NAHB

National Association of Home Builders

Testimony of Jerry Howard

On Behalf of the

National Association of Home Builders

Before the

Committee on Financial Services

Hearing on

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

July 18, 2013

Chairman Hensarling, Ranking Member Waters, and members of the House Financial Services Committee, I am pleased to appear before you today on behalf of the National Association of Home Builders (NAHB) to share our views on the *Protecting American Taxpayers and Homeowners (PATH) Act* and the need for comprehensive housing finance reform legislation. We appreciate the invitation to appear before the committee on this important issue.

My name is Jerry Howard and I am NAHB's Chief Executive Officer. NAHB represents over 140,000 member firms involved in building single family and multifamily housing, remodeling, and other aspects of residential and light commercial construction. Each year, NAHB's builder members construct about 80 percent of all new housing in America.

NAHB commends the Chairman for starting the dialogue in the House of Representatives about long-overdue reforms to the housing finance system. After years of conservatorship for Fannie Mae and Freddie Mac, it is time for Congress to address this critical issue. The PATH Act begins this process, and while the draft bill includes some constructive legislative proposals supported by NAHB, we strongly believe that it diminishes housing as a major policy priority for this nation. Rather than reform and restructure the basic housing finance system, the PATH Act dismantles the Housing Government Sponsored Enterprises (GSEs) and deflates the Federal Housing Administration (FHA) by both removing and diminishing the federal support critical to meet our nation's current and future mortgage liquidity needs.

Past abuses, by nearly all participants in the financial industry, combined to create a tragic impact on the well-being of our country. The early stages of the economic downturn became evident in the housing finance arena due in large part to the origination of excessively risky mortgage products and an overly zealous securitization market. The resulting meltdown of the mortgage finance industry led, ultimately, to the crises in the financial markets as a whole.

Today's mortgage finance system is in a state of uncertainty. There is no clear path for housing finance reform, or agreement on the components of reform. However, nearly all system participants agree that reform is critical to the economic recovery of this nation. NAHB believes that legislation to address the past abuses should be designed to ensure transparency, as well as safety and soundness in the housing finance system, but not so restrictive as to impede viable transactions by home buyers, lenders, and investors.

America's future housing finance system must be designed to ensure that creditworthy borrowers have access to prudently developed and underwritten housing finance options and therefore are provided the opportunities bestowed in the Housing Act of 1949. Directly resulting from the recent negligence and mismanagement in the financial industry, millions in the U.S. are suffering from the loss of employment and are thereby increasing the burden on the national government to extend unemployment benefits and other supports to citizens we can, and should, put back to work. No other industry in the country depends more on the U.S. labor force to manufacture its product than the housing industry. Homes and apartments are not manufactured overseas and shipped to the U.S to sell – we build and sell our products right here in the U.S.A.

NAHB believes that the U.S. housing finance system should be multifaceted with both competing and complementary components, including private, federal and state sources of capital. The system should support a reasonable menu of sound mortgage products for both single family and multifamily housing, governed by prudent underwriting standards and adequate oversight and regulation.

NAHB supports policies designed to ensure that the United States is the best-housed nation in the world. The Housing Act of 1949 pledged a "decent home and a suitable living environment for every American family." The American dream of homeownership, as well as the availability of decent, safe and affordable rental housing, should continue to be supported by federal policy within reasonable, safe, and sound parameters. NAHB believes this goal should be emphasized in U.S. housing policy and urges this committee to reestablish housing as a national policy priority.

First, NAHB urges the committee to make changes to the PATH Act to ensure that the federal government continues to provide a backstop for a reliable and adequate flow of affordable housing credit in all economic and financial conditions. 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 has made recommendations to this committee outlining a plan by which Fannie Mae and Freddie Mac would be gradually phased into a private-sector-oriented system, where the federal government's role is explicit, but its exposure is limited. Federal support should be limited to catastrophic situations where carefully calibrated levels of private capital and insurance reserves are depleted before any taxpayer funds are employed to shore up the mortgage market. NAHB believes federal support is particularly important in continuing the availability of the affordable 30-year fixed-rate mortgage, which has been a staple of the U.S. housing finance system since the 1930's. As currently drafted, the PATH Act does not provide the federal support necessary to ensure a strong and liquid housing finance system, and we urge the committee to make the necessary changes.

Secondly, NAHB urges the committee to make modifications to the sections of the bill outlining changes to the Federal Housing Administration (FHA). Taken as a whole, the PATH Act represents a drastic diminishing of FHA's vital liquidity mission. By simultaneously leaving all federal support for housing to the FHA, and then by greatly reducing the overall scope and reach of the FHA's programs, the PATH Act will greatly limit homeownership and rental housing opportunities for many qualified Americans. While we believe that the private market should be the primary source of mortgage financing, that market remains extremely limited.

NAHB has long advocated for reforms to keep the FHA financially solvent and stable, and will continue to support any and all reforms to accomplish this goal. Nevertheless, we strongly support the ability of the FHA to serve a broad group of potential homeowners and renters, especially in times of economic crisis and recovery when private sector lending participants have not yet returned to the marketplace. NAHB urges the committee to make the changes necessary in the PATH Act to preserve FHA's vital liquidity mission.

NAHB looks forward to working with all members of this committee to make these necessary changes.

TITLE I – Wind-down of Fannie Mae and Freddie Mac
GSE Bailout Elimination and Taxpayer Protection Act

Incorporated in the PATH Act is the "GSE Bailout Elimination and Taxpayer Protection Act " that lays out the steps to wind-down Fannie Mae and Freddie Mac (the Enterprises) while encouraging the return of a private market without a federal government guarantee.

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 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'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. 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.[1]

<u>Section 103. Termination of Conservatorship; Mandatory Receivership.</u>

Five years after the enactment of PATH, Fannie Mae and Freddie Mac would be put into receivership and stripped of their government charters. As noted above, while NAHB agrees that Fannie Mae and Freddie Mac should be phased out and the market should transition to a new mortgage securitization system, NAHB does not support removing all government support from the conventional mortgage market. In addition, NAHB believes that a transition must be done in an orderly fashion over time and should not conclude until a viable alternative system is fully functioning. There is no mention of a transition to a new secondary market system in Title I, although the PATH discussion draft offers a plan for transition to a market utility in the third section titled, *National Mortgage Market Utility Act of 2013.* NAHB urges the Committee to carefully evaluate transition issues to ensure that any changes do not cause market disruptions or dislocations.

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[1] 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.

