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2011 PRESIDENT
NATIONAL ASSOCIATION OF REALTORS®

SUBMITTED FOR THE RECORD TO THE

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

HEARING TITLED

LEGISLATIVE HEARING ON IMMEDIATE STEPS TO PROTECT TAXPAYERS FROM THE ONGOING BAILOUT OF FANNIE MAE AND FREDDIE MAC

MARCH 31, 2011

INTRODUCTION

On behalf of the 1.1 million members of the NATIONAL ASSOCIATION OF REALTORS® (NAR), thank you for holding this hearing on the need for reform of our Nation's housing finance system.

My name is Ron Phipps, and I am the 2011 President of the National Association of REALTORS. I am proud to be part of a four-generation, family-owned residential real estate business in Rhode Island. My passion is making the dream of home ownership available to all American families. I am proud to testify today on behalf of the more than 1.1 million REALTORS who share that passion, and the 75 million Americans who own homes and the 310 million Americans who require shelter.

REALTORS® agree that the existing system failed and reforms are needed. However, we caution you to heed the words of Treasury Secretary Timothy Geithner and Senator Richard Shelby that, "…housing finance must be addressed and reform passed. However, proper homework must be done before action is taken and federal housing policies must be adequately assessed."

The speed at which the Capital Markets Subcommittee is moving – having a hearing today on GSE reform legislation that was only recently introduced, and planning subsequent hearing in 4 days to mark-up this legislation – constitutes what we believe is moving too quickly, and in too simple a fashion, in an attempt to resolve an issue that is extremely complex and that requires a comprehensive analysis and solution. Therefore, today we will speak in opposition of the bills introduced because they represent a piecemeal approach to reforming the housing finance system, and effectively make Fannie Mae and Freddie Mac nonviable without putting forth an adequate replacement secondary mortgage market mechanism. In an attempt to offer an alternative solution, NAR is collaborating with the offices of Congressmen Gary Miller and Brad Sherman to develop a comprehensive approach to reform the secondary mortgage market.

REALTORS® are fervent in their belief of "free markets", and the need for private capital to reduce Federal government financial support of the housing sector if the housing finance system is to right itself. However, REALTORS® are also practical and understand that in extreme economic conditions, private capital will retreat from the market, requiring the participation of entities that will participate in the market regardless of economic conditions. Secondary mortgage market entities created to support this specific mission are the only way that taxpayers will be assured that they will is always have access to mortgage capital.

REALTORS® agree that taxpayers should be protected, open-ended bailouts should end, private capital must return to the housing finance market, and that the size of the government participation in the housing sector should decrease if the market is to function properly. Where there is disagreement is around the "how" these aspirations should be accomplished. When reviewing proposed legislation that effectively constrains Fannie Mae and Freddie Mac and relies only on private capital to operate the secondary mortgage market, one need only examine the miniscule activity in the jumbo and manufactured housing markets in order to understand the implications of just having private capital form the foundation of the housing market. In both instances, mortgage capital became nearly non-existent, which prohibited qualified borrowers from access to the funds required to purchase a home.

REALTORS® believe that reform of the U.S. housing finance system must be a methodical, measured, and comprehensive effort based on practical market experience, and not just theory. Recently, NAR signed onto an industry letter that espouses the fundamental principles that we all believe are required to ensure a viable secondary mortgage market going forward (see appendix). NAR believes that the industry's basic principles, in concert with our own, form a good foundation on which the secondary mortgage market can be reformed.

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, the entities will have considerable political independence and be self-sustaining given the appropriate structure.

- The mission would 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 & 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 residential 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.

PRIVATE CAPITAL PARTICIPATION, BUT NOT A FULLY PRIVATE SECONDARY MORTGAGE MARKET

REALTORS® believe that full privatization is not an effective option for a secondary market because private firms' business strategies will focus on optimizing their 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, we believe, 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 mortgages to consumers, or both.

According to research provided 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 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 on to 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. Ms. Woodward highlights 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 $10.6 trillion, with the GSEs owning or guaranteeing $5 to $6 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 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, and should that occur in the residential market it would come to an abrupt and complete halt. Should that happen in the residential mortgage market space, 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.

