
Native Hawaiian Housing Block Grant	13	3
Choice Neighborhoods Initiative	120	-
Native Hawaiian Loan Guarantee Program	-	-
Housing Trust Fund	-	-
Capacity Building	-	-
Rental Housing Assistance Fund	-	(1)
Flexible Subsidy Fund	-	(54)
Nehemiah Housing Opportunity Fund	-	-
DEPARTMENT OF AGRICULTURE		
Rural Housing Insurance	1,284	1,303
Rental Assistance Program	905	1,115
Multifamily Housing Revitilization Program	46	57
Rural Housing Assistance Grants	33	39
Mutual & Self-Help Housing Grants	30	33
DEPARTMENT OF TREASURY		
Grants to State for Low-Income Housing Projects in Lieu of Low-Income Housing Tax Credit Allocations	-	627
TARP Housing Programs	-	604
Capital Magnet Fund	-	5
DEPARTMENT OF VETERANS' AFFAIRS		
Veterans Housing Benefit Program	1,715	1,717
Native American Veteran Housing Loan Program	15	14

Source: OMB

TABLE 2. TAX EXPENDITURE ESTIMATES, F 2012-2017 *(Billions of Dollars)*		
	CORPORATIONS	INDIVIDUALS
Deduction for Mortgage Interest on Owner-Occupied Residences	-	447.5
Deduction for Property Taxes on Real Property	-	177.4
Exclusion of Capital Gains on Sales of Principal Residences	-	152.0
Exclusion of Interest on State & Local Government Qualified Private Activity Bonds for Owner-Occupied Housing	1.8	5.6
Deduction for Premiums for Qualified Mortgage Insurance	-	0.5
Exclusion of Income Attributable to the Discharge of Principal Residence Acquisition Indebtedness	-	2.9
Credit for Low-Income Housing	40.3	2.1
Credit for Rehabilitation of Historic Structures	2.6	1.3
Credit for Rehabilitation of Structures, Other than Historic Structures	0.6	1.2
Exclusion of Interest on State & Local Government Qualified Private Activity Bonds for Rental Housing	1.7	4.4
Depreciation of Rental Housing in Excess of Alternative Depreciation System	2.5	23.2
Total	**49.5**	**818.1**

Source: Joint Committee on Taxation[11]

[11] Joint Committee on Taxation, "Estimates Of Federal Tax Expenditures For Fiscal Years 2012-2017," (February 01, 2013); https://www.jct.gov/publications.html?func=select&id=5

PREPARED STATEMENT OF ETHAN HANDELMAN

VICE PRESIDENT FOR POLICY AND ADVOCACY, NATIONAL HOUSING CONFERENCE

NOVEMBER 7, 2013

My name is Ethan Handelman, and I am the Vice President for Policy and Advocacy at the National Housing Conference. I am grateful to the Committee for inviting me to testify, and I particularly thank the Chair, the Ranking Member, and the many other Committee Members who are working on housing finance reform in a constructive, bipartisan manner.

I appreciate your choice of "affordable options for housing" in the title of this hearing, as that should be a central goal of housing finance reform. The work of rebuilding the mortgage finance system cannot be only about making markets function—it must be about shelter. As the Federal Government creates new mechanisms for housing finance, deploys its full faith and credit, and encourages private entities to put capital to work, the social purpose of safe, decent, and affordable housing for all in America must guide those efforts. The new housing finance system you are working hard to create must find ways to harness the creativity and energy of the private sector to provide homes for people across this country: in cities, suburbs, and rural areas; in houses, apartments, and manufactured homes; for old and young, renters and owners, singles and families, of all backgrounds. To accomplish that, the housing finance system must by design serve as broadly as possible, and there must be mechanisms to fill in the remaining gaps.

About the National Housing Conference

The National Housing Conference (NHC) represents a diverse membership of housing stakeholders including tenant advocates, mortgage bankers, nonprofit and for-profit home builders, property managers, policy practitioners, realtors, equity investors, and more, all of whom share a commitment to safe, decent, and affordable housing for all in America. We are the Nation's oldest housing advocacy organization, dedicated to the affordable housing mission since our founding in 1931. As a nonpartisan, 501(c)3 nonprofit, we are an evidenced-based research and education resource working to advance housing policy at all levels of Government in order to improve housing outcomes for all in this country.

The Large and Growing Need for Affordable Housing

The reform of our Nation's housing finance system occurs in the context of a long trend of increasing housing need. For both homeowners and renters, the cost of housing outpaces income, often creating a severe burden. The annual Housing Landscape publication from NHC's Center for Housing Policy documents the prevalence of severe housing cost burdens, meaning housing costs in excess of 50 percent of income, for working households. More than one in four working renter households (26.4 percent) spent more than half of their income on housing costs in 2011, an increase of more than three percentage points since 2008. Despite falling mortgage interest rates and home prices—a period when housing affordability for owners should have improved—rates of severe housing cost burden remained stable and high for working owners between 2008 and 2011. Roughly one in five working owners experienced a severe housing cost burden during this period.[1]

If we look beyond the subset of working households to all housing need, the picture is even worse. In 2011, over 40 million households in this country were paying more than 30 percent of their income for housing, and 20.6 million were paying more than 50 percent. Recent increases in cost burdens have been primarily among renters, with those of lowest income hit hardest. Yet, only one in four households eligible for housing assistance actually receives it.[2]

Looking to the future, we should expect the aging of the population and an Echo Boom with an increase in minority households to drive much housing need. Aging households will increase demand for modification of existing homes, smaller homes with supportive services, and better access to transportation. Rental housing demand will rise, driven by the more mobile Echo Boom and a larger proportion of minority and low-wealth household. Demand for starter homes and the need of low-wealth households for affordable home mortgages without overly restrictive down-

[1] Center for Housing Policy, "Housing Landscape 2013", May 2013, available at *http://www.nhc.org/media/files/Landscape2013.pdf.*

[2] Harvard Joint Center for Housing Studies, "State of the Nation's Housing 2013", p. 5, available at: *http://www.jchs.harvard.edu/research/state_nations_housing.*

payment requirements will directly affect households' ability to achieve home ownership.[3]

Serving Housing Needs by Encouraging Private Enterprise

The urgency of mortgage finance reform stems both from the growing housing needs of Americans and the need to restore a reliable source of mortgage capital in the wake of the 2008 financial crisis. We are still operating with what was thought to be a temporary conservatorship for Fannie Mae and Freddie Mac (the Government Sponsored Enterprises, or GSEs). Overall, the Federal Government continues to guarantee over 85 percent of new mortgages. Private capital has yet to return to sustainable precrisis levels. Finance for multifamily housing has fared somewhat better thanks in large part to the GSE's multifamily operations, but overall production of multifamily housing has only just returned to historically stable levels, leaving 5 years of pent-up demand to make up.

Mortgage finance reform must address both reliable capital flows and household need. A strong Government presence in the secondary mortgage market can create the necessary stability and liquidity for private enterprise to provide home mortgages and finance rental housing effectively—in other words, to make the market function well. But we know that private enterprise does not serve all parts of the market well. Many rural areas, lower-income households, small rental properties, manufactured housing properties, subsidized rental housing, communities of color, and neighborhoods hit hard by waves of foreclosure lack adequate capital. Government's action must be about more than just market functioning. It should aim to unleash the energy of private enterprise to serve the shelter needs of all in America.