Section 104. Limitations on Enterprise Authority; Section 106. Mandatory Risk-Sharing; Section 110. Authority of Receiver to Repeal Enterprise Charter

Many of the provisions in Title I that are intended to shift the market away from its current dependence on the Enterprises already are taking place through mandates by the Federal Housing Finance Agency (FHFA) and the U.S. Department of Treasury (Treasury). In March 2013, FHFA issued a Conservatorship Scorecard that outlined specific objectives and priorities to implement the agency's own strategic plan for how the Enterprises should operate in conservatorship. The Conservatorship Scorecard directed Fannie Mae and Freddie Mac to: 1) raise guarantee fees to be more consistent with the risk-based pricing as it would be in the private market and, 2) incorporate risk sharing in single family transactions of $30 billion of unpaid principal balance for both Enterprises in the year 2013.

The PATH Act would require similar steps in its strategy to wind down the Enterprises – specifying that a credit risk-sharing program should be established between the Enterprises and the private market covering at least 10 percent of the Enterprises' new business each year; and that the FHFA Director ensure, on an annual basis, that the guarantee fees charged by the Enterprises are equivalent to the amount an Enterprise would charge if it were held to the same capital standards as private banks or financial institutions.

Risk Sharing Program

NAHB supports the exploration of risk-sharing structures for the Enterprises' mortgage securities, since such experimentation can provide valuable information that will be useful in structuring first-loss positions for private capital providers in a reformed housing finance system.

Guarantee Fees

NAHB does not support further increases in Enterprise guarantee fees that are not required to ensure the safety and soundness of Fannie Mae and Freddie Mac. Enterprise guarantee fees (or "g-fees") have doubled since 2011 while their risk exposure has dramatically decreased due to more stringent underwriting standards, improving home prices and declining mortgage defaults. Further g-fee increases would have a major adverse effect on both the affordability and availability of credit while having a very uncertain impact in attracting private capital to the mortgage markets. A recent study by the Office of Inspector General of FHFA raises strong questions on the effectiveness of g-fee increases in increasing the flow of private capital. The study states that "significant guarantee fee increases, under some scenarios, could result in higher mortgage borrowing costs and dampen both consumer demand for housing and private sector interest in credit risk."[2]

NAHB supports appropriate charges to those benefitting from government mortgage market support and looks forward to working with Congress and financial market experts to determine the pricing for insurance premiums to be paid by the issuers of mortgage-backed securities receiving a federal government backstop.

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[2] Federal Housing Finance Agency Office of Inspector General, "FHFA's Initiative to Reduce the Enterprises' Dominant Position in the Housing Finance System by Raising Gradually Their Guarantee Fees," Evaluation Report EVL–2013–005, July 16, 2013

Preferred Stock Purchase Agreements

In October, Treasury modified the terms of the Preferred Stock Purchase Agreements (PSPA) structured between Treasury and the Enterprises in September 2008 at the time the Enterprises were placed in conservatorship. Per the agreements in effect today, the Enterprises are required to transfer all of their profits, on a quarterly basis, to Treasury.

The new Treasury agreement also accelerates the winding down of the Enterprises' portfolios by requiring a 15 percent reduction per year until each portfolio is reduced to $250 billion.

NAHB has not taken a position on these Treasury requirements, both of which are maintained in the PATH Act.

<u>Section 105. Modifications to Increases in Conforming Loan Limits</u>

The PATH discussion draft calls for a five-year phased reduction of the conforming loan limit in high-cost areas, from the current ceiling of $625,500 to $525,500. NAHB is concerned that such a phase down does not consider the fragile state of recovery in many of the affected markets and could result in a reversal of the modest recoveries that have occurred. Furthermore, NAHB believes that it is premature to establish a new high-cost conforming mortgage ceiling without an analysis of such impacts. Conforming loan limits in the new conventional mortgage system that NAHB is proposing would be established based on an evaluation of the condition of housing markets and level of home prices at the time that system is activated. These loan limits would be indexed to a measure of home prices and adjusted as specified in HERA.

<u>Section 107. Limitation of Enterprise Mortgage Purchases to Qualified Mortgages</u>

Effective for mortgages with application dates on or after January 10, 2014, the PATH Act would only allow the Enterprises to purchase, make commitments to purchase, service, sell, lend on the security of, or otherwise deal in a mortgage that is a qualified mortgage as defined by the regulations issued by the Consumer Financial Protection Bureau (CFPB) in January 2013. The CFPB issued the regulation to implement the "ability to repay" provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act).

In fact, FHFA placed this qualified mortgage restriction on Fannie Mae and Freddie Mac on May 2, 2013 with the exception that Fannie Mae and Freddie Mac will continue to be permitted to purchase loans that meet the underwriting and delivery eligibility requirements stated in their respective selling guides. This includes loans that are processed through their automated underwriting systems and loans with a debt-to-income ratio of greater than 43 percent. Loans with a debt-to-income ratio of more than 43 percent are not eligible qualified mortgages under the CFPB's final rule unless they are eligible for purchase by Fannie Mae and Freddie Mac under the special or temporary qualified mortgage definition.

The PATH discussion draft does not address whether or not Fannie Mae and Freddie Mac will continue to be allowed to purchase mortgages loans with a debt-to-income ratio of greater than 43 percent. NAHB recommends a revision to the draft to clarify that such purchases would be permitted.

Section 108. Prohibition Relating to Use of Power of Eminent Domain

The PATH Act would prohibit Fannie Mae and Freddie Mac from purchasing or guaranteeing any mortgage loans that are secured by a structure or dwelling unit located within a county that has invoked the use of eminent domain during the preceding 120 months to seize mortgage loans out of legally binding securities.

NAHB supports this provision. NAHB opposes the use of eminent domain to take mortgages from mortgage-backed securities or financial institution portfolios, which would significantly harm mortgage finance markets, reduce access to credit for borrowers, and undermine efforts to revive the private label mortgage securities market.

TITLE II – FHA Reform

FHA Reform and Modernization Act

The PATH Act lays out a reform plan for the Federal Housing Administration (FHA). The bill would establish FHA as a wholly owned government corporation, removing it from the U.S. Department of Housing Urban Development (HUD), although it would remain as an agency of the United States. The new structure of the agency is defined, along with its purposes and powers, how it would be funded, eligible activities and specific program parameters, among other items. The bill also appoints the Federal Housing Finance Agency as the safety and soundness regulator of the newly reformed FHA and describes how FHA would function during its transition from an agency of HUD to an independent government corporation.

