U.S. Department of the Treasury

Housing Reform Plan

Pursuant to the Presidential Memorandum Issued March 27, 2019

SEPTEMBER 2019

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I. SUMMARY

Housing Finance Reform Goals

On March 27, 2019, President Donald J. Trump issued a Presidential Memorandum (the "Presidential Memorandum") directing the Secretary of the Treasury to develop a plan for administrative and legislative reforms to achieve the following housing reform goals: (i) ending the conservatorships of the Government-sponsored enterprises (each, a "GSE") upon the completion of specified reforms; (ii) facilitating competition in the housing finance market; (iii) establishing regulation of the GSEs that safeguards their safety and soundness and minimizes the risks they pose to the financial stability of the United States; and (iv) providing that the Federal Government is properly compensated for any explicit or implicit support it provides to the GSEs or the secondary housing finance market. This plan includes legislative and administrative reforms to achieve each of these goals. It has been prepared by the U.S. Department of the Treasury ("Treasury") under the direction of Secretary Steven T. Mnuchin in response to the Presidential Memorandum.

The housing finance system is in serious need of reform. The GSEs remain in conservatorship more than 10 years after the financial crisis, and they continue to be the dominant participants in the housing finance system. Although they remain critical to the functioning of that system, they are not yet subject to capital and other regulatory requirements tailored to the risks they pose to financial stability. This lack of reform has left taxpayers exposed to future bailouts. The lack of reform has also prolonged the Federal Housing Finance Agency's ("FHFA") management of the GSEs through the conservatorships, perpetuating far-reaching Government influence over the housing finance system. This plan addresses this last unfinished business of the financial crisis in a way that preserves what works in the current system, protects taxpayers, and reduces the influence of the Federal Government in the housing finance system.

Consistent with the goals set forth in the Presidential Memorandum, this plan recommends reforms to define a limited role for the Federal Government. To that end, the existing Government support of the secondary market should be explicitly defined, tailored, and paid-for, and the GSEs' conservatorships should come to an end, subject to the preconditions set forth in this plan. To avoid duplication of Government support, FHFA and the Department of Housing and Urban Development ("HUD") should develop and implement a specific understanding as to the appropriate roles and overlap between the GSEs and the Federal Housing Administration ("FHA").

This plan also recommends reforms to enhance taxpayer protections against future bailouts. Central to this objective will be ensuring that the GSEs and their successors are appropriately capitalized to remain viable as going concerns after a severe economic downturn and also to ensure that shareholders and unsecured creditors, rather than taxpayers, bear losses.

Finally, this plan endeavors to promote private sector competition in the housing finance system. A driver of the GSEs' growth has been a regulatory framework that is biased in favor of GSE-supported mortgage lending – a bias that has increased following the enactment of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"). The recommended reforms will level the playing field between the GSEs and private sector competitors by simplifying the Consumer Financial Protection Bureau's (the "CFPB") qualified mortgage ("QM") rule and eliminating the QM patch, reducing unnecessary regulatory impediments to responsible private-label securitization ("PLS"), and limiting certain GSE activities for which Government support is not necessary or justified.

While this plan includes both legislative and administrative reforms, Treasury's preference and recommendation is that Congress enact comprehensive housing finance reform legislation. Although Treasury does not believe a Government guarantee is required, Treasury would support legislation that authorizes an explicit, paid-for guarantee backed by the full faith and credit of the Federal Government that is limited to the timely payment of principal and interest on qualifying mortgage-backed securities ("MBS"). Legislation could also achieve lasting structural reform that tailors that explicit Government support of the secondary market and repeals the GSEs' congressional charters and other statutory privileges that give them a competitive advantage over private sector competition. At the same time, reform should not and need not wait on Congress. FHFA already has expansive statutory authorities to implement reforms in the absence of further Congressional action, and the housing finance system has functioned for some time, and continues to function, without an explicit full faith and credit guarantee by the Federal Government. Pending legislation, Treasury will continue to support FHFA's administrative actions to enhance the regulation of the GSEs, promote private sector competition, and satisfy the preconditions set forth in this plan for ending the GSEs' conservatorships.

A compilation of the legislative and administrative recommendations set forth in this plan, and the proposed timing for each administrative recommendation, is attached as an appendix.[1]

Legislative Reforms

The existing Government support of each GSE under its Senior Preferred Stock Purchase Agreement ("PSPA") with Treasury should be replaced with an explicit, paid-for guarantee backed by the full faith and credit of the Federal Government that is limited to the timely payment of principal and interest on qualifying MBS. The explicit Government guarantee should be available to the re-chartered GSEs and to any other FHFA-approved guarantors of MBS collateralized by eligible conventional mortgage loans or eligible multifamily mortgage loans (each GSE and competitor, a "guarantor"). These guarantors would credit enhance the mortgage collateral securing the Government-guaranteed MBS, such that the Federal Government's guarantee would stand behind significant first-loss private capital and would be triggered only in exigent circumstances.

The guarantors should be supervised and regulated by FHFA. FHFA's regulatory capital requirements should require each guarantor to be appropriately capitalized by maintaining capital sufficient to remain viable as a going concern after a severe economic downturn and also to ensure that shareholders and unsecured creditors, rather than taxpayers, bear losses. Single-

[1] The term "administrative" is used broadly to describe any reform that would not require new authorizing legislation. While Treasury consulted with FHFA and other Government agencies as required by the Presidential Memorandum, each agency will determine in its own discretion whether to adopt any particular recommendation set forth in this plan. Relatedly, each amendment to the PSPAs recommended in this plan would entail arms-length negotiations between Treasury and FHFA in its capacity as conservator for the GSEs and would remain subject to FHFA's independent discretion.

family guarantors should be required to maintain a nationwide cash window through which small lenders can sell loans for cash, and also should be prohibited from offering volume-based pricing discounts or other incentives to their lender clients.

Finally, the reformed regulatory framework should not create capital arbitrage or other regulatory incentives that bias mortgage lenders toward securitizing their loans through guarantors. In particular, similar credit risks generally should have similar credit risk capital charges across market participants.

Administrative Reforms

To ensure stability in the housing finance system pending comprehensive housing finance reform legislation, Treasury expects that it will be necessary to maintain limited and tailored Government support for the GSEs by leaving the PSPA commitment in place after the conservatorships. The Federal Government should be compensated for its continued support through the periodic commitment fee, as originally established by the PSPAs. Each GSE should be recapitalized with significant first-loss private capital so that Treasury's ongoing commitment under each PSPA could be drawn upon only in exigent circumstances. To facilitate recapitalization of the GSEs, Treasury and FHFA should consider adjusting the variable dividend (also known as the "net worth sweep") required by the terms of Treasury's senior preferred shares, as well as the other approaches set forth in this plan.

In parallel with recapitalizing the GSEs, FHFA should begin the process of ending the GSEs' conservatorships. Although applicable law does not prescribe a specific end point for the conservatorships, no conservatorship is meant to be permanent. An eventual end is also necessary to reduce the far-reaching Government influence over the housing finance system inherent in FHFA's management of the GSEs through the conservatorships.

Even after recapitalization, taxpayers will still bear some risk of a future draw on the PSPA commitment. The PSPAs should be amended to enhance Treasury's ability to mitigate the risk of a draw on the commitment after the conservatorships. Other PSPA amendments should ensure that each GSE continues to be subject to appropriate mission and safety and soundness regulation after the conservatorship, for example, to require each GSE to maintain a nationwide cash window and provide equitable secondary market access to all lenders. Still other amendments should conserve the remaining PSPA commitment by limiting future GSE activities to those that have a close nexus to the underlying rationale for Government support.

The GSEs should also continue to support affordable housing for low- and moderate-income, rural, and other similar borrowers. As described in the reform plan of HUD, and consistent with the Presidential Memorandum, FHA and the Government National Mortgage Association ("Ginnie Mae") have primary responsibility for providing housing finance support to low- and moderate-income families that cannot be fulfilled through traditional underwriting. Consistent with its charter, each GSE's role should be to perform activities relating to mortgages on housing for low- and moderate-income families involving a reasonable economic return that may be less than the return earned on other activities. As set forth in this plan and HUD's reform plan, FHFA and HUD should develop and implement a specific understanding consistent with these defined roles for the GSEs and FHA so as to avoid duplication of Government support.

Finally, continuation of limited Government support for the secondary market should not be regarded as a federal preference for mortgage lending through the GSEs. To achieve a level playing field between the GSEs and other private sector competition, the regulatory frameworks governing the GSEs and other market participants should be harmonized, and in particular, the QM patch should be replaced with a bright line safe harbor that does not rely on the GSEs' practices.