Enabling Long-Term Financing With a Federal Guarantee

The critical first part must be a Federal guarantee that is explicit, paid-for, and protected by layers of risk-bearing capital. The guarantee should be limited to securities, separate from the issuing entities or their debt. Absent that guarantee, there simply would not be enough private capital to make 30-year fixed-rate mortgages widely available. Nor would the To Be Announced (TBA) market function, which would make mortgages more expensive and deprive homeowners of the ability to lock an interest rate before closing.

The Federal Housing Administration (FHA), the U.S. Department of Agriculture (USDA), and Veterans Affairs (VA), are essential and at times play a critical countercyclical role, but they should remain focused on specific populations such as veterans, first-time homebuyers, and low-wealth households. We cannot rely on them to be the sole source for affordable, long-term mortgages.

Rather, we need to allow multiple, proven capital channels to serve housing needs. Ensuring a mechanism by which housing finance agencies, credit unions, community banks, and other smaller lenders have access to securitization on an equitable footing would provide additional means to finance affordable home loans and finance affordable rental housing.

Safe and Sustainable Low-Downpayment Lending

Downpayment has an intuitive appeal from a regulatory standpoint, since it is a simple, bright line with a correlation to default rate. However, it is only one factor among many in a full underwriting analysis, and on its own is neither a necessary nor sufficient condition for a good loan. Using downpayment as a minimum threshold, moreover, powerfully disadvantages responsible low- and moderate-income homebuyers. Eliminating the overly rigid 5-percent downpayment requirement currently in S.1217 is an important step toward broadening access to the most efficient source of mortgage capital.

A high downpayment threshold creates a powerful barrier to home ownership for low-wealth families, one that is uniquely difficult to overcome. A family can improve its credit performance over time or pay down nonmortgage debt, but saving up $20,000 or $40,000 (even more in high-cost markets) for a downpayment can take decades. Making the accumulation of wealth a requirement for access to affordable mortgage finance in effect excludes Americans who do not already have individual or family wealth. Not only is that fundamentally unfair, but it also skews disproportionately against communities of color.[4]

[3] "State of the Nation's Housing", p. 16. Also, Bipartisan Policy Center Housing Commission, "Demographic Challenges and Opportunities for U.S. Housing Markets", March 2012, available at *http://bipartisanpolicy.org/sites/default/files/BPC%20Housing%20Demography.pdf.*

[4] "Plan B, a Comprehensive Approach To Moving Housing, Households, and the Economy Forward"; April 4, 2011, by Lewis Ranieri, Ken Rosen, Andrea Lepcio, and Buck Collins. Figure 14 shows that minority households in 2007 had median before tax family income of about

We know that well-structured, low-downpayment loans to responsible borrowers perform well. The best data on this come from the Center on Community Capital, which found that properly structured, low-downpayment loans performed 3.5 to 3.99 times better than subprime loans to comparable borrowers, even during the height of the foreclosure crisis.[5] The well-structured low-downpayment loans perform with comparable stability to prime loans. Data illustrate the converse, too: in the fourth quarter of 2010, the percent of prime fixed rate loans in foreclosure was 2.67 percent, the highest level in the history of the Mortgage Bankers Association National Delinquency Survey. The rate for prime adjustable rate loans was a whopping 10.22 percent.[6] These data underscore that the housing crisis resulted from inherently risky mortgage features—exploding ARMs, no-doc loans, negative amortization—rather than loans with low downpayments.

We further know that downpayment assistance programs provided by localities and approved nonprofits generate low-risk loans. Indeed, buyers with assistance from affordable home ownership programs have default rates well below local market averages, even with very low or no downpayment from the buyer's own funds.[7] Home ownership assistance programs use public resources efficiently to create long-term affordable housing, often making the loans safer than some unassisted transactions.

Serving All Qualified Borrowers

Discussions of how to get the mortgage finance system to serve all qualified borrowers often bog down in circular questions of whether the primary or secondary market should lead. The primary market lenders originate loans and so are the first gatekeepers of access to credit. However, their ability to lend is constrained by the liquidity supplied by the secondary market. Without a capital supply, the primary market cannot originate large volumes of loans. The secondary market, in contrast, focuses on efficiency, using high volumes of homogeneous loans to achieve economies of scale and attract capital. Packaging easily standardized, lower-risk loans into securities has great benefits, but the business is necessarily constrained to work with the loans that the primary market originates. It therefore becomes difficult for either the primary market or the secondary market to cause the other to broaden its parameters for what loans to provide, since neither can act without the support of the other.

Government is uniquely placed to align the primary and secondary markets to serve as broadly as possible. A rebuilt housing finance system should include a strong regulatory agency with the necessary powers to supervise the market. The regulator could implement a requirement that secondary market participants who benefit from the stability, transparency, and liquidity created by the housing finance system serve the entire primary market. To the extent that the primary market is serving low-income areas, rural areas, communities of color, small rental properties, subsidized rental housing, manufactured housing, and other underserved market segments, the secondary market should also.

The Housing and Economic Recovery Act of 2008 (HERA) created a framework for measuring the secondary market's performance and evaluating it against the primary market. Home Mortgage Disclosure Act data provide a useful metric, among others. Similar mechanisms could be incorporated into the new legislation the Committee is developing, for both single family and multifamily, provided there is a strong regulatory agency with the ability to gather market information and supervise participants.

Financing Affordable Multifamily Housing

Renters make up more than one third of the country, and their median income is approximately half that of owners.[8] Demand for rental housing is increasing, and multifamily properties are an important component of meeting that demand. Ensur-

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$37,000, compared to about $52,000 for white families. Similarly, Figure 15 shows minority family net worth in 2007 of almost $30,000, compared to more than $170,000 for white families.

[5] Lei Ding, Roberto G. Quercia, Wei Li, Janneke Ratcliffe, "Risky Borrowers or Risky Mortgages: Disaggregating Effects Using Property Score Models", Center for Community Capital Working Paper, May 17, 2010. Available at *http://www.ccc.unc.edu/documents/Risky.Disaggreg.5.17.10.pdf.*

[6] The survey is available at *http://www.mortgagebankers.org/NewsandMedia/PressCenter/75706.htm.*

[7] Urban Institute. "Balancing Affordability and Opportunity: An Evaluation of Affordable Home Ownership Programs With Long-Term Affordability Controls", October 26, 2010.

[8] "State of the Nation's Housing 2013", p. 22.

ing a steady supply of capital to multifamily housing, therefore, is a necessary part of ensuring that Americans can afford a range of housing options.

