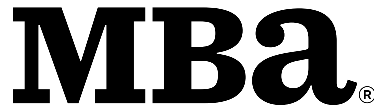

MORTGAGE BANKERS ASSOCIATION

April 14, 2017

The Honorable Mike Crapo
Chairman, Committee on
Banking, Housing, and Urban Affairs
534 Dirksen Senate Office Building
Washington, DC 20510

The Honorable Sherrod Brown
Ranking Member, Committee on
Banking, Housing, and Urban Affairs
534 Dirksen Senate Office Building
Washington, DC 20510

Dear Chairman Crapo and Ranking Member Brown:

Thank you for the opportunity to submit legislative proposals to promote economic growth and enable consumers, market participants, and financial companies to better participate in the economy. As an association representing the entire mortgage finance industry, including a broad cross-section of financial institutions, MBA has consistently supported reasonable requirements that will prevent a reemergence of housing and market disruptions. However, while some of the new regulations enacted in the past several years have made the mortgage market safer, in many other respects these rules have reduced the availability and affordability of mortgage credit for many families.

The current regulatory environment has increased costs and forced many responsible mortgage bankers to limit lending. This most often harms low-to-moderate income borrowers, minorities, and first-time homebuyers. We urge the Committee to do a thorough review of current rules and regulations and make adjustments where necessary in order to balance the need for consumer protection while ensuring access to safe, sustainable mortgage credit. In this regard, we strongly urge that particular attention be given to simplifying rules, providing greater clarity and certainty, and mitigating supervisory burdens. These goals are particularly important for smaller, community lenders that may not be able to sustain excessive compliance and legal infrastructures.

In addition to the discrete suggestions outlined below, we applaud your bipartisan efforts on comprehensive housing finance reform and encourage you to continue work on that important topic. We also urge you to consider efforts already underway by members of the Committee to address the ability of loan originators to transition to new jobs under the SAFE Act, legislation to address consumer protection concerns with PACE lending (S. 838), as well as reauthorization of the National Flood Insurance Program and legislation to further develop the private flood insurance market (S. 563).

I. Regulatory Clarity and Relief

Description: The Consumer Financial Protection Bureau's (CFPB) use of consent decrees and administrative decisions to make changes in the rules, rather than formal rulemaking or published guidance, has created uncertainty in the market and higher costs for consumers. MBA believes the CFPB, when implementing new rules or changing the interpretation of existing rules, should adopt clear "rules of the road" through the issuance of

official, written interpretative rules, supervisory guidance and/or compliance bulletins to facilitate regulatory certainty and consistent consumer protections throughout the market.

Impact on Consumers and Market Participants: Over the past five years, the costs of originating a mortgage loan have increased and HMDA data indicate the total number of lenders has declined. Furthermore, large institutions have pared back their participation in the market. This ultimately impacts the American consumer, driving up the cost of credit, delaying closings, as well as limiting borrowers' choices due to reduced market competition. Increasing regulatory clarity will allow lenders to operate under clear guidance and decrease costs for lenders and consumers alike.

Economic Impact: Residential mortgage credit availability remains constrained due in part to uncertainty regarding the lack of clear guidance and overly aggressive enforcement actions, both of which have led to the rising costs of originating and servicing home loans. Restrictions on credit availability for housing may in turn hinder the ability of potential first-time homebuyers to purchase a home and existing homeowners to move. With the reduced pace of home sales, household mobility has declined. Research shows that a lack of mobility has a negative impact on economic growth as labor resources do not move to where they are most needed. Further, tight credit conditions may exacerbate the widening wealth gap in the United States as fewer first-time homebuyers gain access to the ability to build housing wealth, especially those not receiving parental financial assistance.

Specific Recommendations: Congress should require the CFPB to establish and abide by a consistent framework for providing industry with authoritative written guidance that facilitates efficient compliance, reduces implementation costs, and ensures consistent consumer treatment across the market. That framework should:

- For existing rules, require rulemaking or, where appropriate, written guidance (prospectively applied) if the CFPB is making a change in prior rules or guidance (whether formal or informal).
- For significant new rules, require the CFPB to comprehensively evaluate implementation and dedicate resources to providing written guidance or amendments to the rule to address post-rule contingencies, unintended consequences, or other infirmities in the rule.