II. BACKGROUND

The Origins of Government Support

Before the Great Depression, mortgage finance in the United States was provided largely by life insurers, commercial banks, and thrifts without much financial support from the Federal Government. In 1932, with an aim to boost construction activity among other purposes, Congress created the Federal Home Loan Bank System (the "FHLBank system") and tasked it with establishing regional Federal Home Loan Banks (each, a "FHLBank") that would make advances to insurance companies and thrifts to fund their mortgage lending activities.[2] In 1934, FHA was established to offer federal insurance on long-term mortgage loans.[3] The Federal National Mortgage Association ("Fannie Mae") was then established in 1938 as a Government corporation to operate a secondary market facility that would purchase FHA loans.[4] In 1948, after the Department of Veterans Affairs' ("VA") lending program began in 1944, Fannie Mae was re-chartered under a congressional charter and authorized to also purchase mortgage loans guaranteed by VA.[5]

In 1968, Congress established a path for Fannie Mae's privatization.[6] Fannie Mae was partitioned into two entities – an entity that kept the Fannie Mae name and inherited its secondary market operations, and a newly established Government corporation in HUD, Ginnie Mae, that assumed administration of Fannie Mae's portfolio of Government-insured mortgage loans. That same legislation also authorized Ginnie Mae to provide a full faith and credit

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2 Federal Home Loan Bank Act, Pub. L. No. 72-304, 47 Stat. 725 (1932) (codified as amended at 12 U.S.C. §§ 1421-1449).

3 National Housing Act of 1934, Pub. L. No. 73-479, 48 Stat. 1246 (1934) (codified as amended at 12 U.S.C. §§ 1701-1750g).

4 The 1934 legislation establishing FHA also authorized FHA to charter national mortgage associations to purchase and sell mortgage loans. *Id.* § 301. There was initially little commercial interest in chartering one of these associations, prompting Congress to enhance this authority in 1938. *See* National Housing Act Amendments of 1938, Pub. L. No. 75-424, §§ 4-7, 52 Stat. 8 (1938). FHA then chartered the National Mortgage Association of Washington on behalf of the Reconstruction Finance Corporation, and it was soon renamed the Federal National Mortgage Association. *See* U.S. DEP'T OF THE TREASURY, FINAL REPORT ON THE RECONSTRUCTION FINANCE CORPORATION 95 (1959).

5 Amendments to National Housing Act and Servicemen's Readjustment Act, Pub. L. No. 80-864, 62 Stat. 1207 (1948).

6 Housing and Urban Development Act of 1968, Pub. L. No. 90-448, §§ 801-810, 82 Stat. 476, 536-46 (1968). Congress had again re-chartered Fannie Mae in 1954 and also begun the process of converting it into a public-private mixed ownership corporation by requiring the lenders that sold mortgage loans to Fannie Mae to purchase stock in the entity. *See* Housing Act of 1954, Pub. L. No. 83-560, § 201, 68 Stat. 590, 612-13 (1954).

guarantee on certain MBS issued by private issuers and collateralized by FHA and other Government-insured mortgage loans.

In 1970, Fannie Mae completed its conversion to a shareholder-owned corporation, and Ginnie Mae guaranteed its first MBS. That year Congress also authorized Fannie Mae for the first time to acquire mortgage loans not insured by the Federal Government (i.e., conventional mortgage loans), and Congress established the Federal Home Loan Mortgage Corporation ("Freddie Mac") as a part of the FHLBank system to provide some competition to Fannie Mae.[7]

The two GSEs initially had different business models. Both acquired conventional mortgage loans from mortgage lenders, but Fannie Mae retained those acquisitions on its balance sheet, while Freddie Mac securitized most of its acquisitions into pass-through participation certificates.[8] Fannie Mae eventually followed Freddie Mac's lead and began to securitize some of its acquisitions after the interest rate risk it retained through its portfolio holdings pushed it to the verge of insolvency following the increase in interest rates in the early 1980s.[9] In 1989, Congress authorized Freddie Mac to become, like Fannie Mae, a publicly-traded shareholder-owned corporation.[10]

The GSEs' Growing Systemic Importance

Even with the establishment of a second GSE and their new authority to acquire conventional mortgage loans, the GSEs' combined footprint remained relatively limited during the 1970s – generally less than 10% of the outstanding single-family mortgage debt.[11] (Figure 1) The GSEs did not begin to grow rapidly until the 1980s, around the time that, among other things, the banking regulators began increasing regulatory capital requirements for thrifts and other banks following the wave of thrift insolvencies and the Latin American debt crisis.[12] Because the GSEs' regulatory capital requirements generally remained well below those of thrifts and other banks, the GSEs had a competitive advantage in holding mortgage-related risks that created incentives for banks and other mortgage lenders to sell their mortgage loan originations to the GSEs.

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7 Emergency Home Finance Act of 1970, Pub. L. No. 91-351, §§ 301-310, 84 Stat. 450, 451-58 (1970).

8 FED. HOUS. FIN. AGENCY OFFICE OF INSPECTOR GENERAL, A BRIEF HISTORY OF THE HOUSING GOVERNMENT-SPONSORED ENTERPRISES 3-4 (undated).

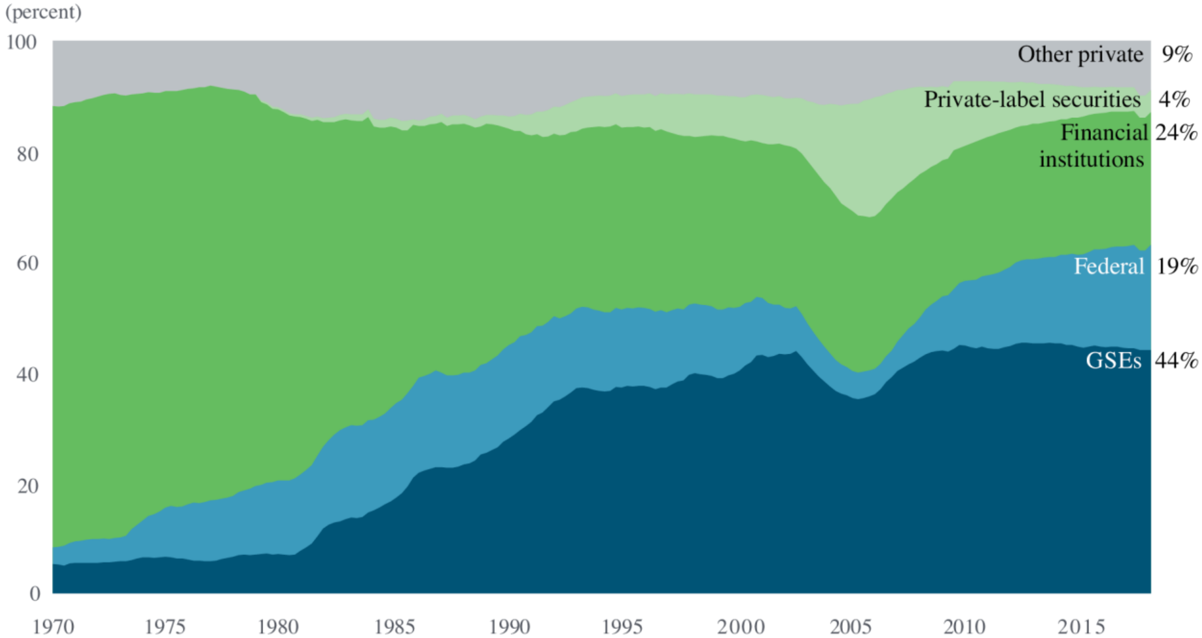
9 *Id.* at 4.

10 Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73, § 731, 103 Stat. 183, 432 (1989).

11 *See* PRESIDENT'S COMM'N ON HOUS., THE REPORT OF THE PRESIDENT'S COMMISSION ON HOUSING 160 (1982).

12 The federal banking regulators first issued a coordinated rule governing capital adequacy in 1981. *See* Capital Adequacy Guidelines, 68 FED. RES. BULL. 33 (Jan. 1, 1982) (setting forth the policy of the Board of Governors of the Federal Reserve System (the "Federal Reserve Board") and the Office of the Comptroller of the Currency (the "OCC")); Federal Deposit Insurance Corporation (the "FDIC") Statement of Policy on Capital Adequacy, 46 Fed. Reg. 62,693 (Dec. 28, 1981) (setting forth the FDIC's policy). The banking regulators then adjusted their capital requirements in 1983 after the International Lending Supervision Act directed them to set minimum levels of capital. International Lending Supervision Act, Pub. L. No. 98-181, § 908(a)(1), 97 Stat. 1278, 1280 (1983) (codified at 12 U.S.C. § 3907(a)(1)). Bank capital requirements changed again with the implementation of the 1988 Basel Accord (Basel I), which was implemented by the banking regulators over several years starting in 1989. *See, e.g.*, Risk-Based Capital Guidelines, 54 Fed. Reg. 4,186 (Jan. 27, 1989); FDIC Statement of Policy on Risk-Based Capital, 54 Fed. Reg. 11,500 (Mar. 21, 1989).

Figure 1. Single-Family Mortgage Debt Outstanding by Mortgage Holder



Note: "Other private" includes mortgage debt owned by mortgage companies, REITs, credit unions, individuals, and other entities. "Financial institutions" includes mortgage debt owned by depository institutions and insurance companies. "Federal" includes mortgage debt owned by Ginnie Mae, the FHLBanks, and other federal instrumentalities. Mortgage debt owned by a PLS trust is included in "Private-label securities," even when a GSE owned a portion of the PLS. The holder of mortgage debt is not always the bearer of the underlying credit risk. There have been no adjustments to the data, for example, to reflect financial institutions' ownership of FHA or other Government-insured loans, the GSEs' ownership of PLS, or the GSEs' credit risk transfer transactions.
Source: Federal Reserve, Mortgage Debt Outstanding.

