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The Voice For Real Estate®

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TESTIMONY OF

VINCE MALTA

NATIONAL ASSOCIATION OF REALTORS®
2010 VICE PRESIDENT AND LIAISON TO GOVERNMENT AFFAIRS

BEFORE THE

UNITED STATES HOUSE OF REPRESENTATIVES COMMITTEE ON FINANCIAL SERVICES

ENTITLED

"HOUSING FINANCE AND THE PATH TO REFORM: PART I – GOVERNMENT AND STAKEHOLDER PERSPECTIVES"

MARCH 23, 2010

INTRODUCTION

Chairman Frank, Ranking Member Bachus, and members of the committee, thank you for inviting me to testify today and to offer the REALTOR® perspective on housing finance.

I am Vince Malta the 2010 Vice President and Liaison to Government Affairs for the NATIONAL ASSOCIATION OF REALTORS® (NAR). I am a third-generation REALTOR® and the CEO and founder of Malta & Co., Inc. I have been in the real estate business for over 25 years and served the industry in countless roles. Most recently, I chaired the National Association of REALTORS® Presidential Advisory Group (PAG) on Government-Sponsored Enterprises (GSEs).

I am here to testify on behalf of more than 1.2 million REALTORS® who are involved in residential and commercial real estate as brokers, sales people, property managers, appraisers, counselors, and others engaged in all aspects of the real estate industry. Members belong to one or more of some 1,400 local associations/boards and 54 state and territory associations of REALTORS®.

We thank the House Financial Services Committee for holding this very important hearing on an issue that is paramount to the future viability of the U.S. housing market and our overall economy.

REALTORS® PERSPECTIVE

REALTORS® recognize that our current housing finance structure, with 1) loans backed by the Federal Housing Administration (FHA) comprising up to 30% of the market, 2) the Government-Sponsored Enterprises (GSEs) in conservatorship and controlling nearly 70% of the market, and 3) little-to-no private capital in the marketplace, is both unwanted and unsustainable.

Also, REALTORS® recognize the fragility of the housing market and the overall economy, where any misstep in the implementation of a new housing finance system will likely cause the derailment of our current tenuous recovery, leaving us either back where we started or in a worse predicament. Therefore, until the housing market and overall economy stabilize, and economic and industry experts have an opportunity to fully determine and understand the impact of any proposed new housing finance model, REALTORS® respectfully recommend that we—the industry and government—move forward deliberately, but cautiously, in designing a new housing finance model.

In the balance hang many potential homebuyers who currently have the desire and ability to purchase a home. Any artificial disruption to the housing recovery would injure these aspiring new homeowners (specifically, those taking advantage of the soon to expire home purchase tax credit), as well as existing homeowners, as home values / prices, which have begun to stabilize in most markets, start falling again.

RESTRUCTURING THE SECONDARY MORTGAGE MARKET

As our members began exploring the question of "how to improve the U.S. housing finance sector", there were a couple of significant issues for which they sought a solution. First, and foremost, REALTORS® wanted to ensure that in all markets there is always mortgage capital available for the creditworthy housing consumer. Second, and as important, REALTORS® wanted to ensure that taxpayer dollars were optimally protected. These were the driving forces behind the initial nine principles (see Appendix A) that NAR drafted in late 2008, and they are the drivers behind the recommendation that we put forward today.

Presidential Advisory Group Background

In late 2008, the National Association of REALTORS® formed a Presidential Advisory Group (PAG) to specifically focus on the restructuring of Fannie Mae and Freddie Mac when they come out of conservatorship. The PAG's immediate task was to suggest to restructure Fannie Mae and Freddie Mac (Government-Sponsored Enterprises) in a manner that supports the Nation's historical housing policy of ensuring the continual flow of capital into the housing and mortgage markets in all economic conditions, and that removes the current private profit and public loss structure.

