June 13, 2012

Edward DeMarco
Acting Director
Federal Housing Finance Agency
400 7th Street, SW
Washington, DC 20024

Re: Civil Rights Perspective on FHFA Strategic Plan: Fiscal Years 2013--2017

Dear Director DeMarco:

The undersigned civil rights, fair housing and consumer advocates are working toward housing and financial markets that strike the right balance of liquidity, stability, transparency, consumer protection, access, and affordability. Central to a healthy housing market is affordability and access for modest income borrowers and communities of color. Moreover, the right combination of housing options overall will provide a path toward economic mobility for families now and generations to come. With this in mind, we write in response to the FHFA's updated plan to incorporate the strategic plan for the conservatorships of Fannie Mae and Freddie Mac released on May 14, 2012, entitled *Federal Housing Finance Agency's (FHFA) Strategic Plan: Fiscal Years 2013--2017.*

The *FHFA strategic plan: Fiscal Years 2013 to 2017* highlights four strategic goals for FHFA, including: 1) Safe and sound housing government-sponsored enterprises (GSEs); 2) Stability, liquidity, and access in housing finance; 3) Preserve and conserve Enterprise assets; and 4) Prepare for the future of U.S. housing finance.

The strategic plan contains a number of important objectives on which we agree, such as increasing the level of transparency and equal access to small lenders. In an effort to better improve the outcomes of the strategic plan, we offer the following additions to strengthen the plan's stated objectives:

- **Monitor access to housing markets for modest income and households of color.** We agree that monitoring access to housing markets for modest income and households of color is critical to ensuring that Fannie Mae, Freddie Mac, and Ginnie Mae actively serve underserved communities. The historic role of subprime and predatory lending in communities of color and among low-income, elderly, and female borrowers has caused disproportionate harm and unequal access to sustainable loans. Therefore, to achieve the goal of serving these consumer segments well, FHFA must monitor the secondary market for consumer safety and market stability in modest income and communities of color. The current foreclosure crisis has made it evident that irresponsible financial institutions have used these markets to introduce toxic mortgage products to the wider market.

  In addition to monitoring access, FHFA must also collect more detailed data to assesses the risk of securities. Publicly accessible and timely data will assist GSEs, regulators, researchers and advocates in monitoring the GSEs progress in facilitating affordable access to mortgage products for modest income households and communities of color. Furthermore, monitoring access and mortgage terms in housing markets for modest income and communities of color will assist the dissolution of a dual mortgage market. Specifically, the following data should be generated by the GSEs and publicly available: Race, gender, national origin, and other relevant characteristics of borrowers; how a loan was serviced, purchased, and securitized; and the terms and conditions of a loan's underwriting information and product features.

- **Equal footing for small institutions in GSEs.**
  Ensuring fair and impartial access to Enterprise products and services for smaller institutions that would otherwise be at a disadvantage is a critical component of the proposed FHFA strategic plan. Local institutions vested in their community are often leaders in mortgage innovations that directly address the community's home buying needs. Without a secondary market outlet, the volume of these loans will always be constrained. Furthermore, because innovation is not always immediately scalable or easily standardized, it runs the risk of being overlooked by large financial institutions or secondary market purchasers. Therefore, a key component to ensuring that small institutions have access to products and services in the future GSE structure is to provide equal footing for local institutions in the GSE governance structure. This will ensure, among other things, that insurance or guarantees are similarly priced no matter the size of the institution, thereby facilitating market competitiveness.

While we agree on the elements outlined above, we are disappointed that the proposed strategic plan lacks detail on how to better achieve access and affordability for underserved yet prepared borrowers. The plan mentions the FHFA affordable housing goals mandated by HERA. While the HERA affordability goals are an acknowledgment of the broader social purpose of the GSEs, these intended goals remain unaddressed due to a lack of implementation and the ineffectiveness in increasing access and affordability. The lack of concrete language on these issues creates concerns that access and affordability goals are low priorities for the FHFA. To support FHFA's thinking on this topic, we offer five recommendations:

- **Avoid overreliance on the Federal Housing Administration (FHA).**
  FHA has an important role in meeting the homeownership needs of low and middle income (LMI) households. However, the housing finance system cannot rely solely on FHA to fulfill the housing needs of creditworthy low and middle income borrowers. The future finance market must be inclusive so that any prepared borrower can access a reasonably-priced loan that is within his/her ability to repay.