The GSEs were able to operate with higher leverage than banks and other mortgage lenders due to the perception among investors in the GSEs' MBS and debt securities that the Federal Government would not permit either to default on its financial obligations.[13] Each GSE is unique in that its congressional charter endows the GSE with a public mission, a mechanism to obtain up to $2.25 billion in support from Treasury,[14] and exemptions from state and local taxes (except on real property).[15] The Federal Open Market Committee may direct Federal Reserve Banks to purchase GSE MBS and debt securities, a status generally reserved for Federal

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[13] This perception was contrary to several statutory and other disclaimers that there was no such guarantee by the Federal Government. 12 U.S.C. § 1455(h)(2) (directing Freddie Mac to insert language in its securities indicating such are not guaranteed by the Federal Government); *id.* § 1719(b), (d), (e) (directing Fannie Mae to include similar language); *id.* § 4501(4) (stating as a finding of Congress that "neither the enterprises nor the Banks, nor any securities or obligations issued by the enterprises or the Banks, are backed by the full faith and credit of the United States"); *id.* § 4503 (providing that the Safety and Soundness Act of 1992 "may not be construed as implying that any such [GSE or FHLBank], or any obligations or securities of such [GSE or FHLBank], are backed by the full faith and credit of the United States.").

[14] *Id.* §§ 1455(c), 1719(c).

[15] *Id.* §§ 1452(e), 1723a(c)(2).

Government debt,[16] and other laws treat each GSE's MBS and debt securities like Federal Government debt.[17]

The GSEs' congressional charters and other special legal advantages together confer on each entity a unique status as a "Government-sponsored enterprise" that has given rise to the perception of an implicit Government guarantee of each GSE. Relying on that perception, GSE investors have been willing to invest in the GSEs' debt and MBS at borrowing costs near that of debt of the Federal Government, despite the GSEs' high leverage, which has incentivized risk taking and growth at the GSEs. At the end of 1981, the GSEs owned or guaranteed around 8% of outstanding single-family mortgage debt. (Figure 1) That share grew to 25% by the end of the 1980s and to 44% by the end of 2003, where it stands today. Similarly, FHA has generally remained a significant source of Government support, hovering around 10% of mortgage originations in the early 1980s, declining during the 1990s and mid-2000s to as low as 2%, but then growing back to more than 10% of mortgage originations today.[18] The GSEs' growth supported significant profits for their shareholders (Figure 2), while the increase in GSE, FHA, and other Government-supported mortgage lending correlated with an increase in single-family mortgage debt. (Figure 3) Critically however, this significantly expanded Government role did not lead to much, if any, increase in homeownership. (Figure 3)

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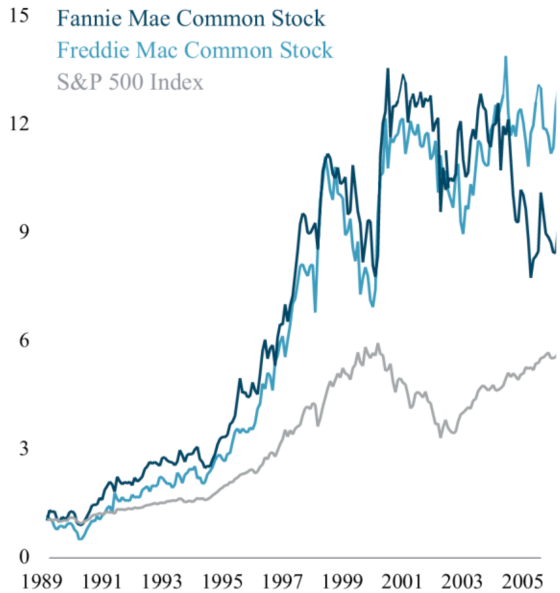
16 *Id.* § 355(2).

17 Securities issued or guaranteed by a GSE are, like government securities, exempt from the registration requirements of the Securities Act of 1933. *Id.* §§ 1455(g), 1723c. These securities are also considered government securities under the Securities and Exchange Act of 1934 and may be traded by government securities brokers. 15 U.S.C. § 78c(a)(42)-(43). GSE securities are exempt from the Trust Indenture Act of 1939 and the Investment Company Act of 1940. 15 U.S.C. §§ 77ddd, 80a-2(b). GSE MBS and debt securities are "Level 2A" assets for purposes of the liquidity risk management standards applicable to banking organizations, 12 C.F.R. § 50.20(b) (applicable to OCC-regulated banking organizations), and they have a 20% risk weight under the risk-based regulatory capital requirements applicable to banking organizations, *id*. pt. 3 app. A § 3(a)(2)(vi) (applicable to OCC-regulated banking organizations).

18 *See* Kerry D. Vandell, *FHA Restructuring Proposals: Alternatives and Implications*, 6 HOUSING POL'Y DEBATE, iss. 2, 1995, at 299, 310; U.S. DEP'T OF HOUS. & URBAN DEV., *U.S. Housing Markets Historical Data,* table 16, available at https://www.huduser.gov/Periodicals/ushmc/winter98/histdat4.html; U.S. DEP'T OF HOUS. & URBAN DEV., *FHA Single-family Market Share (2019 Q1),* table 1, available at https://www.hud.gov/sites/dfiles/Housing/documents/FHA_SF_MarketShare_2019Q1.pdf; U.S. DEP'T OF HOUS. & URBAN DEV., FHA AT 80: PREPARING FOR THE FUTURE 2 (2014); Neil Bhutta, Steven Laufer & Daniel R. Ringo, *Residential Mortgage Lending in 2016: Evidence from the Home Mortgage Disclosure Act Data*, 103 FED. RES. BULL., no. 6, 2017, at 5.

Figure 2. Cumulative Stock Returns

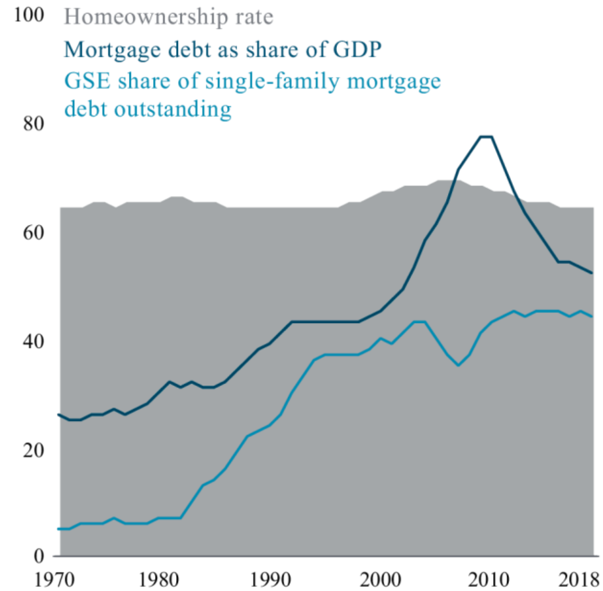
($ thousands)



Note: Cumulative return on a $1,000 investment made in August 1989, assuming reinvestment of dividends.
Source: Wharton Research Data Services, The Center for Research in Security Prices.

Figure 3. Mortgage Trends Over Time

(percent)



Note: Data are not seasonally adjusted.
Source: Federal Reserve, Bureau of Economic Analysis, Census.

A Flawed Regulatory Framework

In 1992, after reports from Treasury, the General Accounting Office[19] ("GAO"), and the Congressional Budget Office ("CBO") identified gaps in the GSEs' regulation,[20] Congress established the Office of Federal Housing Enterprise Oversight ("OFHEO") as the new safety and soundness regulator for the GSEs. However, heavy lobbying by the GSEs succeeded in

[19] In 2004, Congress changed GAO's name from the General Accounting Office to the Government Accountability Office. GAO Human Capital Reform Act of 2004, Pub. L. No. 108-271, § 8, 118 Stat. 811, 814 (2004) (codified at 31 U.S.C. § 702 note).

[20] U.S. GEN. ACCOUNTING OFFICE, GGD-90-97 1, GOVERNMENT-SPONSORED ENTERPRISES: THE GOVERNMENT'S EXPOSURE TO RISKS (1990); U.S. DEP'T OF THE TREASURY, REPORT OF THE SECRETARY OF THE TREASURY ON GOVERNMENT SPONSORED ENTERPRISES (1990); U.S. CONG. BUDGET OFFICE, CONTROLLING THE RISKS OF GOVERNMENT-SPONSORED ENTERPRISES (1991); U.S. GEN. ACCOUNTING OFFICE, GGD-91-90 1, GOVERNMENT-SPONSORED ENTERPRISES: A FRAMEWORK FOR LIMITING THE GOVERNMENT'S EXPOSURE TO RISKS (1991).

constraining the new regulator.[21] OFHEO had limited authority to set risk-based capital requirements, which were instead set pursuant to a prescriptive statutorily-specified stress scenario that contemplated only a regional, not a national, decline in housing prices.[22] OFHEO also was not authorized to place a GSE into receivership. Perhaps most notably, OFHEO's funding and staffing were limited, and it struggled under these resource constraints from its beginning.[23] Given these limitations, the establishment of OFHEO did not end the GSE reform debates, and legislators – in particular, Senator Richard Shelby (R-AL) and Representative Richard Baker (R-LA) – continued to advocate for new legislation that would establish a "world class" regulator for the GSEs. Those efforts failed in the face of vigorous opposition by market participants and the GSEs themselves.

