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WRITTEN TESTIMONY OF

TOM SALOMONE
2012 DIRECTOR, REALTOR® PARTY ACTIVITIES
NATIONAL ASSOCIATION OF REALTORS®

BEFORE THE

UNITED STATES HOUSE OF REPRESENATIVES
COMMITTEE ON FINANCIAL SERVICES
SUBCOMMITTEE ON CAPITAL MARKETS AND GOVERNMENT-SPONSORED ENTERPRISES

HEARING REGARDING

THE PRIVATE MORTGAGE MARKET INVESTMENT ACT, PART II

DECEMBER 7, 2011

INTRODUCTION

On behalf of the more than 1.1 million members of the National Association of REALTORS® (NAR), thank you for holding this important hearing examining the U.S. housing finance system.

My name is Tom Salomone, NAR's Committee Liaison for the Issues Mobilization, the Political Involvement and REALTOR® Political Action committees. I have been a REALTOR® for more than 31 years and am the owner of Real Estate II and Real Estate II of Margate, firms specializing in residential real estate. Currently, I serve as a member of NAR's Executive Committee and from 2000 to 2011 was a member of NAR's Board of Directors. As with many of my colleagues who have testified before this committee in the past, my life and passion is real estate. So, it is my honor to be here today to speak on behalf of NAR's 1.1 million members, and the millions of Americans who own a home, want to sell a home, or just provide rental opportunities to those who require a home.

Since the onset of the global financial crisis there have been relentless attacks on the U.S. housing finance system. The majority of these attacks were carried out by groups who are ideologically opposed to the existing system, which includes some government participation in the conventional conforming market. Of distinct interest to NAR as an advocate for the housing consumer is that this vocal minority is increasingly being told that the current guiding principles of the U.S.' existing housing finance system (e.g. long-term payment structures, reasonable down payment levels, and government participation), are appropriate and necessary. However, the American public and policy experts are saying that "we"—lenders, consumers, real estate professionals, regulators, and Congress—must be better stewards of the system if it is to effectively serve future American homebuyers and mortgage investors as it did prior to the recent financial market meltdown.

THE PRIVATE MORTGAGE MARKET INVESTMENT ACT

REALTORS® believe that the legislation proposed by Chairman Garrett (R-NJ), the "Private Mortgage Market Investment Act", is a good first step toward bringing stability, confidence and transparency to the private side of housing finance. REALTORS® are fervent believers in "free markets", and acknowledge the need for private capital to reduce the Federal government's role in this sector. The rules put-in-place by this legislation to: (1) create standards and uniformity, (2) provide investors with transparency, and (3) ensure legal certainty with regard to investors' rights could create the confidence required to reignite the private label securities market. Should growth in the private market space result from the implementation of this legislation, then ultimately the role the government plays in housing finance will be reduced, which is what we all desire. REALTORS® also believe that even when the government's role in the housing sector is reduced, there will still be a need for some government participation in the conventional conforming space.

Therefore, REALTORS® believe that this bill's approach cannot be viewed as a comprehensive solution to the housing finance sector's reform needs. If enacted, this proposed legislation must be coupled with comprehensive reform of the Government-Sponsored Enterprises (GSEs) if we are going to ensure that the housing finance system will work efficiently, and more importantly, effectively in the future. An example of a bill that this legislation could be coupled with is H.R 2413, the Secondary Market Facility for Residential Mortgages, introduced by Representatives Gary Miller (R-CA) and Carolyn McCarthy (D-NY), which has a role for government participation in the conventional conforming portion of the secondary mortgage market.

REALTORS® believe the inclusion of government participation in the conventional conforming portion of the secondary mortgage market is necessary and appropriate because we understand that in extreme economic conditions private capital will retreat from the market, requiring the participation of an entity that will remain active in the marketplace regardless of economic conditions. A full shut-down of the conventional conforming portion of the secondary mortgage marketplace, means there would be very limited or no funding for middle class homeowners or homebuyers, which would be devastating to the national economy—possibly causing a catastrophic collapse. Presently, we continue to see the downward pressure that housing is having on the economy; therefore, tools that can be used to mitigate such effects, should be put-in-place and utilized to unsure viability of this extremely important economic sector.