Legislative Language: Proposed language to address many of these concerns is attached (Attachment A: Regulatory Clarity and Relief Language).

II. Servicing Market Regulations and Basel III Requirements

Description:

Cost of Servicing: MBA believes that mortgage servicing market regulations would benefit from review and coordination among federal agencies and government guarantors. The streamlining and harmonization of existing regulations will allow lenders to lower costs and increase the availability of credit. The variations in procedures or regulatory requirements among the federal agencies create inefficiencies and add complexity to the system, and can have adverse consequences for consumers that may not be clear at origination. For example, the Department of Veterans' Affairs (VA), Federal Housing Administration (FHA), and Fannie Mae and Freddie

Mac (GSEs) under the conservatorship of the Federal Housing Finance Agency (FHFA) all have different loan modification programs, despite a broad consensus on what constitutes the elements of a successful loss mitigation program. To alleviate these differences, MBA strongly urges government insurer and guarantor alignment toward the recently released GSE “Flex modification” program to harmonize these requirements, reduce cost for servicers, and lessen confusion as well as disparities in outcomes based on loan products.

Basel III: The punitive treatment of mortgage servicing rights (MSRs) under the Basel III risk-based capital standards is acting as an impediment to lending and servicing and should be reconsidered. These standards, imposed on U.S. institutions by an international regulatory body, threaten to undermine the value of this important asset, with adverse implications for the entire mortgage finance chain. The new Basel III rule increases the risk-weighting of MSRs held by banks from 100 percent to 250 percent. It also decreases the cap on MSRs that a bank may hold on its balance sheet from a 50 percent common equity component of tier one capital to a more stringent 10 percent limit with MSR assets above the limit deducted from regulatory capital. In addition, MSRs, deferred tax assets and equity interests in unconsolidated financial entities are limited, in aggregate, to a 15 percent common equity component of tier one capital before they must be deducted from regulatory capital. This unnecessarily punitive treatment of MSRs makes them one of the most costly asset classes in the entire Basel III framework, despite any clear linkage of MSRs to the financial upheaval that Basel III is intended to address.

Impact on Consumers and Market Participants: MBA data show that the cost to service a performing loan has gone from $58 in 2008 to $228 by the first half of 2016. For a non-performing loan this increase is even more dramatic, as costs have gone from $482 to $2,522. These additional costs ultimately get passed through to consumers by raising the cost of new loans. Likewise, they directly impact consumer access to credit as defaulted loans cost more than 11 times as much to service as performing loans, causing lenders to reduce their exposure to borrowers that are perceived to pose greater risk.

With regard to Basel III, MSRs are not widely utilized outside of the United States but are a vital component of the American housing finance system’s ability to provide a 30-year fixed-rate mortgage. Furthermore, the punitive treatment of MSRs and the increase in servicing costs has forced many community banks and smaller institutions to significantly scale back mortgage loan servicing or exit the market altogether.

Economic Impact: Higher servicing costs are ultimately passed on to consumers. Some potential homebuyers will not be able to afford a home at the higher cost and others will be unable to refinance in order to access the equity they have built in their homes, or to lower their monthly payments. On the margin, some borrowers will not be provided access to credit at all, reducing mobility and wealth building opportunities for American households.

Specific Recommendations: MBA believes the agencies tasked with regulating mortgage servicing should be required to coordinate with one another in order to provide consistency in the mortgage servicing space and minimize regulatory conflicts.

MBA believes that performance, capacity, and consumer service quality should be the primary drivers of which servicers gain market share, not excessively high capital standards on a particular segment of the industry. Nor should American banks be handicapped by an international agreement that discriminates against an asset that is uniquely integral to the

American mortgage finance system. The current Basel treatment of MSRs, amid the backdrop of complicated and conflicting servicing rules, discourages many community banks from originating mortgages and retaining the servicing, or from acquiring servicing assets. Moreover, it impacts nonbank lenders by removing an important bid for MSR assets from the market.