It took the onset of the financial crisis to overcome opposition to meaningful regulation, and in 2008, Congress passed the Housing and Economic Recovery Act of 2008 ("HERA").[24] HERA established FHFA as an independent regulator funded through industry assessments. It also gave FHFA broad new authorities, including discretion to set risk-based capital requirements and the authority to place a GSE into receivership. The enhanced regulatory framework never took effect, as the GSEs were placed into conservatorship just three months after HERA's enactment.

Taxpayer Bailout of the GSEs

OFHEO was aware that the GSEs had begun to loosen their credit standards for mortgage loan acquisitions in the mid-2000s, but it did not move to curtail the increased risk taking.[25] Housing prices began to decline in 2006, mortgage defaults began to rise, and, by mid-2007, GSE default-related losses began to accelerate. In November 2007, Fannie Mae and Freddie Mac reported third-quarter losses of $1.4 billion and $2.0 billion, respectively. Losses continued to mount in early 2008, the spreads on GSE debt widened, their share prices tumbled, and the Bush Administration began to develop contingency plans. In mid-July 2008, Treasury Secretary Paulson announced that the Administration would ask for temporary authority to provide funds to the GSEs. In late July 2008, Congress passed HERA, which, besides establishing an enhanced

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21 Former OFHEO Director Falcon testified to the Financial Crisis Inquiry Commission that the "Fannie and Freddie political machine resisted any meaningful regulation using highly improper tactics." FIN. CRISIS INQUIRY COMM'N, THE FINANCIAL CRISIS INQUIRY REPORT: FINAL REPORT OF THE NATIONAL COMMISSION ON THE CAUSES OF THE FINANCIAL AND ECONOMIC CRISIS IN THE UNITED STATES 42 (2011) [hereinafter FCIC Report]. Former FHFA Director Lockhart also testified the GSEs were "allowed to be . . . so politically strong that for many years they resisted the very legislation that might have saved them." *Id.* Lockhart recalled finding in an examination an email from Fannie Mae's Chief Operating Officer Daniel Mudd to CEO Franklin Raines saying "[t]he old political reality [at Fannie] was that we always won, we took no prisoners . . . we used to . . . be able to write, or have written rules that worked for us." *Id.* at 180.

22 Housing and Community Development Act of 1992, Pub. L. No. 102-550, § 1361(a)(1), 106 Stat. 3672, 3972 (1992) (defining "stress period" for purposes of the credit risk capital charge).

23 *See* James R. Hagerty, THE FATEFUL HISTORY OF FANNIE MAE: NEW DEAL TO MORTGAGE CRISIS FALL 92-93.

24 Housing and Economic Recovery Act of 2008, Pub. L. No. 110-289, 122 Stat. 2654 (2008).

25 FCIC REPORT 180 ("OFHEO, the GSEs' regulator, noted their increasing purchases of riskier loans and securities in every examination report. But OFHEO never told the GSEs to stop. Rather, year after year, the regulator said that both companies had adequate capital, strong asset quality, prudent credit risk management, and qualified and active officers and directors.").

regulatory framework for the GSEs, gave Treasury temporary authority to purchase obligations and other securities from the GSEs.[26]

On September 6, 2008, FHFA placed the GSEs into conservatorship, and the next day Treasury exercised its temporary authority under HERA to enter into the PSPAs. Under the PSPAs, Treasury has committed to invest in each GSE to the extent necessary to maintain a positive net worth. Treasury's commitment was capped initially at $100 billion for each GSE. It was later increased to $200 billion for each GSE, and then to $200 billion plus the aggregate draws made from 2010 to 2012, less the GSE's net worth as of December 31, 2012 (i.e., to $233.7 billion and $211.8 billion for Fannie Mae and Freddie Mac, respectively). As of June 30, 2019, the remaining PSPA commitment to Fannie Mae and Freddie Mac was $113.9 billion and $140.2 billion, respectively.

In return for the PSPA commitment, Treasury received from each GSE nonvoting senior preferred shares with a liquidation preference of initially $1.0 billion, warrants to purchase 79.9% of the GSE's outstanding common stock for a nominal price, and a right to a periodic commitment fee to be determined at a later date. The liquidation preference of the senior preferred shares is increased by the amount of each draw on the PSPA commitment and, after $191.5 billion in combined draws and a $3.0 billion non-cash increase for each GSE in 2017, the GSEs' combined senior preferred liquidation preference now stands at $199.5 billion.

Treasury's senior preferred shares initially received quarterly dividends at an annual rate of 10% of the liquidation preference. Neither GSE was able to consistently generate earnings to cover the required dividend, which, by mid-2012 was nearly $19 billion each year for the GSEs together. Consequently, Treasury and FHFA amended the senior preferred shares in August 2012 to replace the fixed 10% dividend with a variable dividend that requires each GSE to pay a quarterly dividend to Treasury equal to the GSE's positive net worth above a specified capital reserve amount.[27] Through June 30, 2019, the GSEs have paid a total of $301.0 billion in dividends to Treasury.

A Decade of Conservatorship

Initially, FHFA's conservatorships focused on reducing the GSEs' losses, managing their operational and credit risks, and stabilizing the housing market. In 2012, FHFA published a Strategic Plan for Enterprise Conservatorships that set three strategic goals for conservatorship, one of which was to "[g]radually contract the [GSEs'] dominant presence in the marketplace while simplifying and shrinking their operations."[28] FHFA then directed a series of administrative reforms to further reduce risk to the taxpayers, prepare for the eventual resolution of the conservatorships, and build a secondary market infrastructure that would increase the role

[26] 12 U.S.C. §§ 1455(l), 1719(g).

[27] The August 2012 amendments also suspended the periodic commitment fee as long as the variable dividend is in place.

[28] FED. HOUS. FIN. AGENCY, A STRATEGIC PLAN FOR ENTERPRISE CONSERVATORSHIPS: THE NEXT CHAPTER IN A STORY THAT NEEDS AN ENDING 2 (2012).

of private capital while also supporting congressional reform efforts. In 2014, a revised strategic plan moved FHFA away from its effort to contract the role of the GSEs, but many of its core reform initiatives continued.[29] Key FHFA administrative reforms during the conservatorship have included:

- gradually aligning the GSEs' guarantee fees to some extent with what regulated private financial institutions would charge;

- establishing programs for credit risk transfers ("CRT"), with more than 90% of the unpaid principal balance on certain categories of newly acquired single-family mortgage loans targeted for CRT; and

- building the common securitization platform as a joint venture of the GSEs, which has facilitated the segregation of two distinct GSE roles – securitization and credit enhancement – into separate entities.

As a result of these and other efforts by FHFA, the conservatorships have in some respects reduced the risk to taxpayers, increased the role of private capital, and enhanced the secondary market infrastructure. However, the continued conservatorships have also given the Federal Government far-reaching influence over a large portion of the economy, while providing only limited transparency or accountability to taxpayers. For example, FHFA, through its management of the GSEs as conservator, has control or other influence over:

- the underwriting of single-family mortgage loans through the GSEs' underwriting criteria, which have become the industry standard even for non-GSE mortgage loans in part as a result of the exemptions afforded GSE-eligible mortgage loans from certain requirements of the CFPB's ability-to-repay rule pursuant to the QM patch;

- the pricing for single-family mortgage loans through approval of the GSEs' loan-level price adjustments and their capital framework;

- which mortgage lenders, servicers, mortgage insurers, and CRT counterparties may participate in the secondary market and how they are monitored (e.g., through FHFA's role in approving the GSEs' capital requirements for mortgage insurers); and

- the GSEs' pilot programs and entry into new lines of businesses, which are all ultimately supported by taxpayers through the PSPAs.

In light of this far-reaching Government influence inherent in the conservatorships, ending the conservatorships is a critical step toward defining a limited role for the Federal Government in the housing finance system.

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[29] FED. HOUS. FIN. AGENCY, THE 2014 STRATEGIC PLAN FOR THE CONSERVATORSHIPS OF FANNIE MAE AND FREDDIE MAC 5 (2014).

III. DEFINING A LIMITED ROLE FOR THE FEDERAL GOVERNMENT

A. CLARIFYING EXISTING GOVERNMENT SUPPORT

1. 30-year Fixed-Rate Mortgage Loan

For almost 50 years, the GSEs have fostered the widespread availability of the 30-year fixed-rate mortgage loan. After acquiring mortgage loans from lenders, the GSEs transfer the underlying prepayment and other interest rate risk on those loans to the purchasers of their MBS while retaining the credit risk on those loans through their guarantees of the MBS. This GSE-facilitated separation of credit risk and interest rate risk is meant to allocate the constituent risks to those investors that require the least compensation to bear each particular type of risk, thereby expanding the base of investor demand and reducing the cost of credit on long-term mortgage loans. Some investors in the GSEs' MBS are, for example, international and other investors that are restricted by business, regulatory, or other constraints in their ability to assume mortgage credit risk but have an appetite for the interest rate risk on the underlying mortgage loans.

