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HEARING BEFORE THE

HOUSE FINANCIAL SERVICES COMMITTEE
SUBCOMMITTEE ON CAPITAL MARKETS, INSURANCE AND GOVERNMENT SPONSORED ENTERPRISES

ENTITLED

LEGISLATIVE PROPOSALS ON GSE REFORM

WRITTEN TESTIMONY OF
THOMAS M. STEVENS, CRB, CRS, GRI
2007 IMMEDIATE PAST PRESIDENT

NATIONAL ASSOCIATION OF REALTORS®
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Chairman Kanjorski, Representative Pryce and Members of the Subcommittee, thank you for inviting me to testify today. My name is Tom Stevens, and I am the 2007 Immediate Past President of National Association of REALTORS®. I am also the former President of Coldwell Banker Stevens (now known as Coldwell Banker Residential Brokerage Mid-Atlantic) – a full-service realty firm specializing in residential sales and brokerage.

I am here to testify on behalf of our more than 1.3 million REALTOR® members 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®. Fannie Mae and Freddie Mac are partners in the housing industry and as such, I appreciate the opportunity to share our views on the issues involved in legislative proposals designed to strengthen the regulation of the housing government-sponsored enterprises (GSEs) and the Federal Home Loan Banks.

It has been almost two years since REALTORS® testified before Congress on the issue of improving the regulation of the housing GSEs. When we first testified on this issue, the subject was still new; various issues had yet to be considered or debated; and some ideas that had been discussed were quite controversial. While there was a considerable amount of activity in the 109th Congress, it unfortunately adjourned without enacting a GSE reform bill. It is our understanding that at the end of the 109th Congress, Chairman Frank, then ranking member of the House Financial Services Committee, worked with Treasury to negotiate a compromise proposal, some provisions of which may be included in forthcoming legislation.

NAR did not take a public position on any of the particular compromise provisions that were reported in the media and I do not attempt to do so today. Instead, my remarks will focus on six elements which we believe are important to address in GSE reform legislation. They are:

1. Strong regulator and GSE governance;
2. Housing mission;
3. New program approval;

4. Separation of mortgage origination and the secondary market ("bright line");
5. Portfolio limits; and
6. Conforming loan limits.

As we testify today, we eagerly await new draft legislation which will create a strong regulatory regime that preserves the housing mission of the GSEs and strengthens the nation's housing finance system.

Strong Regulator and GSE Governance

Over the last two years, a general agreement on the basic framework for a new GSE regulatory structure has evolved. That consensus strongly suggests that the current regulatory responsibilities of the Office of Federal Housing Enterprise Oversight (OFHEO), the Department of Housing and Urban Development (HUD), and the Federal Housing Finance Board should be transferred to a single, independent safety and soundness regulator for Fannie Mae, Freddie Mac, and the Federal Home Loan Banks. This new housing enterprises regulator should have the authority to set capital standards; liquidate a financially unstable enterprise through a conservator or receiver; and approve new programs and products. The Federal Home Loan Banks should be regulated under the same framework, with due concern for cooperative ownership by member financial institutions. There is also general agreement that Fannie Mae and Freddie Mac affordable housing goals should be refined.

NAR supports strengthening financial soundness regulation for Fannie Mae, Freddie Mac, and the Federal Home Loan Banks through an independent regulatory agency. Having independent, expert financial oversight will enhance confidence in the nation's housing finance system. This new regulator should have the appropriate authority and resources to oversee safety and soundness of the GSEs. The regulator also should understand and support the GSEs' vital housing finance mission and the role that housing plays in the nation's economy and public policy.

NAR also supports a continued independent, public voice in the corporate governance of the GSEs. We believe that the board of Fannie Mae, Freddie Mac and the Federal Home Loan Banks should be well balanced in knowledge and expertise in the full range of GSE-related issues and activities. NAR supports the legislative efforts to address concerns regarding the governance of the Federal Home Loan Banks by enhancing the Banks' direct role in selecting board members, raising the number of independent directors, adding community and economic development expertise, and allowing appointed independent directors to continue their service until a successor is in place.

Housing Mission and the Secondary Mortgage Market

Congress chartered Fannie Mae and Freddie Mac with advantages unavailable to commercial banks and other financial institutions. Fannie Mae and Freddie Mac enjoy lower funding costs, the ability to operate with less capital, and lower direct costs. These advantages were and are an integral component of the GSEs' public policy mission. The advantages of GSE status have helped the secondary mortgage market grow and provided much needed stability to our nation's housing financial system.

Very simply, Congress created Fannie Mae and Freddie Mac to do what no fully private company could or was willing to attempt. Unlike private secondary market investors, Fannie Mae and Freddie Mac remain in housing markets during downturns, using their federal ties to fulfill their public purpose obligation to facilitate mortgage finance and support homeownership opportunity.