NAHB is supportive of reforms to FHA to ensure that FHA is able to maintain its critical mission of facilitating the flow of mortgage credit to homebuyers and producers of rental housing. FHA has a long track record of achievement in insuring loans for over 37 million American families, many of whom would not otherwise have been able to own a home. FHA pioneered the concept of a 30 year fixed-rate mortgage and low down payments, and the nation still benefits from that program today. FHA maintains strong underwriting criteria to protect the tax payers and is intended to be self-funded through the upfront and annual mortgage insurance premiums that borrowers pay.

Contrary to the belief of some, FHA is not a subprime lender and has never required a federal bailout. Although the single family mortgage insurance program is experiencing shortfalls in its excess reserves due to the effects of the worst economic downturn since the Great Depression, FHA remains an integral part of our nation’s economic recovery. Since the downturn in the housing market, FHA has become the primary source of mortgage credit for first-time home buyers, minorities and those with limited downpayment capabilities as other sources of mortgage credit have disappeared. NAHB believes that the private market should be the primary source of mortgage financing, but that market is extremely limited. While these circumstances prevail, it is entirely appropriate for FHA and other federally backed programs to continue to have a larger than historical market share.

FHA historically also has played an important role in the financing of multifamily rental housing and provided critical support during the recent economic crisis. In 2008, FHA endorsed just over $2 billion in multifamily loans (excluding health care programs), which grew to $14.6 billion in FY2012. This unprecedented increase in FHA multifamily loan volume occurred as other private market sources of multifamily financing withdrew from the market as economic conditions worsened. FHA, along with Fannie Mae and Freddie Mac, are the primary sources of multifamily financing today. Like in the single family market, the FHA multifamily mortgage insurance programs are fulfilling the function and mission for which Congress originally intended. Further, the FHA multifamily programs generate revenue over and above what it costs to administer the program and fulfill claims.

Within this context, NAHB provides the following comments on Title II.

Subtitle A - Organization

NAHB supports the proposed restructuring of FHA as a wholly owned government corporation. NAHB believes, however, that rather than removing FHA from HUD, that reform of FHA can best be accomplished by restructuring FHA as an independent government corporation within HUD, separate from Ginnie Mae. FHA would continue its current mission of supporting liquidity, innovation and continuity in the housing finance markets by providing mortgage insurance backed by the full faith and credit of the U.S. government. In NAHB's view, a restructured FHA would be led by a chief executive officer, appointed by the President, who would report to a presidentially appointed board, chaired by the HUD Secretary.

The PATH Act contains provisions that are similar to NAHB's position on a restructured FHA. For example, NAHB believes that, while under general Congressional oversight, FHA should have the authority, without further Congressional action, to create or alter specific insurance programs in order to have the flexibility to react promptly to changes in market and other conditions. NAHB also supports provisions by which hiring, salaries, personnel management, and procurement would be freed from current, confining federal government constraints in order to be more consistent and competitive with the private sector. Further, NAHB agrees that FHA should be operated in a manner that does not require a federal subsidy and that FHA should be allowed to retain revenues generated in excess of expenses to be used for mission purposes.

Section 212. Purposes

The PATH Act sets forth the purposes of the newly reformed FHA. In the single-family area, FHA is to provide mortgage insurance and other credit enhancements for single-family homeownership for first-time homebuyers, low-and moderate-income (LMI) homebuyers, homebuyers in counter-cyclical markets and disaster areas. While NAHB agrees that FHA should continue to support these homebuyers, we oppose these limitations in FHA's assistance. FHA currently serves a broader group of potential homeowners and is available during all economic cycles, and NAHB believes that it should continue to do so.

The FHA single-family mortgage programs are a unique and vital component of the housing finance system, providing access to homeownership for underserved communities, primarily first-time homebuyers, minorities and those with limited downpayment capabilities. During the recent mortgage crisis FHA demonstrated how invaluable their counter-cyclical role is in providing mortgage market liquidity during the country's unstable housing market system. Although this role has not been without costs to the FHA program, as evidenced by the recent actuarial studies of the FHA's Mutual Mortgage Insurance Fund (MMIF), numerous steps have been taken to address these issues.

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 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. FHA's 2012 Actuarial Report estimates that the changes in credit policy and pricing have added more than $20 billion in economic value to the fund from 2010 through 2012. This year HUD announced even more steps it will take to improve the health of the fund and expects that these measures, coupled with an estimated additional $11 billion in capital from new business in FY 2013, will return FHA's capital reserves to a positive position within the year.

In the multifamily sector, NAHB also agrees that FHA should continue to support the provision of affordable rental housing. NAHB has long-supported the FHA multifamily mortgage insurance programs. These programs, notably Section 221(d)(4) and Section 223(f), have enabled the construction of needed affordable and market rate rental housing units over the years, as well as contributed to the ability of property owners to acquire, refinance, rehabilitate and preserve 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. NAHB does not support a narrowing of FHA's mission as it relates to supporting the multifamily rental housing market.

NAHB also supports as a purpose the engagement in research, development and testing of new products designed to make single and multifamily housing and residential health care facilities available to hard-to-serve markets. Such markets should include rural areas, as well as distressed urban and rural areas.

Lastly, under Section 212(6), NAHB believes that FHA and the U.S. Department of Agriculture (USDA) should jointly consider ways to coordinate related to risk management and loss mitigation for the FHA and Rural Housing Service (RHS) programs. However, FHA should not control the operations and practices of an agency (RHS) within the USDA. NAHB has supported the joint efforts of HUD, USDA, and the Treasury to coordinate and streamline administrative practices and procedures and in some regulations for the multifamily programs, which often are funded in conjunction with each other (such as Low Income Housing Tax Credits, HOME, FHA multifamily mortgage insurance, and rental housing assistance). These efforts show promise in making the use of these programs more efficient and productive.

NAHB believes that all provisions in the draft bill that direct FHA to oversee or set practices for the RHS should be eliminated. NAHB has not supported the transfer of RHS programs to HUD and would not support the transfer or oversight of the RHS programs to a newly reformed FHA. The RHS programs have financed over two million owner-occupied homes and over 500,000 rental units for low and moderate income families living in rural areas. RHS has also provided funding to repair thousands of single family homes, as well as rental assistance to thousands of low-income rural families, many of whom are elderly or disabled, and financing to provide migrant housing. The RHS programs are uniquely structured to address the housing credit needs of low and moderate income persons in rural areas, which are very different from those found in urban and suburban areas. This oversight responsibility could lead to the consolidation of the RHS programs into FHA programs, which NAHB believes would result in the loss of the important network of state offices that administer the RHS programs, making it more difficult and expensive for persons living in rural areas to obtain an affordable mortgage to purchase a home.

Section 218. Applicability of Laws.

