April 11, 2014

The Honorable Tim Johnson	The Honorable Mike Crapo
Chairman	Ranking Member
Committee on Banking, Housing	Committee on Banking, Housing
& Urban Affairs	& Urban Affairs
United States Senate	United States Senate
Washington, D. C. 20510	Washington, D. C. 20510

Dear Chairman Johnson and Ranking Member Crapo:

On behalf of community banks and credit unions nationwide, we thank you for introducing the Housing Finance Reform and Taxpayer Protection Act of 2014 discussion draft. This bi-partisan effort to create a secondary market that takes into account the unique needs and the necessity to support and preserve secondary market access for small lenders is greatly appreciated and should not go unnoticed as this reform effort continues. This letter discusses our shared objectives and provides constructive recommended changes to the discussion draft.

It is essential to borrowers and the broader economy that the details of any reforms are done right. We look forward to providing ongoing input on the concerns raised by community banks and credit unions as we continue to review and digest the evolving measures. The current secondary market structure works well for community banks and credit unions and allows them to meet their borrowers' needs. Restructuring of this system is unchartered and untested and therefore raises numerous questions regarding fees and functionality when applied to the real-world marketplace. We understand some of the specific details of the proposal are still to be established and we hope those changes will satisfy our ongoing concerns and address the uncertainty faced by our member institutions.

Credit Union National Association (CUNA), Independent Community Bankers of America (ICBA) and the National Association of Federal Credit Unions (NAFCU) are pleased the discussion draft recognizes that a well-functioning, liquid secondary mortgage market with an explicit government guarantee is critical to the national housing market, communities, and main street lenders. We appreciate the creation of a separate mutual corporation to allow small lenders equal access and to continue to sell individual loans for cash, as they do now. In addition, we are pleased the discussion draft recognizes the need for an extended smooth transition from the current government sponsored enterprises (GSEs) to a model with more private capital at risk.

Any housing reform proposal must ensure equal and competitive access for community banks and credit unions, while avoiding further concentration of the primary and secondary mortgage markets to the largest of lenders and Wall Street firms. It is critical that any increased costs associated with establishing a new housing finance system are minimal and borrowers are not saddled with costs that are higher than necessary.

With these objectives in mind, we have identified the following concerns with the draft legislation and urge you to incorporate our recommendations before moving forward:

1) Issue: Vertical Integration

In the discussion draft, approved guarantors can be affiliated with approved aggregators and can also be an approved private market holder of credit risk. A large depository with all of the above capabilities could dominate the market through pricing, by opportunistically leveraging either its guarantor status, balance sheet, or other types of capital market transactions, depending on market conditions. This could lead to the small lender mutual becoming uncompetitive as it will not have these multiple choices, resulting in additional concentration of the mortgage business to the largest financial institutions and Wall Street firms.

Recommendation

No entity should be permitted to be a guarantor if they are an aggregator or an originator.

2) Issue: Capital Requirements

Under the draft legislation, FMIC would require credit support of 10% for each pool of loans securitized and receiving the FMIC wrap. Standard credit enhancement structures would be approved by the FMIC, along with the guarantors and private market holders of credit risk that would provide them. We are concerned specific requirements could be interpreted to be excessive when compared to the real risk to the taxpayer. The use of opaque securities based or capital markets transactions could give the illusion of strong first loss protection at the 10% level. However, these types of structures may pose excessive risk to the insurance fund as they rely on a liquid market to work and have multiple counterparties to stand behind them. Moreover, use of these types of transactions by the largest originators and aggregators would put any entity, including the small lender mutual, at a competitive disadvantage. This could render the mutual useless. More transparency and flexibility could both protect the taxpayer and maintain an affordable housing market. Upfront use of capital markets transactions would prevent the growth of multiple guarantors, and would not support the development of the TBA market for FMIC securities, both key goals in this reform.

Recommendation

FMIC should require a fully adequate level of capital to stand behind any of the approved credit enhancement structures. This capital should be exhausted before any FMIC guarantee is accessed. Models and historical data should be used to determine taxpayer risk, and the corresponding private capital commitment. As such, we recommend only approved guarantors may provide the required credit support in front of the FMIC guaranty. Upfront capital markets transactions or upfront securities-based transactions would be prohibited. Approved guarantors would be able to engage in capital markets transactions or other types of reinsurance transactions to manage credit risk as needed and as approved by the FMIC.