Initially, the PAG, which is comprised of NAR member volunteers, developed nine principles that they believe need to be met in order to ensure a robust financing environment for both residential and multi-family housing. NAR shared these principles with Congress and industry partners on several occasions; however, that was just the beginning.

The PAG then initiated a request for white papers from academics and other secondary mortgage market experts to provide their ideas for a restructure of the GSEs based on NAR's initial secondary mortgage market principles. NAR received a number of papers, and in mid November 2009, the PAG convened a meeting of selected academics, whose ideas ran the gamut from Federalization to Privatization.[1]

Upon completion of the PAG's review of the white papers, the members agreed that a hybrid of a few of the proposals best addressed their principles, and their desire for a safe and sound secondary mortgage market.

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[1] Among the outside experts NAR consulted were Mercy Jimenez (Principal, Covered Bond Investor), Alex Pollack (Resident Fellow, American Enterprise Institute);Tom Stanton (Fellow of the Center for the Study of American Government, Johns Hopkins University); Susan Wachter (Professor of Real Estate, Finance and City and Regional Planning, The Wharton School, University of Pennsylvania); and Susan Woodward (Founder and Chairman, Sand Hill Econometrics).

KEY ELEMENTS OF NAR's RECOMMENDATION

NAR believes that any organization with a private profit and public loss structure, as the GSEs were structured before conservatorship, is flawed and problematic. In order to ensure that the conflict between the new entities' mission and shareholder needs is eliminated, and given the need for some level of government backing to ensure a steady flow of mortgage funding, NAR proposes a structure that is not driven by the shareholders' need to maximize profits.

NAR believes a "government-chartered" structure is the best model for the new entities because this structure type establishes a separate legal identity from the federal government, while serving a public purpose (e.g. the Export-Import Bank of the United States). Unlike a federal agency, government-chartered organizations are established to be politically independent and often are self-sustaining—not requiring appropriations from Congress. The ability of the entities to focus on their mission (provide liquidity to the housing market), without the need to chase risky opportunities in order to maximize profit, meets the criteria of our members.

Moreover, a government-chartered authority should remove any ambiguity regarding the government's backing of this secondary market entity. REALTORS® believe that government backing of a new entity is required in order to instill confidence in potential investors of the entity's mortgage-backed securities (MBS). Without the confidence of these investors, the ability of the entity to raise capital for the purpose of providing liquidity to the secondary mortgage market will be limited.

However, REALTORS® also believe that the entity should not be operated as if the government / taxpayers are in the first lien position. The entity should be self-sufficient (need no appropriations), price risk effectively to cover potential losses, and utilize any profits to establish capital reserves to alleviate losses that occur in economic down turns.

Lastly, our members believe that the conversion of the existing government-sponsored enterprises (Fannie Mae and Freddie Mac) into government-chartered authorities will pose the least amount of market disruption, and ensure a continual flow of capital to the secondary market during the transition period. Because of their existing capabilities and infrastructure, the current GSEs are best positioned to become government-chartered authorities. With this in mind, our members also suggest that the new authorities import the best components from the current GSEs (e.g. their ability to create MBS, their automated underwriting systems, etc.).

<u>Why not Full Privatization or Nationalization?</u>

Privatization

NAR considered a number of different models for the future structure of the GSEs. The first models that our members considered were the obvious, either fully private or fully federal. Our members thought that neither would effectively solve for the two issues that they deemed necessary to address the challenge of restructuring the secondary mortgage market entities.

REALTORS® believe that full privatization is not an effective option for the secondary market because a private firms' business strategy will inevitably focus on optimizing its revenue / profit generation. This model would foster mortgage products that are more aligned with the business' goals (e.g. based upon significant financial risk-taking) than in the best interest of the nation's housing policy or the consumer. This situation would lead to the rescinding of long-term, fixed rate mortgage products (e.g. 30-year fixed-rate mortgage products), and an increase in the costs of these products to consumers, or both.