While NAHB supports giving a newly restructured FHA broader powers than it currently possesses as a means to foster more efficient and modern products and services, we believe that FHA must continue to be subject to applicable laws related to notice and comment rulemaking. Section 218 of Title II exempts any matter relating to credit enhancement or other business of the FHA from such laws, which we do not support. While NAHB supports streamlining of the regulatory process, which currently is too time-consuming, it is critically important for purposes of transparency that a newly reformed FHA provide notice and comment opportunities to stakeholders and interested parties. Government agencies become better informed as to the viability of their proposals during the comment and rule making period, and although the end result may not be reflective of all comments, the consequences of government decisions – positive and negative - become more evident as a result of constructive public input.

Subtitle B – Business Authority and Requirements

Section 232. Eligible Single Family Mortgages

Mortgage Amount

The PATH Act establishes limits on the mortgage amount for single family mortgages eligible for FHA insurance as the lesser of: 1) 100 percent of the appraised value of the property and 2) 115 percent of area median income (AMI) or 150 percent of the Freddie Mac limit (currently $625,500). NAHB notes that these mortgage limits are consistent with those in the FHA Modernization Act of 2008 enacted as part of the Housing and Economic Recovery Act (HERA) of 2008 (P.L. 110-289). The current FHA single family loan limits which are the lesser of 125 percent of AMI or 175 percent of the Freddie Mac limit will be rolled back to the HERA limits at the end of this year. While the proposed limits are consistent with current law, we seek clarification on the definition of the Freddie Mac limit once Freddie Mac's charter is repealed pursuant to Section 110 of the PATH Act.

The PATH Act would also reduce the minimum FHA loan limit or "floor" to no lower than $200,000, down from the current floor of $271,050. NAHB estimates that the reduction in the floor would result in lower limits, relative to the HERA limits, in 2,692 counties, which account for 56 percent of the occupied housing units in the country. Given the large impact of affected housing units, NAHB opposes the reduction in the floor and supports continuation of the current formula for the FHA floor as specified in HERA.

Downpayment

The bill also proposes changes to the minimum downpayment required. First-time homebuyers would be required to provide a 3.5 percent downpayment, and a five percent downpayment would be required from other borrowers. NAHB is concerned that increasing the downpayment from 3.5 percent to five percent will create a substantial burden for all American homebuyers, especially younger buyers and those with strong credit profiles but not enough available funds to make the increased downpayment. Also adversely affected will be current homeowners looking to move up who will not be able to do so because of the reduced number of qualified borrowers.

The increased downpayment burden provides minimal benefits. Research has shown that requiring a higher downpayment does little to reduce risk of default but causes homebuyers to use more of their reserves for the downpayment. This is particularly true for low and moderate-income families seeking to become homeowners. Sound underwriting is the key to minimizing foreclosures and defaults, not downpayments.

Public Purpose Requirement

Section 232 also establishes a public purpose requirement for FHA based on the purposes enumerated in Section 212. The bill restricts FHA single family mortgage insurance to loans that meet one of the following criteria:

(1) first-time homebuyer
(2) low or moderate income homebuyer, defined as a family having an income less than 115 percent of the area median income (AMI) or 150 percent of AMI in high cost areas, which are defined as areas where the median one-family house price exceeds the Freddie Mac limit in effect for that year. (It is not clear what this house price limit might be once Freddie Mac is no longer in existence.)
(3) property is located in a counter-cyclical market (as determined by the FHFA Director and the FHA Chief Risk Officer, CRO)
(4) property is located in a Presidentially-declared disaster area.

As noted previously, NAHB opposes the restriction of FHA's support to these loan categories. Further, NAHB has concerns regarding the counter-cyclical market adjustment specified in Section 232 (C) which would restrict the availability of FHA loans unless:

- there is a joint determination by the FHA Director and Chief Risk Officer that available credit in a specific county or counties has contracted significantly, as measured by a credit availability measure of the Office of the Comptroller of the Currency;
- that house prices in those areas have declined significantly, as measured by the FHFA; or;
- that available credit for purchasing homes or other economic conditions exist that show a significant contraction of capital in the such areas as measured by a metric identified by the Director and Chief Risk Officer in a written notice made publicly available and provided to Congress in advance.

NAHB is very concerned that this process is overly burdensome and the determinations required would take too long to effectively address changing economic conditions. Looking at the dramatic increase of FHA's market share of single-family mortgages over the past few years, it is clear how essential the program is for our nation's economic recovery. 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. 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.

Section 233. Risk-sharing

Section 233 requires FHA to develop a demonstration model and standards for entering into risk-sharing agreements for FHA-insured mortgages. FHA is directed to develop the model within two years of enactment after which FHA would be required to enter into risk-share agreements on 10 percent of its single family business. The risk share portfolio must represent a broad cross-section of single family mortgage products.

The risk-share model is to include guidelines for qualification of persons or entities to participate in risk-sharing agreements and other credit enhancement activities with FHA. FHA is to review the FHFA guidelines that apply to the Fannie Mae and Freddie Mac to determine if they are appropriate for the purposes of FHA. The guidelines must ensure that parties participating in risk-sharing have sufficient liquidity, capital, credit worthiness and are other capable of fulfilling their obligations to FHA.

NAHB believes that dividing the risk with private companies would reduce FHA's loss exposure and could have other operational advantages. However, it would also raise the question of FHA's exposure to adverse selection if the private companies limited their participation to the lowest risk portion of FHA's business. This concept also could reduce or eliminate participation by smaller mortgage lenders, particularly community banks, who would have difficulty meeting the eligibility criteria for the program. A change of this nature would also impact the Ginnie Mae mortgage-backed securities (MBS) program by raising Ginnie Mae's exposure to counterparty risk and would likely require significant changes at that end as a result. The bill does not require FHA to consult with or review Ginnie Mae's guidelines, nor does it mention examining any potential impact on Ginnie Mae.

Section 234. Limitation on Mortgage Insurance Coverage

The bill reduces the coverage of FHA mortgage insurance permitted on a loan over time, from the current 100 percent to 90 percent of the original principal obligation for mortgages insured after the expiration of the one-year period beginning on the date of enactment of this act; 80 percent after two years; 70 percent after three years; 60 percent after four years; and 50 percent after five years. These provisions would become effective upon enactment.

NAHB notes that the Department of Veterans Affairs (VA) has operated its Loan Guaranty Program with a lower insurance coverage with positive results. However, the VA program is restricted to a specific portion of the population, the military, and has operating features that may not be replicable for FHA loans. In addition, as in the case of risk-sharing, Ginnie Mae's counterparty risk exposure would increase, necessitating changes in that program as well. The bill does not provide for a demonstration or study of decreasing the degree of insurance on FHA loans, leaving questions unanswered as to its viability and impact on the programs.