3) Issue: Additional Regulatory Authority

Under the discussion draft, FMIC becomes another regulator that could add cost and regulatory burden. FMIC would have authority to conduct safety and soundness examinations of small lenders who are approved aggregators to the Common Securitization Platform (CSP). Under the current system, GSEs only review compliance with GSE policies and procedures and generally do not perform on-site audits of most small financial institutions.

Recommendation

FMIC should have safety and soundness examination authority for: a) approved guarantors, b) approved mortgage insurance companies, and c) approved aggregators, originators and servicers that are non-depositories or are a subsidiary of an insured depository with more than $500 billion (indexed over time) in assets. FMIC would rely primarily on the prudential banking regulators for safety and soundness examinations and reviews of approved aggregators, originators, and servicers that are insured depository institutions with assets of $500 billion or less (indexed over time).

4) Issue: Governance of the Mutual and the Common Securitization Platform (CSP)

In the discussion draft, the Mutual would be governed by a 14-member board elected by the membership. However, the draft does not specify nor require the board have representatives from all types of institutions who are members of the Mutual.

Under the draft legislation, the CSP would have a nine-member board of directors elected from the approved members. There is no specific representation for a small lender or the Mutual.

Recommendations

The 14-member board of the mutual should be structured as follows:

- Two community banks
- Two credit unions
- Two non-depositories
- One large financial institution (over $50 billion in assets)
- Two Federal Home Loan Banks
- One housing finance agency
- One outside independent director
- Three at-large members

In addition, the nine-member board of the CSP should be structured as follows:

- CEO of Mutual
- One community bank
- One credit union
- One outside independent director
- Five at-large members

5) Issue: The Application of the Qualified Mortgage (QM) Standard

Under the terms of the discussion draft, the existing QM definition is implied as a standard. Community banks and credit unions urge the Committee to provide more flexibility to community lenders who understand the differing needs of their borrowers. Allowing the Mutual to focus more on meeting the Ability-to-Repay factors instead of the QM standards will enable small lenders to extend additional mortgage credit to the communities they serve. Further, under the proposed language, it is questionable whether smaller institutions could qualify for an exemption, as they can now under CFPB rules.

Recommendation

The revised amendment (*see attachment*) would change the definition to address those concerns. The new language is consistent with the CFPB's Ability-to-Repay (ATR) rule, under which a covered loan is generally in compliance with the rule if it is a QM or meets the ATR's factors for prudent mortgage loan originations.

6) Issue: Multiple Lender Issues

Section 335 of the discussion draft, entitled "Multiple Lender Issues," would require any lender placing a junior lien on a property secured by a covered loan to notify the current servicer of that covered loan of the pending transaction prior to the loan consummation when the combined loan-to-value would exceed 80%. We are concerned this would cause the senior lienholder to solicit the borrower for the same credit transaction.

Recommendation

Lenders should be required to notify senior lienholders of any covered loan upon consummation of any junior lien where the combined loan to value exceeds 80%.

7) Issue: Streamlining Process for Fannie/Freddie Approved Lenders to Join Mutual

The procedure to become an approved lender for Fannie Mae and Freddie Mac is time-consuming for smaller financial institutions. Further, institutions already approved to participate in the current system, and in good standing, may decide a new approval process for joining the Mutual is costly and burdensome. The transition to the Mutual should be as seamless as possible.

Recommendation

Institutions under $500 billion in assets approved to sell loans to Fannie Mae and Freddie Mac at the time of transition should be afforded a streamlined process to become a member of the Mutual.

In conclusion, ICBA, NAFCU and CUNA truly appreciate the Senate Banking Committee's exceptional outreach in the preparation of the discussion draft followed by the ongoing and beneficial conversation as the process advances. We look forward to working with you and the other members of the Committee on this important legislation.