According to research presented to NAR by economist Susan Woodward, there is no evidence that a long-term fixed-rate residential mortgage loan would ever arise spontaneously without government urging. Ms. Woodward points out that a few other developed countries have encouraged the use of amortizing long-term loans, but in all instances (save for Denmark), the loans have adjustable rates and recast every 5 years. She goes onto indicate that the United States is unique in supporting a residential mortgage that is long-term, amortizing, fixed-rate and pre-payable, and that Americans have come to view this product as one of their civil rights. Lastly, she notes that in early 2000, when Former Federal Reserve Chairman, Alan Greenspan, hinted at its abandonment, the public outcry was such that he eagerly abandoned that position.

Second, the issue of the size of the US residential mortgage market arises. Currently, the US residential mortgage market stands at $12 trillion, with the GSEs owning or guaranteeing $5 trillion of mortgage debt outstanding and providing capital that supports roughly 70% of new mortgage originations. REALTORS® believe that it is extremely unlikely that enough pure private capital – without government backing - could be attracted to replace existing mortgage funding, or assume the GSEs market share, and make mortgage lending available in all types of markets.

Finally, our members fear that in times of economic upheaval, a fully private secondary mortgage market will cease to exist as has, to a great extent, occurred in the jumbo mortgage, the commercial mortgage, and the manufactured housing mortgage markets. When the economy turns down, private capital rightfully flees the marketplace. Should that happen in the residential mortgage market, the results for the entire economy – because of the plethora of peripheral industries that support and benefit from the residential housing market – would be catastrophic.

Nationalization

In contrast to privatization, full nationalization places the government / taxpayer in the first lien position should the housing market turn down and these institutions run into financial trouble. A top priority of our members is to remove, as much as possible, any ability to have the taxpayer fully on the hook to protect these entities. Converting the GSEs to federal agencies, or merging them with the FHA and Ginnie Mae, conflicts with this goal of our members.

Moreover, nationalization would yield a number of undesirable consequences. First, establishing one public secondary mortgage market entity – Ginnie Mae – would remove competition in the secondary mortgage market, and remove any incentive for innovation. Though our members favor more vigorous regulation of the products the new entities will purchase, they also recognize that innovation is required along the mortgage origination supply chain in order to foster a more efficient and less costly product for consumers.

In addition, a single organization that dominates the secondary mortgage market (e.g. operating in the conventional-conforming space and the FHA space) may lose its ability to adequately focus on the past missions of the prior organizations. For example, an organization that combines FHA and Ginnie Mae with the GSEs could lose focus on either the low- and moderate-income housing mission or ensuring that the middle market has access to affordable mortgage capital. Though today, FHA and the GSEs are serving similar clientele, our members assume that as the economy recovers, these organizations will return to their traditional consumer base.

<u>Protecting Excess Revenue</u>

REALTORS® believe that it is prudent to have the new entities invest all excess capital earned in strong markets into a capital reserve fund so that they can pursue countercyclical activities in weaker markets, as well as store capital to prevent the need for taxpayer funds during economic downturns. Again, a primary goal of our members is to ensure that the government and taxpayers are not immediately on the hook even if a serious downturn occurs.

Also, in the current economic environment, as banks and other financial institutions are being encouraged to hold more capital against well performing assets, the new entities should set the industry standard for safe and sound operations.

<u>Utilization of Retained Portfolio</u>

NAR believes that the entities should maintain a portfolio for the purpose of funding their daily operations, to use in a countercyclical fashion when the market turns down and private capital inevitably leaves the market place, and to test innovative products and house mortgages on products that are not easily securitized (e.g. multi-family housing loans and rural mortgages). The use of the portfolio will ensure that there is a continual flow of capital into the secondary mortgage market during downturns thus preventing a collapse of the housing market, as well as provide much needed capital to those portions of the housing market that don't traditionally have access to large amounts of private capital.