  Currently, FHA accounts for a disproportionate percentage of the overall mortgage market. While the number of home-purchase conventional loans has fallen substantially, the number of non-conventional loans has become a bigger portion of the housing market. In 2010, non-conventional loans made up 52%of the homeowner occupied mortgage market, demonstrating the power of the government in maintaining credit liquidity in counter cyclical times.[1] However, the use of FHA has been increasing not only by low and middle income household but by higher income households as well.[2] In LMI communities, the share of FHA loans constitutes an overwhelming number of all loans made. This raises concerns of fair lending due to the higher cost of FHA loans when compared to conventional loans.[3] This heavy reliance on FHA runs counter to the shared goal of reducing the government's footprint in the housing market. To suggest that the private market serve only middle and upper markets without an obligation to also serve creditworthy moderate-income borrowers is irresponsible. Private lenders availing themselves of public resources must serve the entire market.

- **Create a GSE infrastructure that eliminates the dual credit market.**
  The future of the housing finance system must maintain pathways to homeownership for qualified borrowers and a financing mechanism for affordable rental homes. Despite clear demand from qualified consumers, the mortgage market does not reach all segments of borrowers and all geographic areas, and it unnecessarily exposes them to riskier and more expensive products than those for which they qualify. During the recent housing boom and bust, Asian, Black, and Hispanic families were 1.7, 3.0, and 2.2 times more likely (respectively) than White borrowers to receive subprime loans even after accounting for similar credit profiles.[4] This market divide, where factors other than one's credit profile determining the type of credit made available to a borrower, is known as a dual credit market. The strategic plan is silent on the role of the Enterprises in eliminating this phenomenon, which should be an essential and primary goal for the architects of a new housing finance system. Moreover, the federal government can further support this recommendation by developing the mechanisms necessary to prevent the targeting or limiting of mortgage capital by any segment of the housing finance system in a manner that is discriminatory. Anything short of that will be a step backward from our nation's longstanding goal to support and promote a robust and financially secure middle class for all.

  Also, the proposed strategic plan calls for an increase in private market representation in the mortgage market. While increasing private capital in the housing market is critical for long-term sustainability, we also believe that explicit limited government guarantees should be used to increase the level of conventional loans in modest income and communities of color, further increasing the liquidity of fair and sustainable conventional loans in these communities. As part of this initiative, FHFA should develop plans with

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[1] See Avery, Robert B., Neil Bhutta, Kenneth P. Brevoort and Glenn B. Canner, September 22, 2011, "The Mortgage Market in 2010: Highlights from the Data Reported under the Home Mortgage Disclosure Act," Federal Reserve Bulletin, Volume 97.
[2] Van Order, Robert, and Anthony Yezer, May 2011, "The Role of the Federal Housing Administration in Recovery U.S. Housing Market," George Washington University Scholl of Business FHA Assessments Report, 4th edition, May 2012.
[3] Taylor, John, "The FHA Reform Act of 2010: HUD's Proposal Strike Balance between Access and Safety and Soundness," The FHA Reform Act of 2010 : Hearing before the Subcommittee on Housing and Community Opportunity of the Committee on Financial Services, U.S. House of Representatives, One Hundred Eleventh Congress, second session, March 11, 2010.
[4] Debbie Gruenstien Bocain, et al., "Lost Ground, 2011: Disparities in Mortgage Lending and Foreclosures" (Washington, DC: Center for Responsible Lending and Center for Community Capital, University of North Carolina Chapel Hill, 2011), http://www.responsiblelending.org/mortgage-lending/research-analysis/Lost-Ground-2011.pdf

concrete benchmarks for promoting access and affordability in GSE-backed conventional and unconventional loans.

- **Creditworthiness should be based on a comprehensive analysis of a borrower's income, assets, and debts.**
  The FHFA's strategic plan calls for the tightening of underwriting standards. While we believe this is an historic opportunity to better assess the ability to pay for homes, tightening or restricting credit to mortgage-ready borrowers will not promote a healthier housing market. Since 2009 the FHFA has contributed to the trend of cherry-picking borrowers by increasing credit score restrictions and increasing LTV requirements while leaving those with modest wealth reserves on the sidelines. A recent study by the Center for Community Credit compared low-income homebuyers who received flexible but responsible conventional prime mortgages with similarly situated borrowers who received subprime mortgages.[1] Researchers found that those with subprime loans had a foreclosure rate three to five times higher than that of borrowers who received flexible yet fair fixed loans. In fact, not only were the borrowers with the responsible loans less likely to foreclose, they also gained an average of $20,000 in home equity as of 2009. For borrowers new to the process, advanced preparation with the help of a certified housing counseling organization has been shown to lower the risk of default. NOTE. Predicting the delinquency or default of a loan would be better served by regulating the features of a mortgage rather than tightening credit scores and LTVs.