The Fannie Mae and Freddie Mac multifamily businesses are critical capital sources with a proven track record for the creation and preservation of affordable rental housing. The majority of Fannie Mae and Freddie Mac's multifamily business finances rental homes for families of modest means. In 2012, over 68 percent of units financed by Freddie Mac were affordable to households earning less than 80 percent of area median income (AMI), and 14 percent were affordable to those earning less than 50 percent of AMI. Fannie Mae's performance is comparable: 67 percent of the units financed in 2012 were affordable to households at 80 percent of AMI and 19 percent were affordable to those earning less than 50 percent of AMI.[9]

Production of so much affordable housing is in part due to the specialized products that Fannie Mae and Freddie Mac provide. They are able to provide longer-term debt than pension funds, banks, or conduit lenders typically offer.[10] Having stable debt service costs is often essential to regulated affordable housing properties that must pledge long-term use restrictions, and it also critical to allowing properties to maintain lower rents even without a formal use restriction. Fannie Mae and Freddie Mac have also forged relationships with State housing finance agencies, community development financial institutions, and others financing affordable housing in ways that private capital sources simply will not fill in. A specific example is the advance commitments for permanent take-outs of bond-financed properties without which many bond-financed affordable housing properties could not come about.

The Fannie Mae and Freddie Mac multifamily businesses are proven and profitable, and they remained so even during the crisis. Both businesses have delinquency rates consistently under 1 percent, compared to 12.15 percent delinquency for commercial mortgage backed securities (CMBS) in 2010 and 9.65 percent for CMBS in 2012.[11]

We recommend separating the multifamily businesses now, while still in conservatorship, to prepare for eventually privately capitalizing them as issuers of FMIC-insured multifamily mortgage-backed securities (MBS). FMIC should have a separate Office of Multifamily Finance to oversee the spun-off issuers as well as new issuers who are able to meet the same criteria for participation. All issuers of insured multifamily MBS should be obligated to meet a minimum affordability threshold at a portfolio level. More detail on our specific recommendations for improving treatment of multifamily appears in the proposal developed through the Mortgage Finance Working Group, presented in Attachment 1. Principles developed by NHC to guide mortgage finance reform for multifamily are presented in Attachment 2.

Filling in the Market's Gaps

The secondary mortgage market, despite its great efficiency, does not serve all those who need housing equally well. We therefore need specialized tools to fill in the gaps that are left. As currently proposed, S.1217 includes a small fee on MBS to fund three complementary mechanisms for improving access and affordability:

- The National Housing Trust Fund (NHTF) directly serves the needs of extremely low-income renters using a combination of capital subsidy to create affordable rental homes and rental subsidy to enable those homes to serve extremely low-income households. Enacted in the Housing and Economic Recovery Act of 2008 (HERA), it still requires funding to begin allocating funds to the States for deployment. HUD is a natural fit to implement the NHTF, given its expertise in allocation of block grants and understanding of property finance and rental subsidy.
- The Capital Magnet Fund (CMF) supports financing for the preservation, rehabilitation, or purchase of affordable housing for low-income communities and community service facilities such as day care centers, workforce development centers, and health care clinics. It leverages other funds 10 to 1, and proved extremely effective in its first (and only) round of funding. CMF, also enacted in HERA, is capably managed by the Treasury's CDFI Fund and should continue there.

[9] Data compiled by the National Housing Trust from public sources including Fannie Mae and Freddie Mac quarterly statements and the 2012 FHFA Report to Congress.

[10] Life companies offer some long-term debt, but they are a very small slice of the market and focus on only pristine, A-class properties.

[11] Freddie Mac, "Report to the Federal Housing Finance Agency: Housing Finance Reform in the Multifamily Mortgage Market", December 2012, p. 13.

- The Market Access Fund (MAF) should be created to provide a way for Government to share the risk of new product development and piloting, to help private enterprises develop more effective ways to direct capital to underserved households and communities. Through competitive research and development grants and temporary credit enhancement, MAF would seek to enable the private sector to more efficiently address unmet housing need. MAF would be best administered by FMIC, which would have the necessary expertise and contact with secondary and primary market financing to evaluate product proposals and oversee credit enhancement.

To enable each of these complementary mechanisms, we therefore support the creation and funding of a multipurpose fund that builds on Title IV of S.1217 so that the new housing finance system can better serve a range of housing needs. We recommend assessing all mortgage backed securities (not just guaranteed securities) a 10 basis point annual user fee (i.e., a "strip") that would be used to support the Market Access Fund, the National Housing Trust Fund, and the Capital Magnet Fund. We strongly suggest that percentage allocations to the three funds provided in Title IV be reconsidered to assure that the allocations more closely reflect the needs that each fund addresses.

All MBS, not just those with a guarantee, should pay the small fee to support these programs, for several reasons. Firstly, the entire market benefits from the stability and liquidity that the Government creates through its guarantee and regulation. The jumbo market, for instance, benchmarks to the conventional guaranteed market and is modeled on processes developed by Fannie Mae and Freddie Mac. Secondly, having a fee on just the guaranteed market would distort incentives, unnecessarily steering securitization away from the Government-backed channel and as a result requiring a higher fee. Thirdly, creating opportunities for wealth-building, stable rental housing, and stronger neighborhoods helps ensure more future homebuyers to keep the system running.

Others on the panel have already addressed the NHTF, but additional information on the CMF and the MAF may be helpful.

Capital Magnet Fund

The Capital Magnet Fund was created in HERA to supply capital to community development financial institutions (CDFIs) and nonprofit housing developers to finance affordable housing and related community development activities.[12] The CMF uniquely combines several features to empower nonprofits efficiently:

- *Competitive allocation* encourages efficiency by applicants and, if iterated in successive funding rounds, should lead to increasingly effective uses.
- *A leverage requirement* of 10:1 requires that grantees raise additional private capital to stretch Government dollars further. Indeed, many grantees in the initial round report higher than required leverage ratios.
- *Enterprise-level capital* grants helps high-capacity nonprofits increase their scale and magnify their impact. For instance, grant funds deployed as loans can often be recycled as loans are paid off.
- *Accountability for performance,* monitored by the Treasury Department's CDFI Fund, ensures that program dollars are used well.

A few examples of CMF awards demonstrate the range and effectiveness of the program. Volunteers of America National Services used a CMF soft loan to fill the capital gap for Trailside Heights Apartments in Anchorage, Alaska, providing 446 affordable townhomes for families. Habitat for Humanity International used a CMF grant to create a loan fund to help finance affordable homes in California, Florida, and Tennessee. The Low Income Investment Fund used CMF dollars as credit enhancement for land acquisition funds to create 146 affordable apartments for seniors.

Although the CMF was created in HERA, it was never funded by the intended fee on the GSEs. It did, however, receive a single appropriation of $80 million in 2010 (far below the originally intended funding level). That single initial allocation round received $1 billion in applications from 230 organizations, of which nearly half scored into a highly qualified pool. That level of demand and application quality strongly suggests that the CMF could allocate far more funds to great effect, particularly as the competitive dynamic encourages the applicant pool to grow and improve.

[12] This section relies heavily on material produced by the Housing Partnership Network and the Opportunity Finance Network.