Section 235. Premiums

The bill gives FHA the authority to establish and collect mortgage insurance premiums (MIP). In the case of single-family annual premiums, FHA must charge at least 0.55 percent of the loan balance. The MIP must be sufficient to cover: costs of providing MI; administration, operations, management and technology costs for FHA; capital ratios required for the Mutual Mortgage

Insurance Fund (MMIF) and MI for multifamily mortgages; and, salaries and expenses of FHA personnel.

The bill allows the newly reformed FHA to establish a mortgage insurance premium structure involving a single premium payment collected prior to the insurance of the mortgage or annual payments (which may be collected on a periodic basis), or both. The rate of premiums may vary according to the credit risk associated with the mortgage and the rate of any annual premium for such a mortgage may vary during the mortgage term. The FHA would have the discretion to change this structure, but only for new loans.

NAHB believes that calibrating mortgage insurance premiums to the risk profile of the borrower would allow FHA to better align its revenues with potential claims and thus bolster reserves. However, it would also place FHA in the position of raising the mortgage financing costs of the individuals for whom it has a mission to serve. A key consideration in designing a system of risk-based pricing for FHA is the range and weighting of risk-factors used in determining the schedule of premiums.

Section 237. Occupancy and Rent Limitations for Multifamily Mortgage Insurance

The bill allows FHA to provide mortgage insurance for residential properties having five or more dwelling units – multifamily rental housing – subject to occupancy and rent restrictions which are applied during the life of the mortgages. The bill restricts occupancy to families having incomes no greater than 115 percent of 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.

The FHA multifamily mortgage insurance program is an important resource for meeting the need for affordable rental housing. 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.

NAHB does not support setting occupancy and rent restrictions based on AMI for the FHA multifamily mortgage insurance programs. 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.

Subtitle C. Financial Safety and Soundness

Section 251. Authority of Director

The bill provides that the Director of the Federal Housing Finance Agency (FHFA) shall supervise and regulate the safety and soundness of the newly reformed FHA and the programs of the RHS in USDA.

As discussed with respect to our comments on Title I, NAHB has proposed an improved regulatory regime for a reformed housing finance system that would involve replacing FHFA with a new regulator that is better suited to oversee a broader spectrum of responsibilities. Therefore, NAHB does not support assigning FHFA as the regulator over the new independent FHA.

In addition, NAHB does not support giving FHFA the authority to supervise and regulate the RHS. The RHS should continue to be supervised and regulated by the USDA. NAHB does not object, as previously stated, to the coordination of policies and procedures, to the extent appropriate, between FHA and RHS programs.

Sections 256. Mutual Mortgage Insurance Fund (MMIF) Capital Reserve Ratio; Section 257. Capital Classifications and Performance Measures

Section 256 requires FHA to establish separate accounts in the MMIF for legacy loans and for new loans. The FHA must maintain a capital reserve ratio of four percent for new business, double the current two percent statutory capital reserve ratio. Section 257 provides for consequences if the MMIF should become undercapitalized (i.e., a capital ratio of less than four percent) by restricting the degree of insurance provided by FHA. Pursuant to Section 257, the capital classifications and restrictions on new FHA business are:

"Undercapitalized":
- Capital reserve ratio between two and four percent; FHA would be restricted from insuring single family mortgages with a loan-to-value ratio exceeding 90 percent.
- Capital reserve ratio between zero and 2 percent; FHA would be restricted from insuring single family mortgages with a loan-to-value ratio exceeding 80 percent.

"Significantly Undercapitalized":
- Capital reserve ratio less than zero percent; FHA would be subject to enforcement actions determined by FHFA.

In addition, if FHA is classified as undercapitalized or significantly undercapitalized, it would be required to submit a capital restoration plan to the FHFA Director.

NAHB has significant concerns regarding the proposed doubling of the MMIF capital reserve ratio. The increase in the reserve ratio will directly result in higher MIPs for single family mortgages since, pursuant to Section 235, the MIP must be sufficient to cover the capital reserve ratio. Higher MIPs will result in increased costs for the borrowers to be served by the reformed FHA, specifically first-time and low- and moderate-income homebuyers. These homebuyers are the population least likely to be able to bear the brunt of higher mortgage costs and will have fewer available mortgage options other than FHA-insured mortgages.

In addition, NAHB opposes the proposed restriction in FHA business if FHA is classified as undercapitalized. Restricting FHA's ability to serve its core borrowers will not improve the FHA financial position and will harm these borrowers. NAHB has supported past legislative proposals that would require a capital restoration plan, but strongly opposes restrictions in FHA's activities.

<u>Section 259. Capital Reserve Requirements for Other Funds</u>

The bill requires the Director of FHFA to set capital reserve requirements for the General Insurance Fund (GI), the Special Risk Insurance (SRI) Fund, the Cooperative Management Fund, and the Rural Housing Insurance Fund established under Title V of the Housing Act of 1949. 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, we strongly urge 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 purpose of collecting the mortgage insurance premiums (MIP) for the FHA multifamily programs is to collect sufficient sums to ensure that, in the case of defaults, the government can cover the cost of paying off its financial obligations to the lenders. The Federal Credit Reform Act (FCR) of 1990 directs government agencies to provide a realistic picture of the cost of government loans and guarantees. To comply with the FCR in determining the costs of the FHA multifamily mortgage insurance programs, HUD uses an economic model that takes into account the risks and costs of each program and has traditionally set the MIP for a specific program at a level sufficient to protect the integrity of the insurance fund without overcharging borrowers. The practice, since 2003, has been that the MIPs for Section 221(d)(4) and most other programs are set at roughly breakeven levels.

Thus, 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 to the low- and moderate income families who use the program in the form of higher rents or could result in properties not being built or rehabilitated because of the higher equity contribution required.

It is also important to note that HUD, over the last several years, has instituted new risk management protocols for the FHA multifamily mortgage insurance programs. The new protocols tightened underwriting requirements and created a national loan review committee. New policies were implemented for large loans, including higher standards for credit worthiness and experience, and new policy was implemented related to concentration of risk from borrowers with large FHA portfolios. Processes and procedures throughout the field offices have been strengthened and standardized, with more to come as the multifamily office restructuring unfolds over the next couple of years. There is closer scrutiny on market strength and FHA presence than before the economic crisis struck. MIPs were increased in FY2012 for the first time in 10 years. All of these actions have been taken to ensure the health of the GI/SRI fund.