In their own ways, each of the housing enterprises have used their federal charter advantages to meet their missions. The "mechanism that widens the circle of ownership," as one observer defined the secondary mortgage market, is dynamic, robust and continually evolving – all to the benefit of mortgage originators, home buyers, and other industry participants.

The broad expansion of homeownership, mortgage markets, as well as the related rapid growth of the GSEs has also had another effect. Financial services providers, many of which compete with Fannie Mae and Freddie Mac, now question the GSEs' activities, function, and the continuing need for their government-chartered status. These financial companies argue that Fannie Mae and Freddie Mac have an unfair advantage because of their federal charter ties. Yet these same lenders' parent banking companies have their own federal subsidies that come in the form of deposit insurance and other benefits derived from the nation's banking and financial system safety net.

REALTORS® believe that the GSEs' housing mission, and the benefits that derive from it, play a vital role in the continued success of our nation's housing system. We have opposed and will continue to oppose legislative proposals that would reach beyond safety and soundness regulation and diminish the housing mission of the GSEs.

New Program Approval

Currently, Fannie Mae and Freddie Mac cannot initiate a new program without first obtaining the approval of HUD. When GSE reform was considered in the 109th Congress, the issue of program approval, specifically the limitations of the current statute, was widely debated. NAR believes that any legislative proposal that attempts to address the program approval process should not include new regulatory requirements that could unduly delay or prevent the GSEs from developing new programs and products that support their missions.

For example, such authority should not undermine secondary market innovations based on Fannie Mae and Freddie Mac credit risk management technologies. These innovations assure a smooth supply of reasonably priced mortgage credit and allow homebuyers to manage their interest rate risk when locking loans rates and terms before closing.

NAR believes that whatever approach Congress takes to address the shortcomings of the current statutory framework, the result must be flexible to promote product and program innovation and allow for prompt responses to housing market needs.

Separation of Mortgage Origination and Secondary Market

REALTORS® recognize and support the role that program, business and activity approval may have on the financial safety and soundness of the GSEs. However, not every new activity of the GSEs should be subject to an extended regulatory public comment process. This requirement could directly damage the GSEs' housing mission, and stifle innovation and programs that would help Americans achieve the dream of homeownership.

In the 109th Congress, one legislative proposal that NAR cautioned against was the "bright line" regulation, which would have distinguished mortgage origination from GSE secondary market activities and imposed restrictions on Fannie Mae and Freddie Mac mission-related activities. One "bright line" proposal would have specifically prevented the GSEs from directly or indirectly participating in mortgage origination and may have required Fannie Mae and Freddie Mac to divest themselves of their automated underwriting systems, upon which many banks rely.

REALTORS® oppose overly restrictive "bright line" legislative proposals that explicitly limit GSEs business to the secondary markets, strictly defined. It would instantaneously preclude many of the GSEs' existing products and activities that were designed to increase access to mortgage credit, lower the costs of homeownership, and foster innovations in home financing.

For example, the "bright line" provision would seriously hinder (and possible prohibit) the array of mission-related, consumer outreach activities by lenders and housing counselors that are supported by the GSEs. The GSE-designed counseling and education programs that help lenders, mortgage brokers, REALTORS®, and housing counseling agencies determine a consumer's financial readiness for homeownership are technically on the "wrong side" of the "bright line" and would be prohibited.

This is just one example of the negative impact such a standard would have on critical components of the housing market. REALTORS® urge you to reject the rigidity and arbitrariness of a statutory "bright line" test.

Portfolio Limits

One of the most widely debated issues has been the size of the portfolios currently held by the GSEs and whether the portfolios contribute to the GSEs' mission. Then Federal Reserve Board Chairman Alan Greenspan was one of the most vocal advocates of legislative proposals to shrink the size of the GSEs' retained portfolios. Chairman Greenspan and others have argued that the size of the portfolios, together with the perceived incentives for the GSEs to pursue portfolio growth, increase the possibility of GSE insolvency and destabilization of our nation's financial markets.

Significantly, those advocating retained portfolio limitations do not identify any immediate systemic financial risk. Viewed strictly from a systemic risk perspective, GSE retained portfolios, just like the portfolios of the 5 largest banks in the U.S., are vulnerable to interest rate changes and could pose a risk to taxpayers should the enterprise or the bank become insolvent or improperly hedge risk. Without more information, we do not see a need to impose a systemic risk test on the GSEs that would not also apply to the largest FDIC insured banks.

REALTORS® also oppose rigid statutory limits on the GSEs' portfolio size. Instead, we believe a better legislative approach would be to create a sufficiently strong regulatory authority over capital that would limit portfolio risk and may also moderate portfolio growth, when appropriate.

While it is obviously important to consider the safety and soundness implications of GSE portfolio size and the associated risks, we would ask that the Congress not ignore the advantages that portfolio holdings and size have on mission-related activities and housing markets. The GSEs point out that the returns earned on retained portfolios help support the enterprises' affordable housing programs and also contribute to the availability of financing for low-income borrowers. For example, Freddie Mac reports that approximately $300 billion of the mortgages in their retained portfolio qualify under the affordable housing goals.