Our members do not recommend a specific size of the portfolio; however, they do believe that the portfolio should only be large enough to support the authorities' business needs, the products that lack private market capital, and when necessary because of insufficient private investment, and only to the extent needed, ensure a stable supply of capital consistent with market conditions. REALTORS® insist that the portfolio size should not be driven by for-profit motives.

Covered Bonds as an Additional Liquidity Tool

REALTORS® believe that all options should be utilized to encourage liquidity in the housing market. One tool that has captured the attention of NAR's members is covered bonds. Though an underutilized tool in our current secondary mortgage market arsenal, covered bonds are a product that should be further explored because of the added security these financial vehicles offer to potential investors. REALTORS® do not believe that this tool can be dominant in our secondary market, but its use should be expanded.

As the GSEs are restructured, NAR members feel that whatever model is selected should allow the organizations to pilot the use of covered bonds (e.g. to help improve liquidity for multifamily housing) in order to foster a better understanding of the tool, and then encourage its use in the nation's residential secondary mortgage market.

NAR'S RECOMMENDATION

In order to ensure that the flow of capital continues to enter the mortgage market regardless of the state of the housing or mortgage markets or overall economy, Fannie Mae and Freddie Mac should be converted into government-chartered, non-shareholder owned authorities that are subject to tighter regulations on product, profitability, and minimal retained portfolio practices in a way that ensures the protection of taxpayer monies.

The New Entities Impact on Private Capital Participation in the Secondary Market

Our members expect that the new government-chartered non-shareholder owned authorities will ensure that there is liquidity in the market place for those standard mortgage products (e.g. long-term fixed rate mortgages and traditional adjustable rate mortgages with reasonable annual and lifetime caps) that are the foundation of our housing finance market. Our members realize that initially the authorities may curtail some private participation in this portion of the market; however, over time, the private market participants, as in the past, will offer innovations driven by consumer need and demand. Also, with the new entities offering standard products, private capital will be free to return, compete, and exploit opportunities in addition to the products offered by the new authorities.

REALTORS® believe that this is likely to occur because under the recent GSE model, even as Fannie Mae and Freddie Mac enjoyed very low costs of funds compared to their competitors / customers, beginning in the early 2000s the competitors' share of the secondary market grew at significant rate until the collapse of the marketplace. It is only now, with a collapsed marketplace and private capital sitting on the sidelines, that the GSEs market share has increased significantly. Our members fully anticipate that with the full recovery of the market, and the conversion of the GSEs into these new entities, and a return of private capital into the secondary market, we will see the appropriate balance of government, government-hybrid, and private capital activity in the secondary mortgage market.

CONCLUSION

The National Association of REALTORS® supports a secondary mortgage market model that includes some level of government participation, but that protects the taxpayer while ensuring that all creditworthy consumers have reasonable access to mortgage capital so that they too may attain the American Dream – homeownership. Our members recognize that this is but the first of many conversations regarding how we mend, and improve, a housing finance system that had served us well for many years. We believe that the NAR recommendations, along with some key elements that we mentioned today, will help Congress and our industry partners design a secondary mortgage model that will be in all of our nation's best interest today, and in the future.

I thank you for this opportunity to present our thoughts on reforming our housing finance system, and as always, the National Association of REALTORS® is at the call of Congress, and our industry partners, to help continue the housing and national economic recovery.

Appendix A

National Association of REALTORS® Recommendations For Reforming the GSEs

National Association of REALTORS® Government Affairs Division
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The Issue:

How to restructure Fannie Mae and Freddie Mac (Government-Sponsored Enterprises) in a manner that supports the Nation's historical housing policy of ensuring the continual flow of capital into the housing and mortgage markets in all economic conditions, and removes the current private profit and public loss structure.

NAR's Recommendation:

Convert Fannie Mae and Freddie Mac into **government-chartered, non-shareholder owned authorities** that are subject to tighter regulations on product, revenue generation and usage, and retained portfolio practices in a way that ensures they can accomplish their mission and protect the taxpayer.