It is possible that the 30-year fixed-rate mortgage loan could remain widely available and at similar prices under a market structure that does not depend on Government support. Jumbo mortgage loans remain a sizeable portion of the market and at roughly the same risk-adjusted pricing as conforming mortgage loans.[30] (Figure 4) There might also be other mechanisms for separating credit risk and interest rate risk, for example, covered bonds.[31] Alternatively, the United States could perhaps follow the lead of other countries and rely more on portfolio lending.[32]

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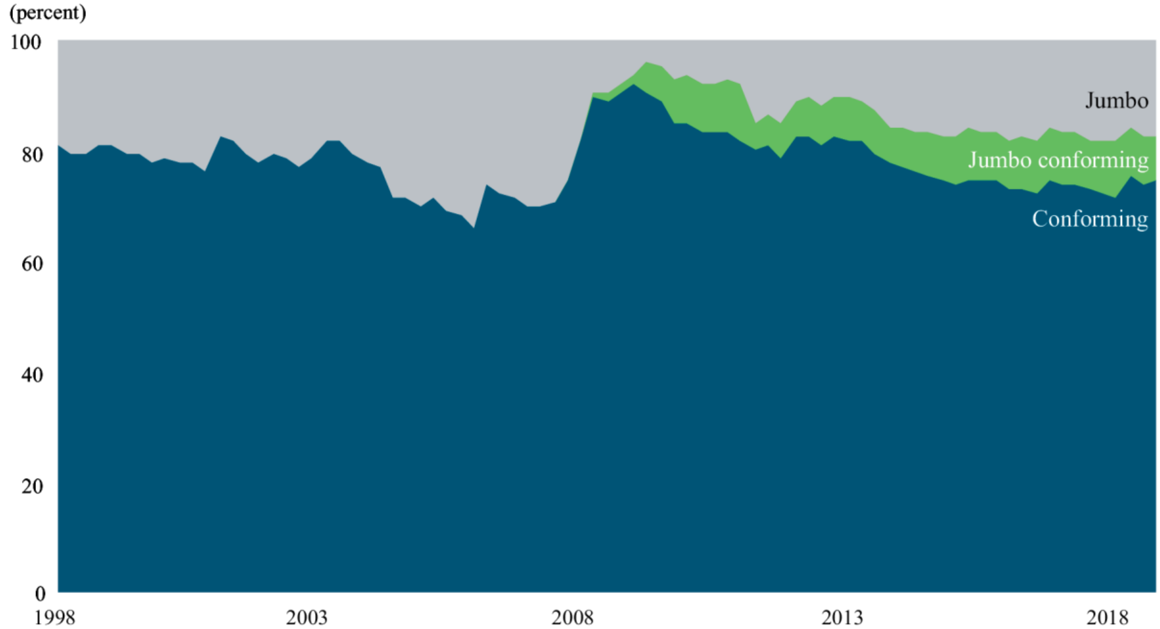
[30] On a risk-adjusted basis, jumbo mortgage loans might actually be slightly cheaper than conforming mortgage loans. *See* Lynn M. Fisher, Mike Fratantoni et. al, *Jumbo Rates Are Below Conforming Rates: When Did This Happen and Why?* (AEI Economics Working Paper 2019-16); Archana Pradhan, *Jumbo-Conforming Spread: Risk, Location, Scale Economies Affect Rate*, CORELOGIC INSIGHT BLOG (Oct. 8, 2018).

[31] In Denmark, covered bond issuances fund a widely available 30-year fixed-rate mortgage loan. *See* Jasper Berg et al., *Peas in a Pod? Comparing the U.S. and Danish Mortgage Finance Systems*, 24 FRBNY ECON. POL'Y REV. 3 (Dec. 2018); Frances Schwartzkopff, *World's Cheapest Mortgage May Be Around the Corner in Denmark*, BLOOMBERG (Mar. 21, 2019); Frances Schwartzkopff, *20-Year Mortgages Hit Zero for First Time in Danish Rate History*, BLOOMBERG (Aug. 7, 2019).

[32] *See* Michael Lea, INTERNATIONAL COMPARISON OF MORTGAGE PRODUCT OFFERINGS 34 (2010) ("Banks (commercial, savings, cooperative) in most countries dominate mortgage lending.").

Figure 4. Market Share of Jumbo Mortgage Loans



Note: "Jumbo conforming" means any loan in a high-cost area that has an original principal balance greater than the national baseline conforming loan limit and less than the high-cost area limit for that area.
Source: National Mortgage Database.

However, any proposal to fundamentally change the housing finance system should take careful account of the risks posed by the transition, particularly as housing-related activity represents a significant share of United States economic activity. Stability in the housing finance system is crucial, and generally counsels in favor of preserving what works in the current system, including the longstanding support of the 30-year fixed-rate mortgage loan.

This existing Government support should, however, be made clearer and better tailored. The PSPA commitment should be replaced with an explicit, paid-for guarantee backed by the full faith and credit of the Federal Government that is limited to the timely payment of principal and interest on qualifying MBS. The explicit Government guarantee should be available not only to the GSEs but also to any other potential guarantors that would be chartered by FHFA. Congress should authorize Ginnie Mae to extend this explicit guarantee on MBS backed by conventional mortgage loans, as it already has experience in marketing and administering MBS guarantee programs.

Pending legislation, the PSPA with each GSE should remain in place after the GSE's conservatorship. In addition to preserving what works in the housing finance system, keeping each PSPA in place would have the benefit of preserving a mechanism for recouping any funding that might be extended by Treasury to a GSE in the future while ensuring taxpayers are compensated for committing to provide that support.

Treasury recommends:

- Congress should authorize an explicit, paid-for guarantee by Ginnie Mae of qualifying MBS that are collateralized by eligible conventional mortgage loans. (legislative)

- Pending legislation, to avoid market disruption, Treasury should continue to maintain its ongoing commitment to support each GSE's single-family MBS through the PSPAs, as amended as contemplated by this plan. (administrative)

2. Underserved Renters

In addition to its single-family business, each GSE has a multifamily business that operates in the secondary market for loans secured by properties containing five or more residential units. The GSEs' role in the multifamily secondary market has historically been much smaller than in the single-family secondary markets – less than 25% of outstanding multifamily mortgage debt until the financial crisis.[33] Multifamily mortgage loans generally have shorter terms (typically 5, 7, or 10 years), balloon payments due at maturity, and restrictions on prepayments. As such, the multifamily secondary market does not depend to the same degree on the GSE-facilitated separation of credit and interest rate risk that has become a cornerstone of the single-family secondary market, and instead the policy rationale for the GSEs' multifamily businesses has tended to focus on promoting the availability of rental units that are affordable to low- and moderate-income and other historically underserved renters.

As with the single-family market, this existing Government support should be made clearer and better tailored. In the place of the PSPA commitments, Congress should authorize Ginnie Mae to provide an explicit, paid-for guarantee of the timely payment of principal and interest on any qualifying multifamily MBS of a GSE or any potential competitor guarantor that might be chartered by FHFA.

Treasury recommends:

- Congress should authorize an explicit, paid-for guarantee by Ginnie Mae of qualifying MBS that are collateralized by eligible multifamily mortgage loans. (legislative)

- Pending legislation, to preserve support for low- and moderate-income and other historically underserved renters, Treasury should continue to maintain its ongoing commitment to support each GSE's multifamily MBS through the PSPAs, as amended as contemplated by this plan. (administrative)

3. Catastrophic Backstop

In the authorizing legislation, Congress should provide that the Government guarantee of qualifying MBS could be triggered only in exigent circumstances. To ensure that significant first-loss private capital stands in front of the Government guarantee, the availability of the Government guarantee should be conditioned on a GSE or other guarantor providing specified

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[33] *See*, *infra*, at 19.

credit enhancement on the mortgage collateral securing the Government-guaranteed MBS. Each guarantor should set its own price for credit enhancing each mortgage loan, so that market discipline and price discovery would tend to mitigate the risk of capital misallocation, safety and soundness risk, and systemic risk posed by underpricing mortgage-related risks.

Similarly, pending legislation, Treasury and FHFA should ensure that Treasury's ongoing commitment under each PSPA could be drawn upon only in exigent circumstances by arranging for significant first-loss private capital to stand in front of Treasury's commitment. The GSEs' CRT already provide some of that private capital. The GSEs also should be recapitalized so that additional private capital bears first-loss risk.