Simply stated, REALTORS® oppose portfolio limits imposed just for the sake of shrinking the GSE mission. Portfolio limits should not be prescribed in statute. Instead, we believe the portfolios should be regulated by the GSEs from a risk perspective, and the regulator should determine if one or both of the GSEs' retained portfolios affect safety and soundness.

Conforming Loan Limits

Fannie Mae and Freddie Mac are currently limited by imposed statute to only purchasing mortgages that are within a cap that is determined based on an annual survey of house prices and applied nationally. The 2007 national cap of $417,000 is well above the national median sales price of $219,300[1] for single family homes and exceeds the local median for the majority of housing markets. However, the 2007 national cap is considerably below the local median in the nation's largest high cost metropolitan areas.

NAR supports regional adjustments to conforming loan limits for high-cost areas as a matter of simple equity for American families in these markets. Regional adjustments will help working families in high-cost areas qualify for conforming GSE loans. It will also expand access to FHA and VA mortgages, since both FHA and VA loan limits are tied to the conforming ceiling. Veterans, teachers, firefighters, and police officers are examples of working families who stand to benefit. Access to safe and affordable mortgages is especially important for first-time homebuyers. Regional limits also help existing, middle income homeowners move into more suitable homes to accommodate growing families. By making it more affordable for homeowners to move up the housing ladder, regional adjustments will also help make more affordable homes available for first-time homebuyers.

Limited regional adjustment authority will enable the GSEs to purchase relatively few additional total mortgages from only a few high-cost areas. According to a 2005 study we commissioned to evaluate the impact of cap adjustments on the market, the number of conforming purchase money loans purchased by the GSEs would have increased by 2.3% nationally. Additionally, based on NAR's Survey of Existing Home Sales for the 4th quarter of 2006, only seven

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[1] Based on 4th Quarter 2006 NAR Survey data.

metropolitan statistical areas will be affected.[2, 3] Such an adjustment would not change the GSE goals for low- and moderate-income housing.

NAR also believes that regional adjustments to conforming loan limits for high cost areas would give homebuyers access to safer mortgages, which is especially important for first-time homebuyers. Borrowers in high cost markets such as California currently account for a disproportionate share of interest-only and option ARM mortgages. HMDA data show that in many high costs areas FHA-insured mortgages are practically nonexistent and the GSE share of the market is shrinking significantly. Greater access to GSE, FHA, and VA mortgages will help promote homeownership in a safer, more sustainable way.

Finally, there is precedent for regional adjustments for high cost areas. In 1980, Congress designated Alaska, Hawaii, Guam, and the U.S. Virgin Islands as high cost areas. The conforming loan limit in these statutory high cost areas is 50 percent higher than for the rest of the nation, but housing prices in these areas are no longer uniquely high. In fact, housing prices in several high cost areas now exceed those in Honolulu. NAR urges Congress to include in any GSE reform legislative proposal the authorization for regional adjustments to the national conforming loan limits for high-cost areas.

Conclusion

The National Association of REALTORS® shares the belief of our industry partners that Fannie Mae, Freddie Mac and the Federal Home Loan Bank System are integral components of this nation's highly acclaimed housing finance system. Home buyers depend on the secondary mortgage market to supply a continued and stable source of funding for single-family and multifamily housing.

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[2] MSAs Affected in 2007 by Regional Adjustments: NY-Northern NJ-Long Island, NY-NJ-PA; Bridgeport-Stamford-Norwalk, CT; Washington-Arlington-Alexandria, DC-VA-MD-WV; San Francisco-Oakland-Fremont, CA; Los Angeles-Long Beach-Santa Ana, CA, San Jose-Sunnyvale-Santa Clara, CA; and San Diego-Carlsbad-San Marcos, CA.

[3] Two markets in each of three states—California, Florida, and Massachusetts—would have benefited from regional conforming loan limit authority in 2005 when the national limit was $359,650. Several of these are within 10% of the current $417,000 limit: (a) the Boston-Cambridge-Quincy, MA-NH MSA has a median sales price of $388,000, and (b) the Riverside-San Bernardino-Ontario, CA MSA has a median sales price of $406,400.

NAR believes GSE reform legislation should be principally focused on safety and soundness regulation and should protect Fannie Mae's and Freddie Mac's abilities to accomplish their housing mission. We hope that Congress can reach a consensus on GSE reform, so that all in the housing industry can focus our efforts on increasing affordable homeownership opportunities, especially among minorities and other underserved populations.

The National Association of REALTORS® pledges to work with the 110th Congress to enact GSE reform legislation that achieves our mutual goals and protects the vibrancy, liquidity and evolution of the housing finance system.