The government-sponsored enterprises (GSEs) were created to support that specific mission within the secondary mortgage market. The future U.S. secondary mortgage market must include an entity with that purpose in order to ensure that creditworthy American families will always have access to affordable mortgage capital.

THE U.S. HOUSING FINANCE SYSTEM: THE REALTORS'® PERSPECTIVE

There are many systems of housing finance globally, and all have their merits for the countries they serve. REALTORS® believe that the U.S. housing finance system, which utilizes securitization to recapitalize mortgage lenders, works best for a nation of our size with our fervor for real property ownership. Mortgage products that offer the populace reasonable down payment requirements, as well as provide affordable access to the remaining capital required to close the property sale, are what REALTORS® believe is in the best interest of the American public. We do not believe that the underlying system, which until recently has afforded many qualified, middle and lower income American families the ability to purchase a home, should simply be scrapped.

Our belief in the existing U.S. housing finance system does not mean that REALTORS® do not believe that reforms cannot, or should not, be undertaken. Over the past 3 years, in testimony before the House Financial Services Committee, as well as the Senate Banking, Housing, and Urban Affairs Committee, REALTORS® have indicated the need for repairs to the U.S. housing finance structure (see Appendix A).

REALTORS® agree with lawmakers and the Administration that taxpayers should be protected, private capital must return to the housing finance market, and that the size of government participation in the housing sector should decrease if the market is to function properly. Those who advocate for legislation that constrains or removes government participation from the conventional mortgage market, and/or relies only on a purely private secondary mortgage market need only examine the current miniscule activity in the jumbo and manufactured housing mortgage markets in order to understand the implications of such a system. In both of these markets, mortgage capital became nearly non-existent, which prohibited creditworthy borrowers from access to the funds required to purchase a home.