REASONABLE QUALIFIED RESIDENTIAL MORTGAGE (QRM) DEFINITION

The definition of what constitutes a QRM is likely to shape housing finance for the foreseeable future. REALTORS® believe that Federal regulators and members of the House Financial Services Committee should honor the intentions of the concept's authors, Senators Isakson and Landrieu, by crafting a qualified residential mortgage (QRM) exemption that includes a wide variety of traditionally safe, well underwritten products such as 30-, 15-, and 10-year fixed-rate loans, 7-1 and 5-1 ARMs, and loans with flexible down payments that require mortgage insurance. A poor QRM policy that does not heed their intention will displace a large portion of potential homebuyers, which in turn will slow economic growth and hamper job creation.

Strong evidence shows that responsible lending standards and ensuring a borrower's ability to repay have the greatest impact on reducing lender risk. A balance must be struck between reducing investor risk and providing affordable mortgage credit. Better underwriting and credit quality standards will greatly reduce risk. Adding unnecessarily high minimum down payment requirements will only exclude hundreds of thousands of buyers from home ownership, despite their creditworthiness and proven ability to afford the monthly payment, because of the dramatic increase in the wealth required to purchase a home.

NAR is concerned that a narrowly defined QRM will also require severe tightening of FHA eligibility requirements and higher FHA premiums to prevent huge increases in its already robust share of the market, adding additional roadblocks to sustainable home ownership.

Saving the necessary down payment has always been the principal obstacle to buyers seeking to purchase their first home. Proposals requiring high down payments will only drive more borrowers to FHA, increase costs for borrowers by raising interest rates and fees, and effectively price many eligible borrowers out of the housing market.

CONCLUSION

The National Association of REALTORS® supports a secondary mortgage market model that includes some level of government participation, but 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 just one of many conversations regarding how we mend and improve the housing finance system that has served us well for many years. We believe that the key points that we mentioned 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.

Principles for Restoring Stability to the Nation's Housing Finance System

March 28, 2011

The nation's housing finance system is at a historic crossroad. As policymakers debate options to restore vitality, integrity and stability to the secondary mortgage market, including an appropriate role for the federal government in supporting homeownership and rental housing, it is essential that care is taken in weighing the choices ahead. The policy decisions in this area will have profound implications for the nation's economic recovery and for generations of future homebuyers and renters, with broad ranging social and economic consequences.

The undersigned organizations, representing a variety of stakeholders in single- and multifamily housing, believe the following principles should help guide efforts to restore and repair the nation's housing finance system:

- A stable housing sector is essential for a robust economic recovery and long-term prosperity. Housing, whether through homeownership or rental, promotes social and economic benefits that warrant it being a national policy priority.

- Private capital must be the dominant source of mortgage credit, and it must also bear the primary risk in any future housing finance system.

- Some continuing and predictable government role is necessary to promote investor confidence and ensure liquidity and stability for homeownership and rental housing.

- Changes to the mortgage finance system must be done carefully and over a reasonable transition period to ensure that a reliable mortgage finance system is in place to function effectively in the years ahead.

Private investment capital is critical for a robust and healthy mortgage marketplace, and the current government-dominated mortgage system is neither sustainable nor desirable. However, investors must be confident that they understand the risks and rules that can affect them. As policymakers move forward with Dodd-Frank Act rulemakings and similar regulatory efforts, it will be important to provide clarity and certainty to the marketplace in a manner that promotes recovery and growth. As such, the future mortgage system should seek to ensure a workable balance between sound underwriting principles, consumer protection and the need for responsible innovation and risk-taking.

As critical as it is to attract private money to the mortgage markets, an appropriate and clearly defined role for the government is essential to preserving financial stability. Government support through various insurance and guarantee mechanisms is especially important to facilitate long-term fixed-rate mortgages, affordable financing for low- and moderate-income borrowers, and financing rental housing in all parts of the country including rural areas. While the goal should be to move toward a largely private secondary market, the private and public sectors should work as partners in creating a variety of financing options to ensure the availability of safe, stable, and affordable financing.

Accomplishing all of these goals will require an on-going dialogue between policymakers and other key stakeholders, including industry and consumer groups. Our organizations stand committed to being part of this process.

American Bankers Association
American Financial Services Association
Community Mortgage Banking Project
CRE Finance Council
Housing Policy Council of the Financial Services Roundtable
Independent Community Bankers of America
Manufactured Housing Institute
Mortgage Bankers Association
Mortgage Insurance Companies of America
National Apartment Association
National Association of Home Builders
National Association of Realtors
National Council of State Housing Agencies
National Multi Housing Council
Real Estate Roundtable
Securities Industry and Financial Markets Association