NAR's Rationale:

Government-chartered entities are organizations that have a separate legal identity from the federal government but serve a public purpose (e.g. the Tennessee Valley Administration and the Export-Import Bank). Unlike a federal agency, the organizations enjoy considerable political independence and often are self-sustaining – not requiring appropriations from Congress. The conversion of the government-sponsored enterprises into government-chartered authorities will ensure that the flow of capital continues to enter the mortgage market regardless of the state of the housing or mortgage markets or overall economy and minimize the incentive for the authorities to take undue risk.

NAR believes that any organization with a private profit and public loss structure, as the GSEs are presently structured, is inherently flawed and problematic. In order to ensure that the conflict between the new entities public purpose (mission) and shareholder demands is eliminated, NAR proposes that the organizations not offer equity to the public.

Appendix A

Key Elements of a proposed restructure that NAR believes are required to ensure the continual flow of capital into the housing and mortgage markets:

MISSION

The authorities' mission is to ensure a strong, robust financing environment for homeownership and rental housing, including access to mortgage financing for underserved segments of the population that have the financial resources to sustain homeownership.

BUSINESS PRACTICES

The government must clearly, and explicitly, guarantee the business of the restructured entities. Taxpayer risk would be mitigated through the use of mortgage insurance on loan products with a loan to value ratio of 80 percent or higher and MBS guarantee fees paid to the government. Only if these pools prove to be insufficient in some future economic crisis would the federal taxpayer be called upon to make good on the federal guarantee of the MBSs.

Sound and sensible underwriting standards must be established for loans purchased and securitized in MBSs, loans purchased for portfolio, and MBS purchases.

The authorities will retain and reinvest all excess revenue to accumulate capital in strong markets, to pursue a countercyclical policy in weaker markets, and to support the secondary market, provide for innovation, remain mission focused, and maintain their capacity.

The primary purpose of the authorities' portfolios will be to support their operations in both the single family and the multi-family housing markets. The portfolios should only be large enough to support their business needs and when necessary because of insufficient private investment in the mortgage market, and only to the extent needed, ensure a stable supply of capital consistent with market conditions.

In order to increase the use of covered bonds, particularly in the commercial real estate arena, the organizations should pilot their use in multifamily housing lending and explore their use as an additional way to provide more mortgage capital for residential housing. Also, initially a government guarantee, such as by the FDIC, should be considered to enhance the covered bond option to entice private market participation.

The authorities should price loan products based on risk. Housing affordability goals will assure that the entities serve a full range of borrowers directly by the GSEs or indirectly by programs assisted by the GSEs.

Appendix A

The organization must set standards for their MBSs that establish transparency and verifiability for loans within the MBSs that are purchased or securitized by the government-chartered authorities.

The entities should only purchase and guarantee transparent and verifiable mortgage loans, and should only purchase derivatives as a limited option in order to manage risk, not to generate profit.

At least two entities are required to provide for competition in the secondary market and avoid the risk a single entity would lose incentive to innovate and to be efficient.

GOVERNANCE

Political independence of the entities is mandatory for successful operation (e.g. the CEOs will have fixed terms so they cannot be fired without cause, and the authorities will be self funded – no ongoing appropriations).

The governance structure should provide for a Chief Executive Officer to oversee daily operations, a Board of Directors with practical expertise to ensure effective and efficient operation, and an advisory board comprised of industry participants and consumer representatives to provide the organization, and its management, with real-time, front-line information regarding the authorities' effectiveness and advice on their operation.

The entities will be permanent (not expire).

OVERSIGHT

There must be strong oversight of the entities (for example, by the Federal Housing Finance Agency – FHFA or a successor agency), that includes the providing of timely reports to allow for continual evaluation of their performance.

ASSOCIATED FINANCIAL REGULATORY REFORM

Reform of the credit rating agency sector is required, to address the inherent conflict of interest in the current system.