NAHB does not support giving the Director of FHFA the authority to set capital reserve requirements for the Rural Housing Insurance Fund. As stated previously, the USDA should be responsible for the oversight and financial safety and soundness of the RHS programs.

Section 263. Limitations on Seller Concessions

The bill prohibits FHA and RHS from newly insuring any mortgage on a one-to four-family residential property with respect to which the seller of the property (or third party or entity that is reimbursed directly or indirectly by the seller) contributes toward the acquisition of the property by the mortgagor any amount in excess of three percent of the total closing costs in connection with such acquisition.

The Discussion Draft uses a different approach to limits on seller concessions than that in current FHA regulations and HUD's changes to FHA seller concession rules proposed in March 2012. The draft bill proposes seller concession limits as a percent of closing costs, while HUD's proposed rules specify limits based on the lesser of appraised value or sales price, which is the measure used in current rules for FHA, Fannie Mae and Freddie Mac. NAHB strongly recommends that the lesser of sales price or appraised value be the base used to determine the limitation on seller concessions.

NAHB opposes limitations on seller concessions below the current FHA limit of six percent of sales price or appraised value. Seller contributions are an important tool for providing access to affordable homeownership by reducing the amount of upfront monies required for mortgage financing. Prudent methods of assisting a borrower to lower the upfront cash needed to purchase a home create more homeownership opportunities and can leave the buyer with reserves after the purchase to absorb economic shocks and unanticipated costs of homeownership.

Seller concessions are critical to many home sale transactions. Changing seller concessions would be a significant blow for financing both resale and new homes now and in the future. A recent NAHB survey found that seller concessions greater than three percent are used on about 60 percent of new home sales with FHA insurance. The survey also found that 44 percent of respondents need a minimum limit greater than three percent on seller-paid concessions to allow them to serve most of their customers.

The current six percent seller concession limit provides the consumer additional tools and flexibility in affordable financing solutions. In addition to covering portions of buyer closing costs, seller concessions can be utilized to buy down the interest rate making the monthly payment more affordable. While buydowns are less prevalent in today's low mortgage rate environment, NAHB believes it is important that this option is available if and when rates move to less affordable ranges.

The proposed three percent limit on seller concessions also does not adequately address high cost areas and areas with high closing costs. FHA has a mission to facilitate affordable housing as well as a counter cyclical mission to support housing when other finance providers are not present. It seems appropriate that consumers living in high cost or high closing cost areas should be provided with the same concessions as those in lower closing cost areas.

Maintaining current seller concession limits will address these markets and the consumers who live there.

Section 266. Prohibitions Relating to Use of Power of Eminent Domain

The bill prohibits the Secretary and the FHA from newly insuring any mortgage that is secured by a structure or dwelling unit that is located within a county that contains any structure or dwelling unit that secures or secured a residential mortgage loan which mortgage loan was obtained by the State during the preceding 120 months by exercise of the power of eminent domain.

NAHB supports this provision. NAHB opposes the use of eminent domain to take mortgages from mortgage-backed securities or financial institution portfolios. NAHB is concerned that this mortgage restructuring proposal would significantly harm mortgage finance markets, reduce access to credit for borrowers, and prevent private capital from returning to the mortgage market.

Section 267. Residual Income Requirement

The bill prohibits FHA from insuring any new mortgages unless the mortgagor meets sufficient residual income requirements to be established by FHA. Residual income is the mortgagor's net monthly income after taking into consideration defined obligations. Currently only the Department of Veterans Affairs Home Loan Guarantee program utilizes residual income underwriting requirements. This method of loan level analysis has produced lower default rates even through the housing finance crisis.

NAHB could support residual income methodologies if they were fair and responsible enabling reasonable guidelines that both protect FHA's MMIF while providing access to credit for homebuyers.

TITLE III – Building a New Market Structure

National Mortgage Market Utility Act of 2013

The PATH Act would set up a new, non-government, not-for-profit entity to restore a robust secondary market for residential mortgage loans. The National Mortgage Market Utility (the "Utility") would be regulated and supervised by FHFA. Specifically, a Division of Utility Regulation would be established within FHFA and led by a Deputy Director.

The Utility would, by statute, perform most secondary market functions of the Enterprises. Generally, the Utility would establish standards for originating eligible residential mortgage loans; develop standard form securitization agreements; develop servicing and servicer reporting standards; create standard data definitions for all aspects of loan origination, appraisals, and servicing; improve transparency related to the performance of residential mortgages; operate a common securitization platform; provide a central repository for mortgage documents and other mortgage-related information; and provide a uniform procedure for default and foreclosure.

Notably lacking is a provision for a federal guarantee of timely payment of principal and interest on mortgage-backed securities. As noted earlier, NAHB believes the absence of a federal backstop for mortgage-backed securities is a significant failing in the design of the PATH Act's housing finance system. NAHB believes a federal government guarantee is critical to ensure an adequate flow of mortgage capital and to avoid highly damaging disruptions in the delivery of affordable housing credit.

The PATH Act provides for the Utility to have significant latitude in developing and adopting standards, processes and procedures to eliminate the weaknesses in the residential mortgage market that were revealed during the financial crisis. Many of the measures called for by the PATH Act to repair and bolster the housing finance system were previously called for by NAHB in its *Comprehensive Framework for Housing Finance System Reform.* NAHB agrees a new framework must be established to prevent excessive risk taking and to ensure the safe and sound operation of the entire housing finance system so the recent crisis is never repeated. NAHB has identified the following components of reform that would correct the operational and structural problems that produced the housing boom/bust:

- Reform the appraisal system
- Prohibit unsound mortgage products
- Ensure the use of prudent mortgage underwriting guidelines
- Require sound mortgage securities structures and full transparency for MBS investors
- Reform mortgage servicing and foreclosure procedures
- Impose adequate oversight on previously unregulated segments of the mortgage and financial markets
- Ensure reforms are undertaken in a balanced and flexible manner so credit worthy borrowers are not disadvantaged

<u>Section 322. Standards for Qualified Securities</u>

Only Qualified Securities, as specified in the PATH Act, would trade through the Utility. Qualified Securities must meet numerous requirements:

- The Utility will establish classifications of residential mortgages based on various risk parameters. Eligible collateral for Qualified Securities must meet the criteria of a defined risk classification and the Utility will allow for the trading of securities collateralized by each classification of mortgages.

- Eligible collateral must use standard securitization agreements that are developed by the Utility and incorporate requirements related to pooling and servicing; representations and warranties; indemnification and remedies; and trustee responsibilities.