  Notwithstanding, in September 2009, Fannie Mae announced that it was increasing its minimum credit score requirement from 580 to 620. While borrowers with a credit score of less than a 500 would no longer qualify for an FHA loan, borrowers with credit scores between 500 and 579 would be required to make a minimum 10% down payment. NOTE This presents clear limitations for communities of color and modest income households. For example, based on a study from the Woodstock Institute, the majority of individuals in the African American community have scores below 620 and over 43% have credit scores below 580. Changes in down payment requirements would unnecessarily lock out a substantial number of African American and other communities of color as well as other modest income borrowers. NOTE

  While the use of credit scores and LTVs allows for reduced underwriting costs on the front end, it presents higher costs in the long run by excluding creditworthy borrowers and forcing them to turn to more expensive credit. For this reason, proxies like credit score or LTVs, as were commonly used in recent years, should not be used to determine creditworthiness going forward. Rather, credit and underwriting decisions should be based on documented and verified information reflected in the borrower's file and a comprehensive analysis of a borrower's income, assets, and debts. In addition to documented information such as paycheck stubs, W-2s, tax returns, and bank statements, third-party documents that provide reasonably reliable evidence of the consumer's income or assets should be used. We strongly believe that counselors from HUD-approved housing counseling agencies are well equipped to evaluate these third-party

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[1] Lei Ding et al., May 2010. "Risky Borrower or Risky Mortgages: Disaggregating Effects Using Propensity Score Models", UNC Center for Community Capital, Chapel Hill, NC, 2010.

documents. In addition, studies have demonstrated that borrowers who participate in housing counseling are less likely to default on their mortgages.

- **Ensure that the GSEs are not downsized at the expense of families who would most benefit.**
  The strategic plan acknowledges that it was not the GSEs' portfolio lending that led to the conservatorship and dependence on public funds—a critical clarification for which we thank you. Yet, the plan supports the Treasury's requirement to shrink their retained portfolio and further business conducted under this model. Traditionally, Fannie Mae and Freddie Mac's portfolio lending has served as a safe place to test new lending models and strategies before launching them into the broader market. Without a sustained portfolio, this critical source of capital will evaporate, with the impact squarely felt by marginally-served consumer segments. Moreover, the proposal misses an opportunity to contract the agencies' footprint by lowering loan limits. In effect, this proposed plan would maintain access for those most likely to be served by the private market while reducing service to those least likely to access credit without the agencies' guarantee. We agree that conservatorship is untenable and in no way a permanent solution. Indeed, current market experience affirms that private investors will not clamor to play the role that GSEs fulfill. FHFA must defend this aspect of the GSE business and request congressional approval to maintain responsible portfolio lending.

- **Substantially improve current foreclosure prevention efforts.**
  We support the idea of building a robust GSE framework that is modernized and protected from the hazards of another crisis. However, the fate of many homes and the housing sector at large still hangs in the balance. Foreclosure prevention must not be a matter of hasty maintenance. The strategic plan overstates the progress GSEs have made in preventing foreclosures since they were put under conservatorship. Standards must be set to ensure that all of a family's options are exhausted before they lose their home. One of the most important yet untapped options continues to be principal reduction. The new HAMP incentives make principal reduction an even more economically feasible option. Therefore we strongly urge you to update your assessment and identify a mechanism for delivering principal reductions that are Net Present Value (NPV)-positive. We must do everything we can to prevent unnecessary foreclosures before forging ahead with the next phases of GSE reform.

With these recommendations, we seek a fairer housing market with true accountability and reasonable access to credit for our communities. To discuss these recommendations further, please contact Janis Bowdler, National Council of La Raza (NCLR), at (202) 776-1748 or jbowdler@nclr.org. We look forward to continuing this dialogue with you and your staff.

Sincerely,