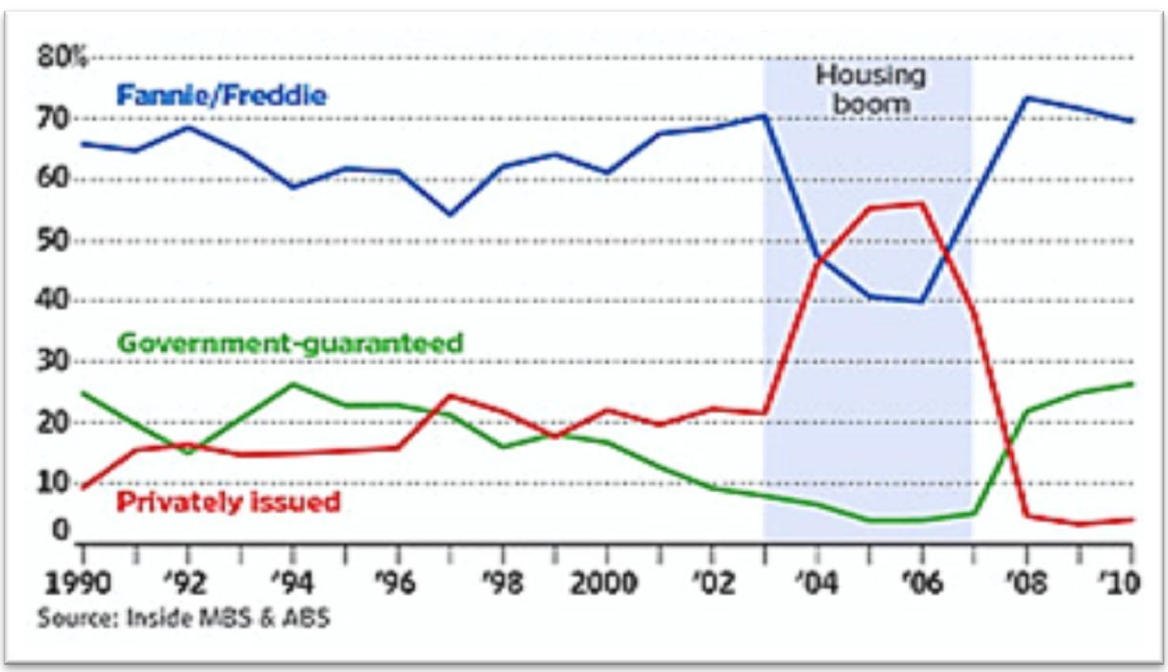
OUR NATION'S UNIQUE SECONDARY MORTGAGE MARKET

Congress chartered Fannie Mae and Freddie Mac to expand homeownership opportunities and provide a stable foundation for our nation's housing finance system. Unlike private secondary market investors, Fannie Mae and Freddie Mac remained in housing markets during past market downturns, and have used their federal ties to facilitate ongoing access to affordable mortgage finance when other players have left the market.

REALTORS® believe that the GSEs' housing mission, and the benefits that are derived from it (e.g. long-term fixed-rate mortgages), played a vital role in the success of our nation's housing system, and continue to play a key role today. Without these secondary mortgage market facilities providing affordable mortgage capital during the current market disruption, there would have been a much more serious disruption to the market.

As the market turmoil reached its peak in late 2008, it became apparent that the role of the GSEs, even in conservatorship, was of utmost importance to the viability of the housing market as private mortgage capital effectively fled the marketplace. As indicated in Table 1, below, if no government-backed conventional mortgage market facility entity (i.e. Fannie Mae and Freddie Mac) existed as private mortgage capital fled to the side lines, the housing market would have fallen even further and thrown our nation into a deeper recession, or even a depression.

Table 1: Share of Mortgage Securitization Market by Segment



THE 30-YEAR FIXED-RATE MORTGAGE

Unique to the U.S. housing finance sector is the availability of affordable, long-term fixed-rate mortgages. The 30-year fixed rate mortgage is the bedrock of the U.S housing finance system. And now, more than ever, consumers are seeking fixed rate 30-year loans because they are easily understood and offer a predictable payment schedule.

REALTORS® believe that full privatization is not an effective option for our secondary mortgage market because private firms' business strategies will focus on optimizing profits. This model would foster mortgage products that are more aligned with these business' goals than in the best interest of the nation's housing policy, or the consumer. We believe that this would lead to the elimination of long-term, fixed rate mortgage products (e.g. 30-year fixed-rate mortgage), and an increase in the costs of mortgages to consumers.

In fact, based on early data from a survey that NAR is conducting on the impact of the new, lower GSE loan limits, we are beginning to see signs of how the private market impacts consumers. Preliminary data indicates that consumers who are now above the new lower conventional conforming loan limit are experiencing significantly higher interest rates and the need for substantially larger down payments. According to data, this is leading to "a loss of interest" in real estate sales. (NAR will provide the committee with details from the full report once the data has been fully analyzed.) At a time when our economic recovery teeters on the edge of collapse, activities and reforms that force further constriction of economic activity should be resisted.

Furthermore, according to additional research by economist Dr. Susan Woodward, there is no evidence that a long-term fixed-rate residential mortgage loan would ever arise spontaneously without government urging. Dr. Woodward points out that a few developed countries have encouraged the use of amortizing long-term loans, but in all instances (save for Denmark) where they do exist, the loans have adjustable rates and recast every 5 years. She goes on to indicate that the United States is unique in having 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. Dr. Woodward points out 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.