Market Access Fund

The Market Access Fund (MAF), if created, would enable participants in the new housing finance system such as lenders, issuers, and guarantors to safely and sustainably serve the broadest possible range of creditworthy borrowers and underserved markets.[13] The MAF would accomplish this goal through competitively awarded grants and temporary credit enhancements that help the private sector find ways to better reach the underserved. Its resources would support a combination of product research and development and testing at a scale sufficient to enable commercial evaluation of new products and processes. In other words, the MAF breaks through the common impasse in which private businesses underserve potentially profitable creditworthy borrowers because it is challenging to invest in specialized systems and products. With the MAF sharing the cost of that initial investment, we can identify ways to serve more housing needs in profitable ways.

Some examples help illustrate areas where the MAF could support useful innovation:

- *Energy efficiency and underwriting:* Household energy costs in this country are about $230 billion annually and make up 15 percent of the total cost of home ownership for average families—even more for lower-income families. Research has found a clear association between home energy efficiency and loan performance, but more research is needed to quantify that link and incorporate it into the mortgage qualification process. Lenders in markets with high energy costs could test using energy savings to adjust their loan underwriting, supported by the MAF.
- *Reserve funds and home ownership success:* To make a downpayment and pay closing costs, low-wealth households often use the bulk of their savings to acquire a home. However, new homeowners with additional liquid reserves have lower default rates. Lenders could experiment with requiring smaller downpayments from borrowers but instead having them contribute to a dedicated reserve fund; this way, they could see if participating borrowers experience lower default rates than similar borrowers who make somewhat higher downpayments but have fewer reserves.
- *Affordable housing preservation:* Owners of affordable rental properties sometimes need to refinance their loans, but often find it difficult to do so at terms that will enable them to keep rents within reach. As a result, affordable units disappear from the market, yet replacing them is less efficient and more expensive than preserving them. One way to fix this problem is to make financing for affordable housing preservation available on better terms, but experiments in doing so will need to be proven before they will become broadly acceptable. MAF resources could help lenders experiment with new ways to serve this market.

Not every experiment will work, nor should we expect them all to. MAF funding will be by nature temporary, so that successful experiments can find a home in the private sector or with specialized lenders and failed experiments can end. Putting the MAF in the hands of an agency with direct understanding of primary and secondary mortgage markets is essential, so that it can measure results accurately and evaluate success or failure. In the framework of S.1217, the FMIC is the logical fit.

The MAF is essential to supplement the housing finance system, but on its own, it cannot fill the overall need for the mortgage market to provide broad access and affordability. It is rather a way to discover and test new tools to better fulfill the goals of access and affordability.

Addressing Housing Need Early To Avoid Emergency Fixes

A large body of research documents the benefits of investments in affordable housing—from transitional housing for homeless individuals and families to rental housing complemented by case management and supportive services to programs supporting affordable home ownership for low- and moderate-income households. Investments in housing early can result in future economic benefits and cost savings.

Myriad studies document the benefits of stable and affordable housing to individual and family well-being, including health, educational opportunities, increased income, and wealth building. Stable, affordable housing helps children's school performance and health, improving outcomes for them and for society. Recent research from Children's Health Watch demonstrated that children living in overcrowded

[13] This section relies heavily on material produced by the Center for American Progress (CAP). The Market Access Fund concept was developed by the CAP's Mortgage Finance Working Group, in which NHC participates.

housing or in families that cannot consistently afford their rent are at increased risk of poor educational outcomes, developmental delays, and hospitalizations compared with other children.[14] Stable and affordable housing is associated with fewer school disruptions, better academic performance, and greater school and community involvement by families.[15] A substantial amount of research has been done to demonstrate the link between education outcomes and future economic prospects for children. In fact, there is little debate about the relationship between academic performance and future earnings (positive relationship), future receipt of public assistance (negative relationship), and future incarceration (negative relationship). As a result, these relationships suggest positive impacts on the economy through higher taxes paid on higher wages and lower use of publicly funded services. Finally, a study by McKinsey and Company Consulting concluded that if the gap in test scores between poor and wealthy students could be closed, yearly gross domestic product would be trillions of dollars higher, or $3 to $5 billion dollars per day higher.[16]

Housing the homeless is perhaps the clearest example of cost-effective housing intervention. Several researchers have found that there are higher rates of emergency room use and hospitalization for mental health and substance abuse problems, and longer in-patient hospital stays, for homeless adults compared with other very low-income individuals.[17] A study of supportive housing in New York City found that homeless individuals who received supportive housing were less likely to be hospitalized or incarcerated than comparable homeless individuals who did not receive services. The authors found that the costs of the supportive housing were offset by the savings in health care, law enforcement, and other service utilization.[18] Additional studies in Seattle, Los Angeles, and Maine reached similar conclusions about the cost effectiveness of investing in permanent supportive housing, specifically finding that for every dollar invested in programs offering long-term housing and services for homeless individuals, there is an average saving of two dollars in terms of other publicly funded services.[19] Additional research has shed light on the relative costs associated with housing families in temporary shelters compared to providing families with rental subsidies. The analysis of homeless families in four U.S. jurisdictions found the average cost of housing a family in a shelter for 1 year was about four times the cost of providing a rental subsidy to that same family, suggesting that investment in rental subsidies was a much more cost effective way of meeting homeless families' needs.[20] In short, making stable housing available to end and prevent homelessness is cost effective.

Housing counseling is a second example of cost-effective preventative housing assistance. Studies have found that housing counseling can prevent foreclosure in times of distress, reduce family housing costs, and reduce the likelihood of mortgage delinquency.[21] A nationwide study of the foreclosure mitigation counseling program

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[14] Children's Health Watch. 2012. "Stable, Affordable Housing Supports Young Children's Health in Philadelphia". *http://www.childrenshealthwatch.org/upload/resource/12_05_PAhousingbrief.pdf* accessed 11/4/2013.

[15] Brennan, Maya. 2011. "The Impacts of Affordable Housing on Education: A Research Summary". Washington DC: Center for Housing Policy. *http://www.nhc.org/media/files/Insights_HousingAndEducationBrief.pdf.* Maya Brennan and Jeffrey Lubell. 2007. "Framing the Issues—The Positive Impacts of Affordable Housing on Education". Washington DC: Center for Housing Policy. *http://www.nhc.org/media/documents/FramingIssues_Education1.pdf.*

[16] Hernandez, Javier C. 2009. "Study Cites Dire Economic Impacts of Poor Schools". *New York Times. http://www.nytimes.com/2009/04/23/nyregion/23klein.html?_r=0* accessed 11/4/2013.

[17] Kushel, M.B., Perry, S., Bangsberg, D., Clark, R., and Moss, A.R. (2002). "Emergency Department Use Among the Homeless and Marginally Housed: Results From a Community-Based Study". *American Journal of Public Health,* 92, 778–784. Kuno, E., Rothbard, A.B., Averyt, J., and Culhane, D. (2000). "Homelessness Among Persons With Serious Mental Illness in an Enhanced Community-Based Mental Health System". *Psychiatric Services,* 51, 1012–1016. Salit, S.A., Kuhn, E.M., Hartz, A.J., Vu, J.M., and Mosso, A.L. (1998). "Hospitalization Costs Associated With Homelessness in New York City". *The New England Journal of Medicine,* 338, 1734–1740.