Appendix B

GOVERNMENT SPONSORED ENTERPRISES
NAR PRESIDENTIAL ADVISORY GROUP

NAR PRINCIPLES:
ENSURING A STRONG, ROBUST FINANCING ENVIRONMENT FOR HOMEOWNERSHIP AND MULTIFAMILY HOUSING

NOVEMBER 2009

In light of disruptions in the credit markets and the conservatorship of Fannie Mae and Freddie Mac, NAR has developed principles for the consideration of the 111th Congress and the Obama Administration. NAR believes that these principles require a continuing role for the federal government in the mortgage market. The new secondary mortgage market model must:

1. Ensure an active secondary mortgage market by facilitating the flow of capital into the mortgage market for all types of housing, in all market conditions.

2. Seek to ensure affordable mortgage rates for qualified borrowers.

3. Establish: (a) reasonable housing affordability goals so all qualified borrowers,[2] including low- and moderate-income households, have an opportunity to realize the dream of homeownership; and (b) reasonable multifamily rental housing affordability goals to increase the availability of financing for rental housing. Housing affordability goals should not provide incentives for the institution that are inconsistent with sustainable homeownership or rental housing.

4. Require the institution to pass on the advantage of its lower borrowing costs (and other costs of raising capital) by making mortgages with lower rates and fees available to qualified borrowers.

5. Ensure mortgage availability throughout the nation.

6. Require sound underwriting standards, consistent with NAR's Responsible Lending Principles adopted in May 2005 (see attached).

7. Require the highest standards of transparency and soundness with respect to disclosure and structuring of mortgage related securities.

8. Ensure there is sufficient capital to support mortgage lending for all types of housing, in all market conditions.

9. Provide for rigorous oversight.

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[2] NAR's Responsible Lending Policy supports requiring all mortgage originators to verify the borrower's ability to repay the loan based on all its terms, including taxes and insurance, without having to refinance or sell the home (with limited exceptions for borrowers with significant assets).

Appendix C

NATIONAL ASSOCIATION OF REALTORS®
RESPONSIBLE LENDING POLICY
ADOPTED MAY 2005

Why Do REALTORS® Seek to Prevent Abusive Lending?

REALTORS® have a strong stake in preventing abusive lending because:

- Abusive lending erodes confidence in the Nation's housing system.
- In a credit-driven economy, the legislative and regulatory response to lending abuses can go too far and inadvertently limit the availability of reasonable credit for prime as well as subprime borrowers.
- Citizens of communities, including REALTORS®, are harmed whenever abusive lending strips equity from homeowners, especially when the irresponsible lenders concentrate their activities on certain neighborhoods and create a downward cycle of economic deterioration.

Responsible Lending Principles

NAR supports the general principle that all mortgage originators should act in "good faith and with fair dealings" in a transaction and treat all parties honestly. NAR's Code of Ethics already imposes a similar requirement on REALTORS®, who are required to treat everyone in the transaction honestly. NAR encourages policy makers to use such a standard of care as a guiding principle when drafting anti-predatory lending legislation and regulations rather than using the phrase to create a new federal duty that would be too general and, therefore, too difficult to enforce.

1. Affordability. NAR supports strong underwriting standards that require all mortgage originators to verify the borrower's ability to repay the loan based on all its terms, including taxes and insurance, without having to refinance or sell the home.[3] Lenders should consider all relevant facts, including the borrower's income, credit history, future income potential, and other life circumstances. Lenders should not makes loans to borrowers that make loss of the home through sale or foreclosure likely if the borrower is unable to refinance the mortgage or sell.