Treasury recommends:

- Congress should condition the availability of the Government guarantee of qualifying MBS on a GSE or other FHFA-approved guarantor taking the first-loss position on the Government-guaranteed MBS through specified credit enhancement on the mortgage collateral securing the MBS. (legislative)

- Pending legislation, each GSE should be recapitalized so that private capital takes the first-loss position on the GSE's exposure to risk and loss. (administrative)

- FHFA and Ginnie Mae should identify and assess the operational and other issues posed by authorizing Ginnie Mae to guarantee the timely payment of principal and interest on qualifying MBS, including any necessary enhancements to existing securitization and bond administration infrastructure. (administrative)

4. Taxpayer Compensation

While guarantors will collect their own fees as compensation for taking the first-loss position on the mortgage collateral securing Government-guaranteed MBS, taxpayers should also be compensated for the residual catastrophic risk borne by the Federal Government under the Government guarantee of that MBS. Congress should authorize FHFA to set and from time to time adjust the fees for Government guarantees of qualifying MBS to ensure that the compensation paid to the Federal Government is, to the extent it might be feasible, consistent with the pricing of similar risk by private sector market participants (accounting for Government support in other market segments). In setting and adjusting the fees for Government guarantees of qualifying MBS, FHFA should consider:

- the expected fees and payments under the guarantee so as to endeavor to reduce the cost of the program, discounted on a risk-adjusted basis, to zero over a period that contemplates fluctuations in economic conditions consistent with historical experience;

- the conditions affecting the housing finance system so as to provide for reasonable stability in the fee, notwithstanding the varying risk through fluctuations in housing and economic conditions during that period; and

- any available pricing information associated with relevant private sector transactions (e.g., CRT transactions of guarantors).

The fees that the Federal Government collects should be deposited in a mortgage insurance fund that would fund any payments that might be required under the Government-guaranteed MBS. The reserve target for the fund should be set each year to ensure taxpayers are protected against losses, should be based on the amounts expected to be paid from or credited to the fund in that year and future years, and also should consider the conditions affecting the housing finance system in order to allow the fund to increase during more favorable conditions and to decrease during less favorable conditions. In the event that the fund fails to satisfy its reserve target, FHFA should have the authority to recapitalize it through industry assessments on guarantors.

Pending legislation, the Federal Government should be compensated for the continued support of the GSEs through the periodic commitment fee, as originally established by the PSPAs. The amount of the periodic commitment fee should be set and adjusted from time to time considering, among other things, the remaining PSPA commitment and the equity financing, CRT, and other loss-absorbing capacity of the GSE. In connection with setting the periodic commitment fee, Treasury and FHFA should also consider adjusting the variable dividend required by Treasury's senior preferred shares.

Treasury recommends:

- Congress should authorize FHFA to set and from time to time adjust fees for Government guarantees of qualifying MBS so that the compensation paid to the Federal Government is, to the extent it might be feasible, consistent with the pricing of similar risk by private sector market participants (accounting for Government support in other market segments). (legislative)

- Pending legislation, each PSPA should be amended to compensate the Federal Government for the continued support of the GSEs through an appropriately priced periodic commitment fee. (administrative)

B. Support of Single-Family Mortgage Lending

Guarantors' activities should be restricted by statute in order to facilitate FHFA's regulation of the guarantors and to limit the exposure of the mortgage insurance fund. Specifically, guarantors should be monoline businesses limited to the business of securitizing Government-guaranteed MBS, which could be statutorily defined to include credit enhancing the mortgage collateral securing Government-guaranteed MBS and ancillary activities such as operating a cash window, loss mitigation on mortgage loans, and holding and disposing of property acquired in connection with collecting on mortgage loans. These activity restrictions need not necessarily apply to non-controlled affiliates of the guarantors, subject to appropriate arms-length and other restrictions on affiliate transactions.

In addition to supporting access to the 30-year fixed-rate mortgage loan, the GSEs also acquire 15-year and 20-year fixed-rate mortgage loans and adjustable-rate mortgages ("ARMs"), as well as conventional mortgage loans made for different loan purposes, such as cash-out refinancings and investor and vacation home loans. (Figure 5) Shorter-term fixed-rate mortgage loans and ARMs do not depend to the same extent, if at all, on the GSE-facilitated separation of credit and interest rate risk, and the GSEs' current role in the market for cash-out refinancings, investor loans, and vacation home loans might not align with the core purpose of Government support for the secondary market.

Figure 5. Acquisition Share

	2014	2015	2016	2017	2018
Product Type					
30-Year Fixed	74%	75%	76%	79%	86%
15-Year Fixed	17%	17%	17%	13%	9%
Fixed Other Terms	5%	5%	6%	5%	4%
ARM	5%	3%	2%	3%	1%
Loan Purpose					
Purchase	52%	45%	44%	57%	67%
Rate-Term Refi	32%	36%	35%	22%	13%
Cash-Out Refi	16%	20%	20%	22%	20%
LTV Ratio					
<=70 Percent	26%	31%	33%	29%	26%
70.1 - 80 Percent	39%	39%	38%	39%	38%
80.1 - 90 Percent	15%	15%	13%	14%	14%
> 90 Percent	19%	16%	15%	19%	23%
Credit Score					
>= 720	71%	74%	75%	71%	71%
660 - 719	23%	21%	21%	24%	24%
< 660	6%	5%	4%	5%	5%
Risk Layering					
Jumbo Conforming	8%	9%	10%	9%	8%
Condo/Cooperative	9%	9%	9%	9%	9%
Investment Properties	8%	7%	6%	7%	6%
Second/Vacation Properties	4%	4%	3%	4%	4%

Source: FHFA.

When the GSEs were first authorized to acquire conventional mortgage loans in 1970, the GSEs were required to set and adjust the limit on the original principal balance of their acquisitions, known as the conforming loan limit, at an amount "comparable" to FHA's loan limit, which was then $33,000.[34] According to the Senate committee report, the "purpose of these [conforming loan] limits is to reduce the risk to the [GSEs] and to encourage the flow of mortgage credit to low and moderate priced housing."[35] In 1980, Congress established a new method that provided for an annual adjustment to the initial conforming loan limit ($93,750) equal to the percentage increase in the national average single-family house price as determined by a monthly survey of major lenders conducted by the Federal Home Loan Bank Board.[36] By 2008, these adjustments had increased the conforming loan limit to $417,000. In 2008, HERA amended the GSEs'

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34 Emergency Home Finance Act of 1970, Pub. L. No. 91-351, §§ 201(a), 305(a)(3), 84 Stat. 450, 451, 455 (1970). There were no conforming loan limits before 1970 because Fannie Mae generally was limited to acquiring FHA and VA loans.

35 S. REP. NO. 91-761, at 9 (1970).

36 The conforming loan limit had been previously amended in 1974 to be based on the statutory mortgage limit for savings and loan associations, Housing and Community Development Act of 1974, Pub. L. No. 93-383, §§ 805(b)(4), 806(f), 88 Stat. 633, 726-27, which was intended to "permit [each GSE] to serve much the same housing market in terms of constant dollars as it was [in 1970]," H.R. REP. NO. 93-1114, at 29 (1974). The savings and loan associations' statutory limit was repealed in 1980, necessitating the new loan limit methodology.

charters to provide on a permanent basis for separate conforming loan limits for high-cost areas.[37] After the 1980 and 2008 changes, the conforming loan limits now in effect do not necessarily focus the GSEs' support on low- and moderate-priced housing in some areas.

While the GSEs' charters permit acquisitions of higher balance mortgage loans and do not limit the range of acquired loan products and loan purposes, it is also the case that the GSEs' charters were granted when the Federal Government expressly denied any implicit or other support of the GSEs.[38] With the PSPAs, Treasury has now committed to support each GSE, and that change warrants FHFA and Treasury revisiting which single-family activities of each GSE should continue to benefit from Treasury's support. Similarly, Treasury's commitment under the PSPAs is fixed in amount by its terms, and Treasury and FHFA should consider whether to conserve that finite commitment by limiting the support of future GSE acquisitions to specified loan products, purposes, or amounts. Given these considerations, Treasury and FHFA should solicit information on whether to tailor PSPA support for cash-out refinancings, investor loans, vacation home loans, higher principal balance loans, or other subsets of GSE-acquired mortgage loans, potentially exploring legal or other mechanisms for tailoring or otherwise limiting PSPA support to specified loan products, purposes, or amounts or perhaps more directly restricting some of these GSE activities.

Related to this, even with the administrative reforms set forth in this report, the GSEs will still have the significant competitive advantages conferred by their congressional charters and other statutory privileges, as well as the benefit of the support from Treasury's PSPA commitment. FHFA should strictly construe the permissible activities authorized by each GSE's charter so that the GSEs' remaining competitive advantages do not crowd out private capital in ancillary markets – for example, the market for loans to non-bank servicers.[39] To that end, FHFA should specify a policy and process for the approval of new pilot programs and other new activities or products, and that process should ensure that each new program, activity, or product is clearly authorized by the GSE's charter and would not compete with products or services already provided by the private sector, while also contemplating the solicitation of public input on these issues and any related considerations.

Treasury recommends:

- Congress should restrict the permissible activities of guarantors to the business of securitizing Government-guaranteed MBS. (legislative)

- Pending legislation, FHFA should assess whether each of the current products, services, and other single-family activities of each GSE is consistent with its statutory mission and should continue to benefit from support under Treasury's PSPA commitment (with

[37] Housing and Economic Recovery Act of 2008, Pub. L. No. 110-289, § 1124, 122 Stat. 2654 (2008).