[18] Culhane, D.P., Metraux, S., and Hadley, T. (2002). "Public Service Reductions Associated With Placement of Homeless Persons With Severe Mental Illness in Supportive Housing". *Housing Policy Debate,* 13, 107–163.

[19] Ludwig, Terri. 2013. "To Curb Medicaid Spending Tomorrow, Invest in Housing Today". *http://www.huffingtonpost.com/terri-ludwig/curb-medicaid-spending_b_4117001.html* accessed 11/4/2013.

[20] Culhane, D.P., Metraux, S., Park, J.M., Schretzman, M., and Ventura, J. (in press). "Testing a Typology of Family Homelessness Based on Patterns of Public Shelter Utilization in Four U.S. Jurisdictions: Implications for Policy and Program Planning". *Housing Policy Debate.*

[21] Laura Williams, Center for Housing Policy, "The Role of Housing Counseling in Reducing Mortgage Delinquency and Foreclosure", 2011, fact sheet available at *http://www.nhc.org/media/files/Role_of_Housing_Counseling_in_Preventing_Foreclosure.pdf.*

found that borrowers who had missed a payment on their mortgage were 45 to 50 percent more likely to get up-to-date on payments if they received counseling. The same study found that households who received counseling had on average lower monthly payments and were 45 percent more likely to sustain their mortgage modifications.[22] Furthermore, most studies of prepurchase counseling find that it reduces mortgage delinquency. Making housing counseling an integral part of mortgage finance would build on the lessons learned during the foreclosure crisis, namely, that housing counseling improves outcomes for borrowers, lenders, and neighborhoods alike by helping more families sustain home ownership.

The foreclosure crisis also provides a cautionary example of the costs of failing to act early. Allowing waves of foreclosure to occur, particularly concentrated in vulnerable neighborhoods, triggered a vicious cycle of disinvestment that has proven expensive and difficult to break.[23] Preventing foreclosures and avoiding long-term vacancy by acting earlier would have avoided costly neighborhood rebuilding, better maintained home values, and helped families avoid the pain and cost of displacement.

Making Housing Finance About Shelter

In closing, I urge you again to make shelter an explicit and central goal of housing finance reform. Realign the incentives of the myriad market participants so that the energy and creativity of the private sector makes affordable housing options available broadly, and use targeted programs to fill in the gaps for those harder to serve. I hope that this bipartisan effort will move our country closer to safe, decent, and affordable housing for all in America.

Thank you again for the opportunity to be here. I am glad to answer questions from the Committee.

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[22] Neil Mayer, et al. 2010. "National Foreclosure Mitigation Counseling Program Evaluation: Preliminary Analysis of Program Effects". Washington, DC: The Urban Institute.

[23] For an overview, see, "Understand Why Foreclosures Matter" on the Center for Housing Policy's site foreclosure-response.org, at *http://www.foreclosure-response.org/policy_guide/why_foreclosures_matter.html.*

Multifamily Housing Finance Reform Proposal for Corker-Warner

Mortgage Finance Working Group
August 2013

We recommend incorporating the following provisions specifically related to multifamily housing finance into S.1217: Housing Finance Reform and Taxpayer Protection Act of 2013 ("the Act"). These recommendations are intended to replace Title VI of the Act.

- **Spin off the current multifamily operations at Fannie Mae and Freddie Mac into two private entities, initially owned by the federal government.**

    - Effective immediately, direct Fannie Mae and Freddie Mac to spin off their current multifamily operations into two independent private, bankruptcy-remote entities, including all assets, staff, systems and other resources necessary to be a self-supporting and separately functioning entity.
    - The new entities will ensure that any multifamily business continues to operate, as applicable, consistent with the Fannie Mae DUS Model and the Freddie Mac CME Program K-Series.
    - Treasury will ensure that the new entities have sufficient capital to carry out the operations of issuing securities, including the ability to obtain warehouse lines of credit.
    - These new entities remain under the supervision of FHFA, later to be transferred to the FMIC when it is fully operational.
    - The new entities will contract with Fannie Mae and Freddie Mac to manage the wind down of Fannie's and Freddie's existing multifamily portfolio.
    - When the FMIC is fully operational, transfer the guarantor function at both companies to the FMIC at no cost to the government. From that point on, the two entities will be able to purchase government insurance from the FMIC on qualifying multifamily securities.
    - When the FMIC is fully operational, require the two entities to raise capital from private sources with the option to buy out the government's interest.

- **Establish a separate insurance fund within the FMIC for qualifying multifamily mortgage-backed securities.**

    - In exchange for a fee, the FMIC shall insure the payment of principal and interest on a covered multifamily security with respect to losses that may be incurred on such security.
    - Levels of risk sharing in the multifamily market must comply with Section 202 of the Act. The private risk-taking capital incorporated in the Fannie DUS Model and the Freddie CME Program K-Series already meet this requirement.
    - In times of market disruption, the terms under which the federal government offers its guarantee can be expanded with the written agreement of the Federal Reserve Chairman and the Secretary of the Treasury, in consultation with the HUD Secretary, per Section 205 of the Act.
    - The FMIC sets a fee for this insurance that covers risk to taxpayers and is subject to calibration based on pre-determined criteria that considers market conditions.
    - The FMIC holds all guarantee fees, minus operating costs, in a Multifamily Housing Insurance Fund, backed by the full faith and credit of the U.S. government. The Multifamily Housing

Insurance Fund must be separate from the single-family Mortgage Insurance Fund established under Section 203 of the Act.

- A covered multifamily security must be comprised of mortgages financing properties of five or more rental units with terms of 5-35 years. The FMIC shall establish at least one pilot program to test the securitization of rental properties with less than five units.
- The FMIC will establish uniform processes, contracts, documents, data disclosures, and other appropriate standardized rules, consistent with the provisions in Subtitle C of the Act for covered single-family securities.

- **Allow other private issuers of qualifying multifamily securities to purchase FMIC insurance, after approval from the FMIC.**

  - Require the FMIC to establish a third qualified multifamily issuer to develop, securitize, sell, and otherwise meet the multifamily issuing needs of credit unions, community and mid-size banks, and non-depository mortgage originators with respect to covered securities. The structure and limitations of this new entity will be similar to the "FMIC Mutual Securitization Company" established under Section 215 of the Act.
  - When the FMIC is fully operational, allow other private entities to issue qualifying multifamily mortgages with the option of purchasing FMIC insurance. Each new entity must be structured as a mono-line businesses, with segregated assets and separate capital standards.
  - All new issuers of covered multifamily securities must be approved by the FMIC through the process laid out in Section 213 of the Act. In addition, any new issuer must show:
    - Experience with multifamily housing finance, including financing of properties with fewer than 50 rental units and in a variety of markets and geographies;
    - Experience with subsidized affordable rental housing properties;
    - Ability to meet the portfolio affordability requirements; and
    - Ability to foster a liquid capital market for multifamily mortgages in a wide variety of markets and geographies.