Sincerely,

Camden R. Fine
President & CEO
ICBA

Bill Cheney
President & CEO
CUNA

B. Dan Berger
President & CEO
NAFCU

<u>Suggested QM Amendment to Johnson-Crapo</u>

(29) ELIGIBLE SINGLE-FAMILY MORTGAGE LOAN.—The term ' 'eligible single-family mortgage loan' ' means—

(A) a loan that—

(i) has been originated in compliance with ~~minimum~~ *Ability to Repay* ~~standards~~ regulations issued by the ~~Corporation~~ *Bureau of Consumer Financial Protection* by regulation, provided that such *regulations* ~~standards~~—

(I) are uniform and equal in kind, nature, and application regardless of—

(aa) the originator of the mortgage loan; or

(bb) the role performed by an approved entity with respect to the mortgage loan*, except to the extent such regulations of the Bureau of Consumer Protection allow for certain exemptions*;

(II) ~~are, to the greatest extent possible, substantially similar to the regulations issued by the Bureau of Consumer Financial Protection under section 129C(b) of the Truth in Lending Act (15 U.S.C. 1639c)~~ ; and

(III) permit—

(aa) residential real estate loans secured by a property with 1 to 4 single-family units, including units that are not owner-occupied;

(bb) loans secured by manu

factured homes, as defined by section 603(6) of the National Manufactured Housing Construction and Safety Standards Act of 1974 (42 U.S.C. 5402(6));

(cc) residential real estate loans secured by a property with 1 to 4 single-family units that are originated by a State housing finance agency, as defined in section 106 of the Housing and Urban Development Act of 1968 (12 U.S.C. 1701x);

(dd) loans originated by a Community Development Financial Institution;

(ee) loans originated by a mission-based non-profit lender; and

(ff) loans secured by real property in a permanently affordable homeownership program or community land trust;

(ii) has a maximum original principal obligation amount that does not exceed the applicable loan limitation established under section 304;

(iii) has an outstanding principal balance at the time of purchase of insurance available under title II that does not exceed 80 percent of the value of the property securing the loan, unless—

(I) for such period and under such circumstances as the Corporation may require, the seller agrees to repurchase or replace the loan upon demand of the Corporation in the event the loan is in default;

(II) an approved private mortgage insurer guarantees or insures—

(aa) not less than 12 percent of the unpaid principal balance of the loan, accounting for any down payment required under subparagraph (D), for loans in which the unpaid principal balance exceeds 80 percent but not more than 85 percent of the value of the property securing the loan;

(bb) not less than 25 percent of the unpaid principal balance of the loan, accounting for any down payment required under subparagraph (D), for loans in which the unpaid principal balance exceeds 85 percent but not more than 90 percent of the value of the property securing the loan; and

(cc) not less than 30 percent of the unpaid principal balance of the loan, accounting for any down payment required under subparagraph (D), for loans in which the unpaid principal balance exceeds 90 percent of the value of the property securing the loan; or

(III) that portion of the unpaid principal balance of the loan which exceeds 80 percent of the value of the property securing the loan is subject to other credit enhancement that—

(aa) meets standards comparable to the standards required of private mortgage insurers under clause (ii); and

(bb) is approved by the Corporation;

(iv) has a down payment that is—

(I) for a first-time homebuyer, as that term shall be defined by the Corporation by regulation, equal to not less than 3.5 percent of the purchase price of the property securing the loan; or

(II) for non first-time homebuyers, equal to—

(aa) not less than 3.5 percent of the purchase price of the property securing the loan, if such purchase occurs prior to the system certification date or less than 1 year after the system certification date;

(bb) not less than 4 percent of the purchase price of the property securing the loan, if such purchase occurs during the period that begins 1 year after the system certification date and ends less than 2 years after the system certification date;

(cc) not less than 4.5 per cent of the purchase price of the property securing the loan, if such purchase occurs during the period that begins 2 years after the system certification date and ends less than 3 years after the system certification date; or

(dd) not less than 5 percent of the purchase price of the property securing the loan, if such purchase occurs during any period after the period set forth in subclause (III);

(v) satisfies standards related to establishing title or marketability of title, as may be required by the Corporation, which standards may include the required purchase of title insurance on the property securing the loan;

(vi) contains such terms and provisions with respect to insurance, property maintenance, repairs, alterations, payment of taxes, default, reserves, delinquency charges, foreclosure proceedings, anticipation of maturity, additional and secondary liens, and other matters, including matters that set forth terms and provisions for establishing escrow accounts, performing financial assessments, or limiting the amount of any payment made available under the loan as the Corporation may prescribe; and

(vii) contains such other terms, characteristics, or underwriting criteria as the Corporation, in consultation with the Bureau of Consumer Financial Protection, may determine necessary or appropriate; or

(B) a loan refinanced pursuant to the authority granted under section 305(