[38] *See* 12 U.S.C. §§ 1455(h)(2), 1719(b), 4501(4), 4503. Each GSE does have a statutory mechanism to obtain up to $2.25 billion in support from Treasury in certain circumstances. *Id.* §§ 1455(c), 1719(c).

[39] *Oversight of the Federal Housing Finance Agency's Role as Conservator and Regulator of the Government Sponsored Enterprises: Hearing Before the H. Comm. on Fin. Servs.*, 115th Cong. 143 (2018) (statement of Melvin L. Watt, Director, FHFA) ("Freddie Mac's pilot program seeks to stabilize its non-bank counterparties that service Freddie Mac-guaranteed loans. The pilot is approved for $1 billion of MSR financing to Freddie Mac non-bank counterparties who service loans guaranteed by Freddie Mac.").

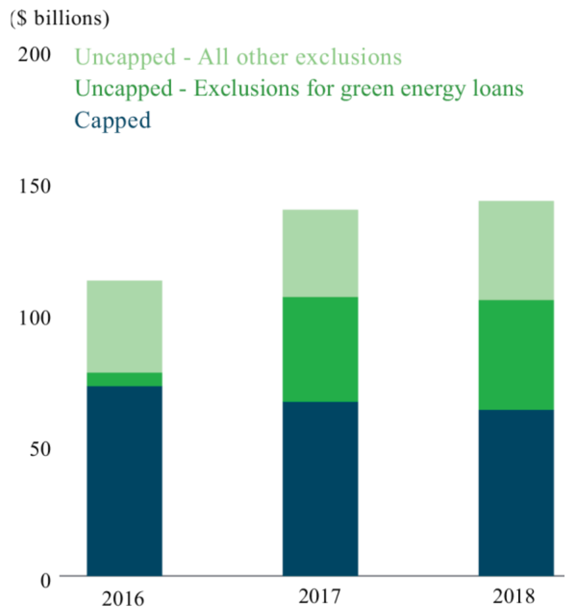
appropriate amendments to the PSPA), and in particular, FHFA should solicit information on whether to tailor support for cash-out refinancings, investor loans, vacation home loans, higher principal balance loans, or other subsets of GSE-acquired mortgage loans. (administrative)

- FHFA should implement a policy and process for approval of the GSEs' new pilot programs and other new activities or products, with that process soliciting public input. (administrative)

C. Support of Multifamily Mortgage Lending

As discussed above, the policy rationale for the GSEs' multifamily businesses has tended to focus on promoting the availability of rental units that are affordable to low- and moderate-income and other historically underserved renters. Consistent with this rationale, FHFA has taken steps to manage the footprint of the GSEs' multifamily businesses since shortly after the conservatorships began. In 2012, FHFA required each GSE to assess the viability of operating its multifamily business without a Government guarantee.[40] Each GSE reported that its multifamily business could be viable without a Government guarantee, albeit with meaningful changes. FHFA's conservatorship strategic plan for 2013 required each GSE to decrease its multifamily acquisitions to 10% below 2012 amounts.[41] In August 2013, FHFA sought public input on strategies for reducing the GSEs' presence in the multifamily housing market,[42] and in December 2015, FHFA announced that it would impose caps on each GSE's annual multifamily loan acquisitions.[43]

Figure 6. Multifamily Acquisitions, Capped and Uncapped



Source: FHFA, 2016-2018 Scorecard Progress Reports.

FHFA adjusts these caps each year, with the 2019 caps limiting each GSE to $35 billion in multifamily acquisitions.[44] The caps are subject to broad exemptions, for example, for certain

[40] Fed. Hous. Fin. Agency, 2012 Conservatorship Scorecard § 2 (2012).

[41] Fed. Hous. Fin. Agency, Conservatorship Strategic Plan: Performance Goals for 2013 § 2 (2013).

[42] Fed. Hous. Fin. Agency, "FHFA Seeks Public Input on Reducing Fannie Mae and Freddie Mac Multifamily Businesses" (Aug. 9, 2013).

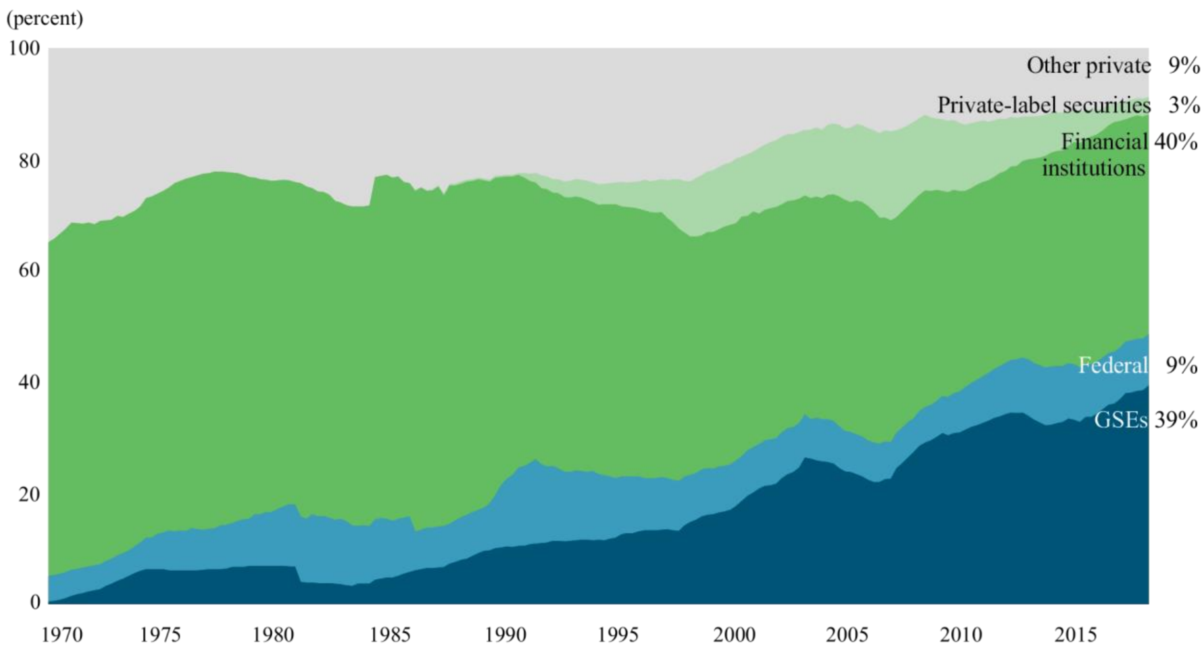
[43] Fed. Hous. Fin. Agency, 2016 Scorecard for Fannie Mae, Freddie Mac, and Common Securitization Solutions 4 (2015).

[44] Fed. Hous. Fin. Agency, "FHFA Announces 2019 Multifamily Lending Caps for Fannie Mae and Freddie Mac" (Nov. 6, 2018).

affordable housing loans and for loans to finance energy and water efficiency improvements.[45] Most of the GSEs' multifamily acquisitions now fall within one of these exemptions, and indeed much of the recent growth in the GSEs' multifamily acquisitions has been driven by the exemption for green energy loans.[46] (Figure 6)

In part because of these broad exemptions, the caps have not been effective in limiting the GSEs' multifamily footprint. The GSEs have grown from owning or guaranteeing 25% of outstanding multifamily debt in early 2008 to almost 40% today. (Figure 7) That share could climb, as the GSEs have acquired approximately 50% of recent multifamily originations.[47]

Figure 7. Multifamily Mortgage Debt Outstanding by Mortgage Holder



Note: "Other private" includes mortgage debt owned by mortgage companies, REITs, credit unions, individuals, and other entities. "Financial institutions" includes mortgage debt owned by depository institutions and insurance companies. "Federal" includes mortgage debt owned by Ginnie Mae, the FHLBanks, and other federal instrumentalities. Mortgage debt owned by a PLS trust is included in "Private-label securities," even when a GSE owned a portion of the PLS. The holder of mortgage debt is not always the bearer of the underlying credit risk. There have been no adjustments to the data, for example, to reflect financial institutions' ownership of FHA or other Government-insured loans, the GSEs' ownership of PLS, or the GSEs' credit risk transfer transactions.
Source: Federal Reserve, Mortgage Debt Outstanding.

In light of the rapid recent growth of the GSEs' multifamily businesses, Congress and FHFA should revisit the framework for ensuring that the Federal Government's support of the multifamily secondary market is tailored to an affordability mission. While a closer mission nexus would help limit the size of the Government-supported multifamily secondary market, still the funding advantage conferred by an explicit guarantee could risk crowding out the already existing private sector funding of multifamily loans. In the place of the existing cap on the

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45 *See* FED. HOUS. FIN. AGENCY, 2019 SCORECARD FOR FANNIE MAE, FREDDIE MAC, AND COMMON SECURITIZATION SOLUTIONS 7-10 (2018).