- **Establish a minimum affordability threshold and other requirements for any issuer of FMIC-backed multifamily securities.**

  - For any issuer of covered multifamily securities, at least 60 percent of the total rental housing units financed in the entity's overall FMIC-backed loan portfolio must at time of origination have been for units whose rents were affordable to households earning at or less than 80 percent of Area Median Income for the locale in which such units were located. For this purpose, "affordable" means the tenant pays no more than 30 percent of their monthly income on rent. The percent of total rental units should be calculated based on a rolling average of at least one year.
  - Annually, each issuer of covered multifamily securities will work with the FMIC to create a plan for serving communities and market segments not well-served by private capital, including low-income communities, rural communities, subsidized affordable multifamily housing and small rental properties. At the end of each year, each issuer must report on their performance toward that plan.

- Each issuer of covered multifamily securities must, on an annual basis, demonstrate compliance with the above provisions to maintain FMIC approval for future issuances.

- **Require private entities to pay a fee on all FMIC-backed multifamily securities to fund the Housing Trust Fund and the Capital Magnet Fund.**

  - The FMIC charges and collects a fee of 5-10 basis points of the outstanding principal balance of eligible mortgages collateralizing covered multifamily securities, consistent with Section 401 of the Act, to fund the Housing Trust Fund, as described in Section 402 of the Act, and the Capital Magnet Fund, as described in Section 403 of the Act.

- **Establish the FMIC as regulator of the entire secondary multifamily mortgage market.**

  - Establish a separate Office for Multifamily Finance within the FMIC, run by a Deputy Director for Multifamily Finance, with the responsibility to manage the Multifamily Housing Insurance Fund and ensure that participants in the secondary multifamily mortgage market (both covered and purely private) abide by all applicable nondiscrimination and consumer protection laws and minimize risk to taxpayers.
  - The FMIC is responsible for approving and overseeing all private mortgage insurers, servicers, issuers and guarantors associated with covered multifamily securities, consistent with Subtitle B of the Act. The FMIC is authorized to suspend or revoke approved status and impose an appropriate civil money penalty of any approved entity that fails to comply with the rules of the FMIC, consistent with Subtitle B of the Act.
  - The FMIC is authorized to develop, publish and adopt additional standards or requirements as necessary to ensure the availability of affordable rental housing and the liquidity, stability, transparency and competition in the secondary multifamily mortgage market, consistent with Section 216 of the Act.
  - The FMIC will establish uniform processes, contracts, documents, data disclosures, and other appropriate standardized rules for covered multifamily securities, consistent with the provisions in Subtitle C of the Act for covered single-family securities.
  - Each fiscal year the FMIC produces a report on the state of the Multifamily Housing Insurance Fund and the covered lending activity from the prior year, including overall volume and rental units financed, affordability of those units, and activity directed to communities and market segments not well-served by private capital, including low-income communities, rural communities, subsidized affordable multifamily housing and small rental properties..
  - The FMIC is authorized to conduct research, create indices and publish reports on the state of the multifamily housing finance industry, comparable to the research being done for the single-family industry.

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NATIONAL HOUSING CONFERENCE

NHC POLICY STATEMENT

GOVERNMENT SUPPORT FOR THE FINANCING OF MULTIFAMILY RENTAL HOUSING

Final, Sept. 28, 2010

The debate on the future of Fannie Mae and Freddie Mac (the "Government-Sponsored Enterprises" or "GSEs") has focused primarily on the role of these entities in financing single-family homeownership. However, the GSEs have also played a major role in financing multifamily housing, including and especially multifamily rental housing.[1] Given the fundamental importance of multifamily rental housing in meeting Americans' housing needs, any overhaul of the government's role in the nation's housing finance system must ensure the continued availability of capital to preserve and develop multifamily rental housing.

In September 2009, the National Housing Conference (NHC) set out a series of ten principles[2] that NHC believes should guide the debate on the future of the nation's housing finance system and the government' role in that system. The recommendations below build on those initial principles to specify specific guidelines for the future of government support for multifamily rental housing (defined here as rental developments with five or more units).[3]

1. **Any restructuring of the nation's housing finance system must ensure the ongoing availability of capital to preserve and develop multifamily rental housing**. Some 15 million U.S. households live in multifamily rental housing, defined as rental housing with five or more units. These households represent more than 13 percent of all U.S. households and nearly 43 percent of U.S. renters.[4] Reliable capital sources are needed to enable the multifamily rental sector to continue to meet America's housing needs.

2. **Multifamily housing finance must be addressed squarely and directly**. While many of the proposed systems for providing government support for single-family lending could be adapted to meet the needs of the multifamily rental housing market, not all would work equally well. Multifamily finance must be addressed directly, rather than as an afterthought to the larger debate.

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[1] While these principles focus specifically on multifamily rental housing, we note that many of the considerations applicable to financing multifamily rental housing also apply to financing multifamily condominiums and cooperatives.

[2] Available here: http://www.nhc.org/media/files/NHC_Housing_Finance_Policy_Principles_FINAL1.pdf.

[3] These recommendations build on the findings of an analysis commissioned by NHC and prepared by Recap Real Estate Advisors. The analysis is based on interviews Recap conducted of a wide range of practitioners as well as their own experience in the multifamily sector.

[4] 2009 American Housing Survey Table 1-1. U.S. Census Bureau. Access on August, 27, 2010 at http://www.census.gov/hhes/www/housing/ahs/ahs09/ahs09.html.

As the debate proceeds, it will be important to consider the differences between the single-family and multifamily markets. One key difference is the fact that the existing system for financing multifamily housing – particularly the lending supported by Fannie Mae and Freddie Mac – has performed much better than the system for financing single-family housing. As of 2009, the GSEs' current multifamily mortgage and Mortgage Backed Securities (MBS) portfolios had distress rates of less than 1%, compared to roughly 7% for multifamily Commercial Mortgage Backed Securities (CMBS) and roughly 11% for the single-family market as a whole.

The soundness of the GSEs' existing book of multifamily business opens up a range of policy options that merit consideration for more effectively meeting the nation's current multifamily housing needs. These options include relaxing the current constraints on multifamily lending under the conservatorship; introducing some elements of the proposed final solution – such as an explicit government guarantee wrap of securities backed by loans underwritten by the GSEs – now, before new entities are chartered; or even moving forward with a resolution of the multifamily finance system first , without waiting for the single-family foreclosure crisis to play out to more fully assess the extent of the GSEs' single-family losses.

3. **Private capital is indispensable for funding multifamily rental housing, but private capital by itself – without government backing in some form, such as a federal guarantee – is not sufficient to reliably meet the full range of the nation's multifamily finance needs**. In particular, government backing is needed to ensure the ongoing availability of long-term fixed rate mortgages for multifamily housing as well as the availability of credit for multifamily lending during financial downturns. Long-term fixed-rate mortgages help to attract a wider range of investors, ensuring that more multifamily deals can get done and thus helping to boost the supply of multifamily rental housing. They also play an essential role in ensuring properties can comply with the requirements of the Low-Income Housing Tax Credit program over the full fifteen-year compliance period.