- For a mortgage to be eligible for a Qualified Security, all documents related to the mortgage must be registered with the newly-created mortgage data Repository.

- Servicing and Servicer reporting standards developed by the Utility must be applied to eligible collateral.

- Loan origination, appraisal, and servicing data, including data relating to underwriting criteria, would be available for residential mortgage loans that comprise qualified securities.

As noted above, NAHB has been recommending the types of reforms that are specified in the PATH discussion draft, and we commend the Committee for including such measures. One concern, however is the requirement that a Qualified Security must be collateralized with mortgages all having the same risk classification, which could impair the liquidity of the market for specific Qualified Securities.

Section 331. Organization and Operation of National Mortgage Data Repository

The Utility is directed to organize, establish and operate a Repository for mortgage-related data and mortgage documents. The authorized activities of the Utility with regard to the Repository will generally include all activities required to set standards and procedures for submission, registration, validation, publication, etc. of data and documents to be deposited in the Repository. Activities of the Utility also will include determining qualifications for those depositors of data to the Repository and fees for using the Repository.

NAHB has no specific policy regarding a national mortgage data repository, however, the lack of availability of mortgage data and other information in mortgage loan and securities documents was one of the key problems faced by lenders, servicers, investors and consumers during the crisis as they tried to work out problem loans. NAHB commends the Committee for exploring means to improve transparency in mortgage and mortgage securities transactions.

TITLE IV – Removing Barriers to New Investment

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 account for more than 90 percent of mortgage originations. Access to credit for home builders is even more constricted where, in the current regulatory climate, lenders are very reluctant to make acquisition, development and construction (AD&C) loans.

Since the beginning of the “Great Recession”, Congress, the administration and independent agencies have taken significant actions in response to the financial crisis. The result is an avalanche of uncoordinated regulations from multiple federal agencies that will impact the cost and availability of housing credit.

The Dodd-Frank Act contained a number of provisions that initiated this regulatory overload. For instance, Dodd-Frank created the Consumer Financial Protection Bureau (CFPB), which has broad authority over consumer mortgages and has proposed and/or finalized rules on determining a consumer’s ability to repay, establishing requirements for servicing mortgages, and revamping mortgage application documentation. Additionally, six other regulators proposed an onerous rule to implement the credit risk retention provisions of Dodd-Frank.

Also in the mix are the new Basel III rules from the federal banking regulators, which have set increased capital requirements for banks along with other provisions.

The cumulative impact of these rules has created overwhelming complexity and heightened compliance risks, which will ultimately increase costs to borrowers or prevent creditworthy and responsible borrowers from accessing mortgage credit.

<u>Sec. 401. Basel III Impact Study</u>

The Basel III regulatory capital final rule, issued by the Federal Reserve Board (Fed) on July 2, 2013 and confirmed by the Federal Deposit Insurance Corporation (FDIC) and the Office of the Comptroller of the Currency (OCC) on July 9, increases the quantity and quality of capital for all federally insured banking institutions and imposes additional thresholds for the largest banking organizations. Basel III will be phased in, beginning January 2014 for the largest banks; community banks have until January 2015 to comply.

This bill would direct the Fed, FDIC and OCC to conduct an empirical study of the Basel III regulatory capital rules. The study would provide important insight into the potential impact on the financial services sector, the cumulative impact on US economic growth, and the impact on the availability and cost of credit, and will help the regulators to implement effective capital requirements without obstructing much needed credit.

This bill would require that a final report be made available to the public for a notice and comment period, that Congress hold a hearing on this report, and that the federal banking agencies review the final rule based on the report and public comments. The bill would delay the final Basel III rules for at least two years for some financial institutions until the study is completed.

NAHB supports conducting a study of Basel III bank capital rules and delaying implementation of this rule until the study has been completed. The increased reserve requirements will significantly increase the capital that banks need to hold and may alter their business plans. NAHB is particularly concerned about adverse effects of Basel III on community banks, which are key sources of credit for both home buyers and home builders.

<u>Sec. 403. Definition of Points and Fees</u>

The PATH Act would make changes to certain provisions of the Ability-to-Repay (ATR) standard that was authorized by Dodd-Frank and promulgated by the CFPB.

The Ability-to-Repay standard sets minimum standards for mortgages by requiring lenders to establish that consumers have a reasonable ability to repay at the time the mortgage is originated, and provides that certain high-quality, low-cost loans (defined as Qualified Mortgages or QMs) are presumed to meet this standard. The CFPB issued a final ATR rule that will become effective on January 10, 2014. Since issuing the final rules in January, the CFPB has issued amendments to the ATR rule to clarify or change provisions of the rule in an effort to ensure a smooth transition.

Among other provisions, the final ATR rule limits the points and fees that can be charged to a borrower to 3 percent of the loan amount in order to qualify as a QM loan under the "ability to repay" regulations. Many industry stakeholders believe the 3 percent cap to be overly restrictive and ultimately could reduce the availability or increase the costs of credit to creditworthy borrowers. There are some exceptions to the 3 percent cap, including small loan amounts, but the rule differentiates point and fee calculations for affiliated and unaffiliated companies, including charges from affiliates but not from affiliated companies. This differential also exists for retail lender and brokered loans. These differentiations create competitive disadvantages for different business models for no apparent reason and would restrict consumers' choice of mortgage settlement services.

NAHB supports balancing mortgage credit availability and consumer protections. NAHB believes that loans should be prudently 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. Great care must be taken to avoid further adverse changes in liquidity and affordability.

Therefore, NAHB supports amending the Truth in Lending Act to exempt certain affiliated business arrangements from the calculation of points and fees, as directed in this section.

<u>Sec. 406. Effective Date of Certain Mortgage Reform Regulations</u>

This section would extend the timeline for certain new mortgage regulations that were authorized by Dodd-Frank for an additional year.

NAHB supports this extension as it would provide much needed time for the lending institutions to adapt to the new regulations and would ensure that there is no disruption in the availability of mortgage credit.

<u>Sec. 407. Repeal of Credit Risk Retention Regulations</u>

This section would fully repeal Section 941: Regulation of credit risk retention, of Dodd-Frank, and would prohibit federal regulators from issuing any regulation that would require risk retention, the creation or maintenance of a premium capture cash reserve account, or any similar mechanism unless directed by Congress.
Sec. 941 of the DFA regulates credit risk retention by requiring loan originators and securitizers to hold at least five percent of the credit risk between them, with noted exemptions. Requiring lenders and securitizers to have "skin in the game" was intended to provide an incentive to ensure that loans are sound and borrowers are creditworthy.