***Legislative Language**:* Language to address these concerns is attached (Attachment B: MBA Servicing language).

III. Ability to Repay and Qualified Mortgage Rule Improvements

Description: The Dodd-Frank Act and the CFPB's Ability to Repay (ATR) rule requires lenders to determine whether a borrower has a reasonable ability to repay a mortgage before the loan is consummated. This obligation is coupled with significant penalties and liability for failing to meet this requirement. The ATR rule also provides a presumption of compliance for loans that are originated as Qualified Mortgages (QMs), which provides greater certainty to lenders and mortgage investors regarding potential liability where there has been compliance but a claim is made. Consequently, most lenders have limited themselves to making only QM safe harbor loans to minimize potential liability and litigation. The ATR rule and QM standards must be improved to responsibly widen the credit box. While MBA appreciates some earlier efforts to address flaws in the QM definition, we believe changes to the ATR rule should not be confined to particular types of institutions or business models. The QM definition should be fixed holistically, not revised in piecemeal fashion with special exceptions for certain categories of lenders.

Impact on Consumers and Market Participants: As a result of some of the constraints in the QM definition, many borrowers who should qualify for a QM are unable to access safe, sustainable, and affordable mortgage credit.

Economic Impact: Especially as ATR/QM creates a negative impact on small loans, the rule has had a negative impact on potential first-time homebuyers and those with lower incomes and less wealth, denying these households the ability to access homeownership and its wealth-building potential. Wealth-building for lower income households is especially important in providing them resources to weather times of economic stress and to provide opportunities for their children, especially with respect to education.

Specific Recommendations:

1. **Expand the Safe Harbor**

   All loans satisfying QM requirements should have a legal safe harbor regardless of their rate. The current 150 bps limit is too narrow considering the inclusion of fees in the Annual Percentage Rate (APR).

2. **Increase the Small Loan Definition**

   The current definition of a smaller loan under the ATR rule – where points and fees may exceed three percent and still qualify as a QM – is set at $102,894 (for 2017). This metric is too low considering the average loan size is approximately $260,000. As a result, too many smaller loans do not qualify as QMs. The points and fees cap should apply only to loans of $200,000 or more, with a sliding scale that permits progressively

higher points and fees caps for smaller loans. This change would increase QM lending to moderate-income borrowers who have smaller loan balances.

3. **Establish Alternatives to Appendix Q**

   For those loans not satisfying the QM patch, underwriting of QM loans must be conducted in accordance with Appendix Q of the rule. Unfortunately, Appendix Q is generally viewed as lacking sufficient guidance and flexibility to be used as an underwriting standard. To rectify this problem, MBA supports regulatory or legislative changes to allow the use of other commonly accepted underwriting standards such as those acceptable to FHFA, FHA, VA, and the Rural Housing Service (RHS).

4. **Broaden Right to Cure for DTI and other Technical Errors**

   MBA has long advocated for an amendment that would permit the correction of errors where the three percent points and fees limit is exceeded. To encourage lending to the full extent of the QM credit box, MBA also urges that the right to cure or correct errors be extended to debt-to-income (DTI) miscalculations and other technical errors. There is an existing points and fees cure, but it will apply only to loans closed on or before January 10, 2021. MBA believes there is a need for both a permanent points and fees cure as well as a DTI cure.

5. **Replace the Patch and the Default QM**

   The “QM patch” – which allows loans approved by the GSEs’ underwriting systems to qualify as QM – is essential at this time, however, it is only a temporary solution while the GSEs are in conservatorship or until 2021. Loans must be consummated on or before January 10, 2021 (unless the conservatorship ends earlier). MBA urges the CFPB to start the process of working with stakeholders to develop a transparent set of criteria, including compensating factors, to define a QM – replacing both the QM patch and the 43 percent DTI standard. Such a standard must provide workable, flexible underwriting standards that are consistent with the Dodd-Frank Act without injecting undue complexity or uncertainty into the process of serving consumers’ credit needs.

Legislative Language: Language to address these concerns is attached (Attachment C: MBA QM Changes).

IV. FHLB Membership Rule

Description: In January 2016, the Federal Housing Finance Agency finalized and implemented a rule that changed the Federal Home Loan Bank System’s (System) membership eligibility requirements to prohibit captive insurance companies from becoming members of the System. The rule amended the Federal Home Loan Bank Act – without congressional approval and contrary to the Act’s express language that “any... insurance company” is eligible for membership. Since 2012, mortgage REITs (mREITs) have utilized their captive insurers as a means to gain membership in the System; now that the eligibility standards have changed, mREITs are no longer permitted to access the System.