   Government backing also provides essential countercyclical liquidity for multifamily lending. As the present financial downturn illustrates, private capital dries up quickly in the event of a financial crisis. Without government backing, financing will be largely unavailable during downturns to fund the preservation and creation of new multifamily rental housing as well as to ensure that existing properties can refinance to ensure their ongoing viability.

4. **To fully meet the diverse range of multifamily housing needs and ensure a competitive marketplace exists to hold down costs and encourage the development of specialized expertise, it is important that government support for multifamily lending be provided through multiple channels.** The Federal Housing Administration has a critical role to play in supporting multifamily lending, particularly for more complicated and non-standard transactions. With more capacity and more flexibility, FHA could meet a broader range of the market's needs. At the same time, however, there are limits inherent in the government structure of FHA that suggest the continued need for GSEs – or successors to the GSEs – that have the authority to assign a government guarantee or other federal backing to multifamily loans and package those loans for sale to the secondary market. As nongovernmental entities, the GSEs can respond more quickly and efficiently to the financing needs of the multifamily rental housing sector and have a greater ability to rapidly scale up in the event a financial downturn causes other financing sources to exit the market.

5. **The most efficient and effective way to provide the additional government backing needed to ensure continued access to capital for multifamily rental housing is to provide for a government guarantee wrap of the Mortgage Backed Securities backed by one or more multifamily loans that the GSEs or their successors underwrite**. The guarantee wrap should ensure timely payment of principal and interest, including full payment at maturity, be explicit in its potential cost, be priced to allow transparency of government exposure, and be focused on public benefit.

   To minimize risks to taxpayers, the GSEs or their successors should be required to maintain minimum capital levels and their lending standards and execution should be carefully overseen by federal regulators. Under this approach, any loan losses not recoverable from the project or lender would be covered first by the GSEs and then by the accumulated guarantee fees. Only if all these sources proved insufficient would taxpayers be responsible for losses.

6. **The government's principal interest is to guarantee loans for housing at rent levels affordable to low-, moderate-, and middle-income households throughout the United States.**

7. **Strong government regulation is necessary and desirable to ensure the safety and soundness of the multifamily financing activities of the GSEs or their successors, as well as to ensure they make multifamily credit available for underserved market segments, including small multifamily loans (5 to 50 units) and in rural, lower income and other underserved markets**. Regulation should help to target GSE involvement in areas where it is most needed without crowding out private capital.

8. **The GSEs or their successors have important roles to play in supporting the financing of affordable housing, including providing long-term fixed-rate financing for low-income housing tax credit properties. But regulators should be careful not to push them to reduce lending standards to unprofitable levels in order to meet arbitrary targets.** A better approach would be for the regulator to work collaboratively with the GSEs to identify opportunities to take advantage of their expertise and market channels to test new approaches that could ultimately be profitable, either on their own, or in conjunction with separately funded subsidy or credit enhancement by the government.

   In addition, funding should be made available to subsidize affordable rental housing for very-low and extremely-low income households through such mechanisms as the National Housing Trust Fund and the Capital Magnet Fund.

9. **The GSEs or their successors will need a limited portfolio capacity for multifamily housing to support many of their core functions**. For example, they may need to season certain types of loans before packaging them for sale to the secondary markets. However, **the large majority of their multifamily business should be to package loans directly for sale to the capital markets.**

10. **It could take several years to transition to a new housing finance system. During this interim period, the existing GSE channels for supporting multifamily lending should be maintained to ensure the ongoing availability of credit for multifamily rental housing.**

RESPONSES TO WRITTEN QUESTIONS OF SENATOR WARREN FROM HILARY O. SHELTON

Q.1. Fannie Mae and Freddie Mac's duty to serve the entire primary market is an important aspect of our current housing finance policy. The duty to serve ensures that creditworthy people in all parts of the country can get access to mortgages with reasonable rates and terms. Without a duty to serve, people in rural areas, lower-income neighborhoods, and primarily immigrant or minority neighborhoods might find that mortgages are no longer readily available.

S.1217 envisions a secondary market with many issuers of Government-guaranteed securities. Unlike Fannie and Freddie, which serve the entire Nation, certain issuers in the S.1217 model may purchase loans only from certain parts of the country or may specialize in targeted loan profiles. Assuming there is a secondary market with several issuers, do you have views on how we could structure and enforce a duty to serve?

A.1. Answer not received in time for publication.

RESPONSES TO WRITTEN QUESTIONS OF SENATOR HEITKAMP FROM SHEILA CROWLEY

Q.1. We have tried to find some kind of actual economic verification of the impact of the affordable housing goals, quantified. Please provide, to the extent that you have actual data, hard data on the impact as we have discussed here.

A.1. Government-Sponsored Enterprise (GSE) activities that meet the affordable housing goals criteria support households with incomes below 80 percent of the area median income. The affordable housing goals were put in place to benefit households at 80 percent of area median income (low income) and 50 percent of area median income (very low income).

The National Low Income Housing Coalition does not have its own data to measure the effectiveness of the GSE affordable housing goals, but we have done a modest scan of what data others may have in order to respond to this question. While it is not possible to discern the precise number of low-income households who would been served absent the goals, it is generally agreed that the goals have allowed access to mortgages and lending in traditionally underserved communities, including low-income communities and communities of color.

Based on the National Community Reinvestment Coalition's analysis of Fannie Mae and Freddie Mac's 2012 Annual Housing Activity Reports, GSE activity that met the criteria the affordable housing goals target amounted to approximately $267 billion, including $41.4 billion of investment in rental multifamily units that met the goals' criteria.

While the affordable housing goals are important, we must note that the goals do not support housing that is affordable to extremely low-income households, those with income at or below 30 percent of the area median or the poverty level, whichever is lower. People with incomes this low generally cannot support mortgages and frequently pay more than affordable levels of rent. In 2011, 76 percent of extremely low-income households spent over half of their income for housing, a level considered a severe cost burden. The market simply can produce and operate housing that this income group can afford, no matter how many goals are set.

That is the rationale for the National Housing Trust Fund (NHTF), which was authorized in 2008 in HERA specifically to expand the supply of housing affordable to extremely low-income households. We are pleased that the NHTF is included on S.1217, the Corker-Warner bill, we object to the addition of other activities to it that were not part of HERA. We urge that the uses of the NHTF remain as written in HERA and that the funding to the NHTF be maximized.

In 2012, there was a nationwide shortage of 7.1 million rental homes that extremely low-income households could afford. We estimate that it would take $30 billion a year for 10 years to close the gap. The funding provided in S.1217 is a good start, but should be increased in further bills developed by the Committee.

In term of the future of the affordable housing goals, NLIHC's position is as follows: It is essential that the U.S. housing finance system assure access to credit for all creditworthy borrowers who want to take out mortgages in order to purchase homes in which they will live. The broadest possible access to credit must reach inner cities and remote rural areas and every geography in between. The U.S housing finance system must affirmatively reach out to all segments of the home-buying market and those lenders who fail to do so must be held accountable.