The affordability and availability of the fixed-rate mortgage has yielded a US residential mortgage market that stands at approximately $11 trillion. Today, the GSEs own or guarantee $5 to $6 trillion of mortgage debt outstanding and provide capital that supports roughly 70% of new mortgage originations. REALTORS® believe that it is extremely unlikely that any secondary mortgage market structure that does not include securitization and have some government backing could support the existing mortgage funding needs of the United States housing sector, while making mortgages available in all markets under all economic conditions.

Lastly, REALTORS® fear that in times of economic upheaval, a fully private secondary mortgage market will largely cease to exist as has occurred in the jumbo mortgage, the commercial mortgage, and the manufactured housing mortgage markets. When the economy turns down, private capital understandably flees the marketplace. Should that happen under a fully private secondary mortgage market model, the results for the entire economy would be fatal because affordable long-term fixed-rate mortgage funding would no longer be available, and the plethora of peripheral industries that support and benefit from the residential housing market would suffer.

CONCLUSION

The National Association of REALTORS® applauds Chairman Garrett's efforts to bring back stability and confidence in the private label mortgage securities market space. However, we believe that this bill will be most effective if coupled with legislation that supports a secondary mortgage market model that includes some level of government participation, while protecting the taxpayer and ensuring that all creditworthy consumers have reasonable access to mortgage capital so that they too may attain the American Dream: homeownership.

I thank you for this opportunity to present our thoughts on the Private Mortgage Market Act. The National Association of REALTORS® is anxious to work with the Chairman, and our industry partners, on this thoughtful piece of legislation which is an excellent first step toward finding a solution that best meets the needs of the U.S. housing consumer and their desire for homeownership.

APPENDIX A:
KEY GSE REFORM POINTS BASED ON NAR's PRINCIPLES

- An efficient and adequately regulated secondary market is essential to providing affordable mortgages to consumers. The secondary market, where mortgages are securitized and/or combined into bonds, is an important and reliable source of capital for lenders and therefore for consumers.

  Without a secondary market, mortgage interest rates would be unnecessarily higher and unaffordable for many Americans. In addition, an inadequate secondary market would impede both recovery in housing and the overall economic recovery.

- We cannot have a restoration of the old GSEs with private profits and taxpayer loss system. The current GSEs should be replaced with government chartered, non-shareholder owned entities that are subject to sufficient 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.

- Government-chartered entities have a separate legal identity from the federal government but serve a public purpose (e.g. the Export-Import Bank). Unlike a federal agency, these new entities will have considerable political independence and be self-sustaining given the appropriate structure.

- The mission must be to ensure a strong, efficient financing environment for homeownership and rental housing, including access to mortgage financing for segments of the population that have the demonstrated ability to sustain homeownership. Middle class consumers need a steady flow of mortgage funding that only government backing can provide.

- The government must clearly, and explicitly, guarantee the issuances of the 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 guarantee or other fees paid to the government. This is essential to ensure borrowers have access to affordable mortgage credit. Without government backing, consumers will pay much higher mortgage rates and mortgages may at times not be readily available at all (as happened in jumbo and commercial real estate loans)

- The entities should guarantee or insure a wide range of safe, reliable mortgages products such as 30 and 15 year fixed rate loans, traditional ARMs, and other products that have stood the test of time and for which American homeowners have demonstrated a strong "ability to repay."

- For additional safety, sound and sensible underwriting standards must be established for loans purchased and securitized in MBSs, loans purchased for portfolio, and MBS purchases.

- The entities should price loan products or guarantees based on risk. The organization must set standards for the MBS they guarantee that establish transparency and verifiability for loans within the MBSs.

- 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, they should not be allowed to lobby, and the authorities should be self-funded—no ongoing appropriations).

- In order to increase the use of covered bonds, particularly in the commercial real estate arena, the entities should pilot their use in multifamily housing lending and explore their use as an additional way to provide more mortgage capital for owner-occupied housing. The entities should be allowed to pave the way for innovative or alternative finance mechanisms that meet safety criteria.

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 the entities' performance.