Impact on Consumers: In the wake of the financial crisis and uneven housing market recovery, captive insurance companies represent an opportunity for private capital to expand homeownership opportunities for credit-worthy borrowers. mREITs provide liquidity to

underserved, non-QM and other non-traditional borrowers, and are helping spur the return of a non-agency mortgage securitization market.

Economic Impact: Restrictions on credit availability for housing may hinder the ability of potential first-time homebuyers to purchase a home and existing homeowners to move. Granting mREITs continued access to the FHLB system would allow them to invest in a broader array of agency MBS, potentially spurring additional lending within the current GSE "credit box."

Specific Recommendations: MBA believes Congress should pass legislation that re-permits captive insurers to gain access to the System. Such legislation would give FHFA the clear direction it needs to allow captive insurance companies who commit to supporting the residential home market access to the System.

The narrowly tailored legislation includes a strong housing nexus that will only permit mREITs primarily engaged in the making or purchasing of residential home loans to join. This will ensure members of the System are aligned with the overall mission of the Federal Home Loan Banks.

Legislative Language: Proposed language to address this issue is attached (Attachment D: FHLB Membership Rule Language).

VII. High Volatility Commercial Real Estate

Description: The final Basel III risk-based capital rule jointly issued by the banking agencies generally treats commercial acquisition, development or construction (ADC) loans as "High Volatility Commercial Real Estate" (HVCRE) if they do not meet certain exemption requirements as to: (1) supervisory loan-to-value (LTV) standards, (2) borrower contribution requirements, and (3) contractual limitations on withdrawal of capital during the life of the loan. Loans characterized as HVCRE are subject to a 150 percent risk weight (12 percent capital requirement).

We are concerned that the rule is not sufficiently clear and that it results in HVCRE treatment for many loans with standard risk characteristics. While MBA and others have brought these concerns to the agencies that promulgated these rules, they have not yet taken sufficient action to address them. We note that the agencies' recent March 2017 Joint Report to Congress addressing the Economic Growth and Regulatory Paperwork Reduction Act[1] indicated an intention to reduce regulatory burden on community banking organizations by simplify the HVCRE rule. There is no indication in the report, however, as to whether that change would address the specific issues we raise. Moreover, if such change applies only to community banks, it will not provide the necessary relief for larger banks, even if it addresses our specific issues.

Economic Impact: Based on the experience of our members, we have seen that the issues described above have caused inconsistency and confusion around the application of the rules, which has resulted in unwarranted increases in costs to borrowers. That, in turn, has had an

[1] Joint Report to Congress; Economic Growth and Regulatory Paperwork Reduction Act, p. 4 (March 2017) (issued by the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation and the National Credit Union Administration); https://www.occ.gov/news-issuances/news-releases/2017/nr-ia-2017-33a.pdf

adverse impact on the availability of funding for ADC commercial real estate projects that can support growth of jobs and the economy, and has undermined the economic feasibility of projects.

Specific Recommendations: We do not recommend eliminating the 150 percent risk weight for HVCRE loans. Rather, to provide clarity to banks and to better align HVCRE treatment with factors affecting credit risk, MBA recommends that the specifications around HVCRE be modified as follows:

- Clarify the definition of an "HVCRE ADC Loan"
- Permit banks to count the value of appreciated property toward the borrower's required 15 percent capital contribution;
- Provide banks with greater flexibility to permit some capital withdrawals during the life of the loan without triggering HVCRE status; and
- Exempt loans originated prior to January 1, 2015.

Legislative Language: Proposed legislation is attached (Attachment F: HVCRE language) that would address these concerns.

VI. CMBS Risk Retention

Description: The final risk retention rule under Section 941 of the Dodd-Frank Act became effective December 24, 2016, for the commercial mortgage backed securities market (CMBS). Under the final rule, a sponsor of a securitization transaction is required retain a 5 percent interest in the transaction. That retained interest can be in the form of (1) a vertical interest; (2) a horizontal interest; or (3) an L-shaped interest combining both vertical and horizontal interests.