RESPONSES TO WRITTEN QUESTIONS OF SENATOR COBURN FROM DOUGLAS HOLTZ-EAKIN

Q.1. In your testimony, you highlighted the Government Accountability Office's finding the Federal Government essentially spends $170 billion a year on 160 housing programs, including tax expenditures. Ironically, as the Committee discusses affordable housing, many of these housing programs are subsidizing those with incomes well beyond the typical aim of Federal assistance. Please identify the proportion and total benefit of the mortgage interest deduction and the capital gains exclusion going to households earning over $100,000 per year.

A.1. Using figures by the Joint Committee on Taxation, approximately 77.3 percent of the total benefit of the mortgage interest deduction goes to households earning over $100,000 per year. Approximately 75.2 percent of the total benefit of the capital gains exclusion goes to households earning over $100,000 per year. 76.7 percent of their combined benefit goes to households earning over $100,000 per year.

Q.2. Please identify the maximum home value that can be insured by the single family loan guarantee programs of the U.S. Departments of Agriculture and Housing and Urban Development.

A.2. The USDA's single family loan guarantee program does not contain such limits; instead the program is limited to applicants with 115 percent of median area income. Loan limits, and therefore the maximum home value, are determined by the applicant's ability to repay the loan.

In a high-cost region—the District of Columbia—these loan limits apply for FHA:

	One-Family	Two-Family	Three-Family	Four-Family
FHA (HUD)	$729,750	$934,200	$1,129,250	$1,403,400

Q.3. Many of the 160 Federal housing programs could be consolidated and better targeted to improve the Federal response to our Nation's housing needs. For example, in 2009, the Congressional Budget Office identified savings of over $500 million annually in Community Development Block Grant (CDBG) funding by slightly reducing the amount going to communities whose median incomes exceed 110 percent of the national median income. Would improving the targeting and allocation of existing Federal resources enable Congress to address affordable housing needs without placing new mandates on the private sector or future housing finance system?

A.3. Yes. The GAO report and the CBO report mentioned highlight the fragmented and inefficient nature of Federal housing assistance. Eliminating waste, consolidating overlapping programs, and limiting existing programs to those most in need of shelter would help Congress better address affordable housing needs. New mandates on the private sector are unattractive, especially given uncertainty over the mechanics of the future housing finance system, and the general trend toward the imposition of new regulatory burdens.

Q.4. Many affordable housing advocates have pointed to the need for the Market Access Fund as proposed in S.1217. This policy would place a fee—essentially a new tax—on all federally guaranteed mortgage-backed securities to the tune of $2.5 billion–$5 billion annually. Would you agree the economic impact of this new tax on guaranteed mortgage-backed securities would likely be to increase the cost of home ownership and dampen the housing sector overall? Do you foresee any other unintended adverse consequences of the tax?

A.4. Yes, this tax on guaranteed MBS would increase the cost of home ownership for borrowers, adding to the existing trend of rising housing prices and mortgage interest rates. It would come on top of the impact of pricing for risk (the guarantee fee, which necessarily raises costs for borrowers) and costs associated with new regulatory burdens under the Dodd-Frank Act. It seems perverse to fund an affordability initiative by making housing less affordable.

Finally, the access to dedicated funds could encourage advocates of the Market Access Fund to grow the FMIC to grow beyond its chartered purpose.

RESPONSES TO WRITTEN QUESTIONS OF SENATOR REED FROM ETHAN HANDELMAN

Q.1. In your testimony, you make the case that "investments in housing early can result in future economic benefits and costs savings." You seem to be suggesting that funding the Housing Trust Fund and the Capital Magnet Fund and addressing known rental housing needs prospectively is actually the more cost effective and efficient way to go. Could you connect the dots for us here? Do we have any evidence that these sorts of investments have actually saved money in the past?

A.1. Thank you very much for the question, Senator. As you say, addressing known rental housing needs prospectively is less costly than providing emergency housing assistance or other emergency services. Stable housing, either rental or home ownership, also provides long-lasting benefits to the children who grow up in it, which provides a net benefit to society.

To connect the dots, as you put it, let me highlight the specific example of programs to end homelessness, which save public dollars by reducing demand for emergency services. Providing homeless individuals and families with affordable rental housing and supportive services reduces the need for emergency hospital treatment, temporary shelters, and incarceration. The studies cited in my written testimony show cost savings of as much as two to one in such diverse locations as New York City, Seattle, Los Angeles, and Maine.

Similar evidence exists for housing counseling services, foreclosure prevention, and provision of stable rental housing more generally. Children with stable housing are healthier and perform better in school, which we know improves their future earnings potential with the concomitant benefits to society. As I detail in my written testimony, a large body of research documents the benefits of investments in affordable housing—from transitional housing for homeless individuals and families to rental housing complemented by case management and supportive services to programs supporting affordable home ownership for low- and moderate-income households.

RESPONSES TO WRITTEN QUESTIONS OF SENATOR WARREN FROM ETHAN HANDELMAN

Q.1. Fannie Mae and Freddie Mac's duty to serve the entire primary market is an important aspect of our current housing finance policy. The duty to serve ensures that creditworthy people in all parts of the country can get access to mortgages with reasonable rates and terms. Without a duty to serve, people in rural areas, lower-income neighborhoods, and primarily immigrant or minority neighborhoods might find that mortgages are no longer readily available.

S.1217 envisions a secondary market with many issuers of Government-guaranteed securities. Unlike Fannie and Freddie, which serve the entire Nation, certain issuers in the S.1217 model may purchase loans only from certain parts of the country or may specialize in targeted loan profiles. Assuming there is a secondary market with several issuers, do you have views on how we could structure and enforce a duty to serve?

A.1. Thank you very much for the question, Senator. The duty to serve the entire primary market is indeed an essential part of ensuring the availability of safe, decent, and affordable housing for all in America. Applying a similar obligation to new participants in a multi-issuer system requires careful structuring and enforcement.

First, the duty to serve must be a threshold obligation for issuers who wish to purchase the Government guarantee of their securities. Simply put, if the Government balance sheet is going to be at risk, public benefits should accrue. An efficient, stable, liquid secondary mortgage market that serves all in America, either through home ownership or rental housing, should be a basic premise of the housing finance system.

Fannie Mae and Freddie Mac, if reconfigured to operate in a new system, should meet the threshold obligation. So should any new issuers who wish to issue Government-guaranteed securities. The playing field should be level.

Second, issuers should be obligated to serve all qualified borrowers within their defined area of business, be that a geographic region or product type. Initial approval by the regulating agency (FMIC, for instance) and ongoing oversight are both essential to ensure that issuers do not simply target the lowest-risk, highest-return loans, leaving out qualified but less attractive loans in areas already underserved by capital markets. For the Government backstop to insure the housing finance system effectively, the pools of loans must include all qualified borrowers.

For geographically defined areas, issuers should be obligated to serve the entire area, such as the entire country, a multistate area, or a single large State. Location alone should not disqualify a loan to a qualified borrower from being part of a security. For issuers defined by product type, the regulator should careful scrutinize the proposed product type and its expected borrower profile to determine whether it is compatible with a duty to serve the entire primary market. The regulator should examine both the borrowers expected to be served and those who would not be served by a particular issuer's proposed scope to ensure that the area defined does not leave a subset of the market without access.