In March 2011, six federal agencies (Office of the Comptroller of the Currency, Federal Reserve Board, Federal Deposit Insurance Corporation, Federal Housing Finance Agency, Securities and Exchange Commission and Department of Housing and Urban Development) released a proposed Credit Risk Retention rule to implement this DFA provision.

The proposed rule has far-ranging implications across the housing and development sectors. In particular, the rule includes exemptions to the risk retention requirements for Qualified Residential Mortgages (QRM) and Qualified Commercial Real Estate (QCRE) loans. The regulators very narrowly defined these exemptions and proposed very conservative underwriting standards and requirements (including a 20 percent downpayment requirement) that will limit the number of loans eligible for these exemptions. In addition, the premium capture cash reserve account (PCCRA) provision has the potential to distort the securitization market and create a disincentive for private investors.

As stated earlier, 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. The housing system and the economy have been affected deeply by the consequences of inappropriate underwriting standards and risky loan features. However, if the credit risk retention rule is finalized as proposed, it could be detrimental to the flow of mortgage credit. Therefore, NAHB supports the repeal of Section 941 of Dodd-Frank as an alternative to the proposed rule.

Sec. 409. Mortgage Loans Held in Portfolio

This provision would exempt mortgage loans held in the portfolio of the creditor that made the loan from the "Minimum standards for residential mortgage loans" ATR rules, mandatory escrow rules, and certain disclosure rules.

NAHB supports the exemption for depository institutions that hold loans in their portfolios from ATR rules and other Dodd-Frank requirements. The costs for community banks to comply with these rules are significant and will potentially limit an important source of responsible mortgage credit for consumers.

Sec. 411. Amendments to the Truth in Lending Act

This bill would amend the Truth in Lending Act, by establishing online and telephone housing counseling and allowing 40 year mortgages to be included in the definition of a QM. This section would also prohibit CFPB from establishing the 3-day rule for closing documents, eliminate the prohibition of prepayment penalties, eliminate single premium credit insurance, eliminate a prohibition of adding arbitration clauses to a mortgage contract, and exempt mandatory reporting requirements for appraisal violations from monetary penalties.

NAHB supports efforts to ensure the availability of sound mortgage products. There should be continued availability of financing for long-term (at least 30-year) fixed-rate mortgages, as well as mortgage products with well understood risk characteristics such as certain standard adjustable-rate mortgages and multifamily products. NAHB believes that mortgage maturities should also be available for longer than 30 years.

Sec. 412. Financial Institutions Examination Fairness and Reform

NAHB is pleased that Section 412 of the PATH Act discussion draft incorporates H.R. 1553, *The Financial Institutions Examination Fairness and Reform Act* to tackle the issue of overly restrictive bank examiner regulation. Introduced by Financial Institutions Subcommittee Chairman Shelley Moore Capito (R-WV) and Representative Carolyn Maloney (D-NY), the language in H.R. 1553 is intended to improve the examination of depository institutions and is strongly supported by NAHB.

NAHB believes that the provisions included in Section 412 of the PATH Act discussion draft would greatly benefit the housing industry and help alleviate the credit crisis that our members have been experiencing since 2008. As NAHB has communicated to this committee on numerous occasions, the home building industry continues to experience a significant lack of availability of land acquisition, land development and home construction (AD&C) loans and builders with outstanding loans often face challenges when seeking to modify their AD&C loans in order to have more time to complete projects and pay off loans. Lenders themselves often cite regulatory requirements or examiner pressure on banks to shrink their AD&C loan portfolios as reasons for their actions. While federal bank regulators maintain that they are not encouraging institutions to stop making loans or to indiscriminately liquidate outstanding loans, reports from NAHB members and lending institutions in a number of different geographies suggest the opposite. We hear that bank examiners in the field have adopted an aggressive stance against AD&C loans.

As a result of this regulatory pressure, the home building industry is having extreme difficulty in obtaining credit for viable projects. Builders with outstanding construction and development loans are experiencing intense pressure as the result of requirements for significant additional equity, denials on loan extensions, and demands for immediate repayment. In short, the credit window is very tight for builders, particularly small-to mid-sized builders, all over the country. NAHB has presented banking regulators with specific instances of credit restrictions, provided data showing no difference in credit access across market conditions; and requested specific changes to current regulatory guidance. To date, these efforts have not produced any tangible results. With the availability for housing production loans so limited, it is clear that congressional action is needed to help expand the flow of credit to home builders. Without such action, there can be no housing recovery, which has major implications for our nation's ability to recover from the current economic downturn.

Section 412 addresses concerns NAHB's members have expressed since the housing downturn with regard to how bank examiners have interpreted guidance from federal banking regulators with respect to performing loans, modified or restructured loans, appraisals where no new funds are extended, and classification of commercial loans where there has been deterioration in collateral value. NAHB specifically supports the examination standards in Section 412 that would require:

- A commercial loan cannot be placed in non-accrual status solely because the collateral has deteriorated in value.
- A modified or restructured commercial loan shall be removed from non-accrual status if the borrower demonstrates the ability to perform on such loan over a maximum period of six months. For loans that are on a quarterly, semiannual or longer repayment schedule such period shall be a maximum of three consecutive repayment periods.
- A new appraisal is not required on a performing commercial loan unless an advance of new funds is involved.
- In classifying a commercial loan in which there has been deterioration in collateral value, the amount to be classified shall be the portion of the deficiency relating to the decline in collateral value and repayment capacity of the borrower.

Moving forward, NAHB would like to work with the committee to include a definition of "commercial lending" in Section 412 that specifies the entire spectrum of such lending activity to ensure that construction lending is not inadvertently excluded from the provisions of the overall section. Furthermore, NAHB would encourage the committee to consider adding language to eliminate use of the 100 percent of bank capital measurement as a hard cap that banks say federal banking examiners use to prohibit them from making loans to home builders. This provision, included in H.R. 1255, *the Home Construction Lending Regulatory Improvement Act*, would require bank regulators to follow their existing rules and not obstruct financial institutions' lending to our nation's small builders. Bank regulators would be directed to cease implementing a 100 percent of capital bank lending threshold for AD&C loans as a "hard" limit, rather than utilizing the 100 percent of capital guideline as it was intended. NAHB strongly believes that these suggested changes would both clarify and strengthen Section 412 for the home building industry.

Conclusion

Thank you for the opportunity to participate in today's important and timely hearing. NAHB looks forward to working with the Committee to create a sustainable housing finance system that will provide a reliable flow of housing credit under all economic and financial market conditions.