Economic Impact: The CMBS market is in the process of adjusting to the risk-retention rule, and we remain concerned that the current retention rules will add costs to the security borne by borrowers, which in turn will stifle economic growth and reduce investor interest in the commercial real estate market.

Specific Recommendations: While the final rule was improved significantly from what was proposed in 2011, we believe the following additional improvements are needed to implement Section 941 of the Dodd-Frank Act in a manner that avoids unnecessarily restrictive impacts on CMBS market:

- Modify the unduly restrictive underwriting metrics for determining which "qualified" CRE (QCRE) loans are eligible for zero risk retention.

- Exempt single asset, single borrower (SASB) CMBS from the risk retention requirement.

- Expand the range of retained interest structures that satisfy risk-retention requirements to permit either a senior-subordinate structure or pari passu for third-party purchasers of the horizontal "risk retention" residual interest. Under current rules, residuals interests must be shared pari passu.

Legislative Language: In February 2016, Representative French Hill (R-AR) introduced H.R. 4620, the Preserving Access to CRE Capital Act, which would have implemented the above changes. The text of that legislation is attached in Attachment E.

V. LIHTC Allocations Must Not Be Tied to Provision of Debt Financing

Description: The Low Income Housing Tax Credit (LIHTC) program has been a critically important catalyst for investment in affordable multifamily rental housing. Qualified private sector multifamily lenders frequently originate and service loans on properties with LIHTC allocations, typically for Fannie Mae, Freddie Mac or FHA/Ginnie Mae. State housing finance agencies (HFAs), which play a crucial role in affordable rental housing production, determine which proposed affordable rental developments are approved for LIHTCs. In recognition of the importance of separating control over both the equity and debt financing components on an affordable rental housing development, the legislative history for the Tax Reform Act of 1986 (Joint Committee on Taxation) states that "Credit allocating agencies may not condition the allocation of credits *to the source of financing* for a low income building" (emphasis added). [2] Many private sector lenders have effective partnerships with HFAs. However, some HFAs have promoted their own in-house debt financing when meeting with potential LIHTC borrowers or developers. Such direct marketing can be very persuasive when suggesting that a borrower (who just received or anticipates receiving a LIHTC allocation from the HFA) should use the HFA's debt financing as the "One Stop Shop" for financing LIHTC multifamily developments.

Economic Impact: Ensuring a competitive market for debt financing and preserving the role of the private sector on LIHTC developments could:

- Reduce a potential inherent conflict of interest when both debt and equity are provided by the same entity.
- Provide competition on multifamily loan interest rates and pricing as well as customer service, both of which are important to reduce costs to the affordable housing transaction.
- Expand expertise on financing affordable multifamily rental housing in the private sector.
- Provide economic benefits associated with public-private sector partnerships since lenders pay taxes, hire employees and otherwise contribute to local economies.

Specific Recommendations: MBA believes the original congressional intent was appropriate and should be incorporated into law so the LIHTC allocating agencies, individually or in partnership with other HFAs, do not provide both the tax credits and debt financing on the same multifamily affordable rental property transaction. Similarly, should there be a workforce housing tax credit program (a.k.a. middle-income housing tax credit) for multifamily rental properties approved by Congress, we urge that distribution of such credits include a prohibition against a HFA providing both tax credits and debt financing on the same property.

Legislative Language: Potential placement of the proposed language is found within the report accompanying the Tax Reform Act of 1986 (P.L. 99-514), at Section 252 Low-Income Housing Credit: Add a provision "Agencies allocating low-income housing tax credits under section 42 of

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[2] General Explanation of the Tax Reform Act of 1986 (H.R. 3838, 99th Congress; Public Law 99-514, page 171), published May 4, 1987.

the Internal Revenue Code may not condition allocation of the credits on the source of financing for the qualifying low-income housing."

Conclusion

We sincerely appreciate the collaborative approach you and your staffs have undertaken since the beginning of the 115th Congress, and we look forward to continuing to work with you on these and other issues important to real estate finance. Should you have any questions regarding any of the suggestions outlined above, please feel free to contact Meghan Sullivan (msullivan@mba.org) or Brad Cheney (bcheney@mba.org) on my team.

Sincerely,

Bill Killmer
Senior Vice President, Legislative & Political Affairs