- Underwriting Subprime Loans with "Teaser Rates." Some loans are structured with a significant jump in monthly payments often resulting in "payment shock" for the borrower. While these mortgages may be a reasonable choice for borrowers who can afford them, a majority of subprime borrowers do not understand the unique terms and conditions of these risky mortgage products that can result in a significant "payment shock." Therefore, lenders (including mortgage brokers) should exercise more caution when underwriting such loans to subprime borrowers to make sure the borrower is able to afford the mortgage. Examples of these risky mortgage products include loans with a short-term interest "teaser" rate for the first

[3] The limited exceptions to this general principle would include prime borrowers with sufficient verifiable assets to handle a balloon mortgage or a significant jump in mortgage payment.

two or three years (known as 2/28s and 3/27s), loans with an initial interest-only period, and mortgages that negatively amortize.[4]

NAR will carefully monitor the debate on underwriting standards for subprime loans and will support policies consistent with the goal of assuring that borrowers who have demonstrated the financial capacity to meet their mortgage obligations, taking into account all relevant circumstances, continue to have access to mortgage loans made by responsible lenders.

- Reasonable Debt-to-Income Ratio. NAR supports requiring lenders to make subprime loans that have a reasonable debt-to-income ratio. Borrowers should have enough residual income after making their monthly mortgage payment, including taxes and insurance, to meet their needs for food, utilities, clothing, transportation, work-related expenses, and other essentials. Requiring underwriting at a fully amortizing, fully indexed rate is meaningless if the lender uses such high debt-to-income ratios that the family doesn't have enough income remaining to pay for other necessities.

- Escrow/Reserve for Payment of Taxes and Insurance. Lenders that make subprime mortgage loans should generally require that the monthly payment include an amount to be held by the mortgage servicer in an escrow/reserve/impound account for the payment of the borrower's periodic payments, such as taxes, insurance, and homeowner association/condominium fees. Similar to the exception for prime loans in some jurisdictions, borrowers that make at least a 20 percent downpayment should have the option to budget for these payments independently.

2. Limit Stated Income/Stated Assets Underwriting. Because mortgages underwritten based on "stated income" and/or "stated assets" (also known as "no income verification" or "no doc" loans) typically have higher rates, lenders making subprime loans should, as a general rule, underwrite loans based on verified income and assets.

3. Flexibility for Life Circumstances. NAR believes that a standard for determining a borrower's ability to repay must be flexible to accommodate borrowers with unique circumstances, such as:

- ✓ Borrowers who have demonstrated the ability to make monthly payments, over a long term, that are higher than underwriting standards would otherwise allow. Lenders should consider, for example, the borrower's history of making rent and student loan payments.
- ✓ Borrowers with high assets but low income who, for cash management or other financial planning reasons, elect a mortgage with a monthly payment that their current income is not sufficient to cover.
- ✓ Borrowers who anticipate a jump in income or assets due to life events such as graduation, completion of professional training, completion of payment obligations for student or car loans, another member of the household entering the work force when young children start school, or an inheritance.

4. Anti-Mortgage Flipping Policy. NAR supports an anti-mortgage-flipping rule requiring mortgage originators making or arranging for a loan that refinances an existing residential mortgage to verify that the new loan provides a significant benefit to the borrower (one test often proposed is

[4] Negative amortization ordinarily results if the mortgage permits a borrower to pay less than the interest on the mortgage for a limited time, in which case the difference is added to the total amount of the loan the borrower must repay.

the loan must provide a "reasonable net tangible benefit" to the borrower). The lender should consider the circumstances of the borrower, as discussed above, all terms of the new loan including taxes and insurance, the fees and other costs of refinance, prepayment penalties, and the new interest rate compared to that of the refinanced loan.

5. Bar Prepayment Penalties. NAR opposes prepayment penalties for all mortgages. Prepayment penalties often work to trap borrowers in loans they cannot afford by making it too expensive to refinance. If complete prohibition of prepayment penalties is not feasible, NAR supports permitting prepayment penalties for the shortest time and the lowest amount possible. For example, a borrower in a 2/28 mortgage should be able to refinance by the end of the initial two-year "teaser" rate period without having to pay a prepayment penalty.

6. Improvements for Assessing Creditworthiness. Borrowers with little or no credit history, as traditionally measured, usually have lower credit scores and must pay more every month for their mortgage than those with higher scores. NAR supports ongoing efforts to take into account consumer payment history not typically considered, such as rent, utility, telephone, and other regular payments and urges HUD, the regulators, the GSEs, and lenders to work to strengthen these efforts. Use of alternative credit approaches will be especially beneficial for low- and moderate-income first-time homebuyers and borrowers with problematic loans that need to refinance their mortgage to avoid foreclosure.

Another public policy issue associated with credit histories is the failure of furnishers to report good payment histories to the consumer reporting agencies. NAR has heard reports that many problematic subprime lenders purposefully withhold information on timely mortgage payments from the credit bureaus in order to prevent their customer from refinancing with another lender. The result is obvious—the borrowers with no positive payment histories for their subprime loan keep treading the waters of high-interest rates and expensive credit products. NAR supports requiring all institutional mortgage lenders, or the mortgage servicers acting on their behalf, to report payment history of all borrowers to at least the three national credit bureaus on a monthly basis.

7. Mortgage Choice for Borrowers. NAR supports requiring mortgage originators to offer borrowers one or more mortgages with interest rates and other fees that appropriately reflect the borrower's credit risk. It remains the responsibility of borrowers to decide which is the best mortgage for their needs and circumstances, but they may only do so if they understand all the facts so they can make an informed decision. The following are suggested principles for consideration of Congress and the regulators:

- For originators who offer nontraditional mortgage products, the originator should:
    - offer all borrowers a choice of several significantly different mortgage options;
    - include at least one traditional loan product as one of the options for the borrower to consider, if the borrower qualifies for such a product offered by the originator; and
    - before application acceptance, disclose information about the maximum potential payment over the life of the loan and the date the initial payment will increase to a fully amortizing, fully indexed payment amount.

- For subprime borrowers, originators that offer FHA-insured mortgages or VA home loan guaranty mortgages should consider whether these types of mortgages should be offered as an appropriate option.

- If the originator does not offer mortgages with rates and fees appropriate for the borrower's credit risk, the originator should inform the borrower a lower interest rate may be available from another originator or that the borrower may wish to seek housing counseling, to allow the borrower an opportunity to shop elsewhere or receive counseling before proceeding. For example, a prime borrower that applies for a loan to a lender that only makes subprime loans should be advised that other options may be available.

- For loans originated by a mortgage broker, the broker should offer mortgage options that are among the lowest-cost products appropriate for the borrower.

8. Enforcement/Remedies. NAR supports enactment of strong remedies and penalties for abusive acts by mortgage originators. Among the options for consideration are:

- Criminal penalties similar to those under RESPA.

- Civil penalties similar to those under RESPA.

- Assignee liability that balances the need to protect innocent borrowers with problematic loans against the risk that increasing the liability of innocent holders of mortgages in the secondary market could reduce the availability of mortgage credit.

- Prohibition of mandatory arbitration clauses that bar victims' access to court.

9. Strengthen Appraiser Independence. NAR believes that the independence of appraisers should be strengthened to ensure that appraisals are based on sound and fair appraisal principles and are accurate. There are reports that appraisers have been pressured to meet targeted values or risk losing business. Appraisal pressure undermines the integrity of the mortgage lending process if the result is a mortgage loan made based on an inaccurate property valuation. NAR recommends the following measures to strengthen the appraisal process:

- Require lenders to inform each borrower of the method used to value the property in connection with the mortgage application, and give the borrower the right to receive a copy of each appraisal at no additional cost.

- Establish enhanced penalties against those who improperly influence the appraisal process. Those with an interest in the outcome of an appraisal should only request the appraiser to (1) consider additional information about the property; (2) provide further detail, substantiation, or explanation for the appraisal; and (3) correct errors.

- Provide federal assistance to states to strengthen regulatory and enforcement activities related to appraisals.

- Support enhanced education and qualifications for appraisers.