46 FED. HOUS. FIN. AGENCY OFFICE OF INSPECTOR GEN., FANNIE MAE AND FREDDIE MAC IN THE MULTIFAMILY MARKET 8 (2017).

47 *See* Freddie Mac, MULTIFAMILY SECURITIZATION OVERVIEW (as of March 31, 2019) 19, available at https://mf.freddiemac.com/docs/mf_securitization_investor-presentation.pdf.

GSEs' annual acquisitions, a shift to a cap that is based on, among other things, the multifamily guarantors' share of outstanding multifamily debt might be better calibrated to ensure that private sector sources of capital are not crowded out, while also permitting more acquisitions during periods of high refinancings.

Pending legislation, Treasury and FHFA should consider amending the PSPAs to focus Government support on the GSEs' current role in supporting affordable rental units for low- and moderate-income and other historically underserved renters. FHFA should revisit FHFA's efforts in 2012 and 2013 to restrict the GSEs' multifamily footprint. Specifically, the exemptions from the cap merit a particularly close look. For example, exempt loans for energy efficient multifamily projects have been a significant driver of growth in the GSEs' multifamily business, while lacking an obvious nexus to an affordability mission. FHFA also should consider requiring that a specified portion of the rental units that are in properties financed by GSE-acquired multifamily loans remain affordable to low- and moderate-income and other historically underserved renters even after origination. FHFA might also consider requiring the GSEs to ensure that those units are on an ongoing basis actually inhabited by these renters.

Treasury recommends:

- Congress should implement a framework to limit the aggregate footprint of multifamily guarantors. (legislative)

- Congress should limit the multifamily mortgage loans that are eligible to secure Government-guaranteed multifamily MBS to ensure a close nexus to a specified affordability mission. (legislative)

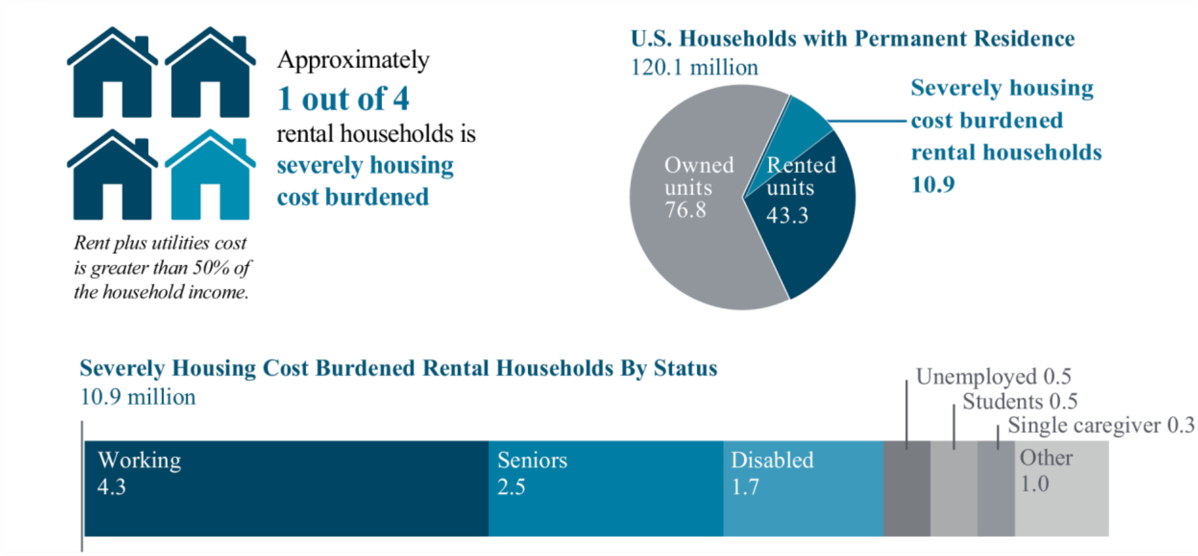
- Pending legislation, Treasury and FHFA should consider amending each PSPA to limit support of each GSE's multifamily business to its underlying affordability mission, including potentially through a revised framework for capping each GSE's multifamily footprint. (administrative)

D. Additional Support for Affordable Housing

1. *Barriers to Housing Development*

Access to affordable housing is far too difficult for many Americans, with rising housing costs forcing many families to dedicate larger shares of their income to housing. (Figure 8) A driver of the rise in housing costs has been a lack of housing supply caused in part by regulatory barriers, including overly restrictive zoning and growth management controls, rent controls, and cumbersome building and rehabilitation codes, among a wide variety of other impediments. Low- and middle-income families are often hit hardest by these barriers to housing development. On June 25, 2019, President Trump signed an Executive Order Establishing a White House Council on Eliminating Regulatory Barriers to Affordable Housing that will work, among other objectives, to identify practices and strategies that reduce regulatory and other barriers that raise the cost of housing development, and Treasury is committed to supporting the Council and implementing the policy set forth in the President's Executive Order.

Figure 8. U.S. Rental Households



Note: "Seniors" means the householder or spouse (if applicable) is at least 62 years of age. "Disabled" means the householder and spouse (if applicable) is younger than 62 and at least one is disabled. "Unemployed" means the householder and spouse (if applicable) are younger than 62, not disabled, and both are unemployed. "Working" means the householder and spouse (if applicable) are younger than 62, not disabled, and at least one is employed. "Students" means the householder and spouse (if applicable) are younger than 62, not disabled, not in the labor force, and both are enrolled in school. "Single caregiver" means the householder is not married with a spouse present, younger than 62, not disabled, not in the labor force, not enrolled in school, and at least one other member of the household is disabled or under 7 years of age. "Other" is the balance of households that are not in the labor force.
Sources: 2017 ACS PUMS tabulation, U.S. Census Bureau Census Reporter, Missouri Census Data Center, OFR analysis.

Related to this, some states and other jurisdictions have explored expanding the scope of their rent control laws.[48] These laws interfere with the functioning of local housing markets, tending to decrease the supply and quality of the available housing. Scarce Government subsidies should not be used to offset the adverse effects of these laws. By limiting the rental income on multifamily properties, these laws also increase the credit and other risks associated with GSE-acquired loans that are secured by multifamily properties in rent-controlled jurisdictions. In light of these developments, FHFA should revisit the GSEs' underwriting criteria for acquisitions of multifamily loans secured by properties in rent-controlled jurisdictions, perhaps prescribing lower loan-to-value ratio ("LTV") limits or other underwriting restrictions on these acquisitions.

Treasury recommends:

- FHFA should revisit the GSEs' underwriting criteria for acquisitions of multifamily loans secured by properties in jurisdictions that adopt rent-control laws or other undue impediments to housing development. (administrative)

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[48] New York recently expanded its rent control law, and Oregon recently enacted a rent control law. *See* Housing Stability and Tenant Protection Act of 2019 (S. 6458); Oregon Senate Bill 608.

2. *Affordable Housing Goals*

In addition to their support of the widespread availability of the 30-year fixed-rate mortgage loan and multifamily housing for low- and moderate-income and other renters, the GSEs also are subject to other statutory mandates to support access to affordable housing.

- Each GSE's charter authorizes it to "promote access to mortgage credit throughout the Nation (including central cities, rural areas, and underserved areas)" and to perform "activities relating to mortgages on housing for low- and moderate-income families involving a reasonable economic return that may be less than the return earned on other activities."[49]

- FHFA is authorized to set affordable housing goals for the GSEs' acquisitions of mortgage loans to low- and moderate-income borrowers and mortgage loans to borrowers in low-income areas.[50] These goals are generally set as a share of the GSEs' acquisitions.

- Each GSE is required to "provide leadership to the market in developing loan products and flexible underwriting guidelines to facilitate a secondary market for mortgages for very low-, low-, and moderate-income families" in three specified markets – manufactured housing, affordable housing preservation, and rural markets.[51] FHFA's rule implementing this "duty to serve" requires each GSE to develop a plan that describes the specific activities and objectives it will undertake in each of the three specified markets.[52]

- Each GSE must set aside 4.2 basis points of the unpaid principal balance of new business purchases to be allocated to the Housing Trust Fund and Capital Magnet Fund.[53]

These statutory mandates should be reformed to more effectively target support for affordable housing. In particular, the GSEs' statutory affordable housing goals should be replaced with a more efficient, transparent, and accountable mechanism for delivering tailored support. The goals were a contributing factor to the GSEs' risk taking and losses in the lead up to the financial

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[49] 12 U.S.C. §§ 1451, 1716 note.
[50] *Id.* §§ 4562-63.
[51] *Id.* § 4565.
[52] 12 C.F.R. §§ 1282.31-1282.41.
[53] 12 U.S.C. § 4567(a). The Housing Trust Fund is administered by HUD and provides grants to the States "to increase and preserve the supply of rental housing for extremely low- and very low-income families, including homeless families" and "to increase homeownership for extremely low- and very low-income families." *Id.* § 4568(a)(1). The Capital Magnet Fund is administered by Treasury and funds a competitive grant program to increase investment in "the development, preservation, rehabilitation, or purchase of affordable housing for primarily extremely low-, very low-, and low-income families" and "economic development activities or community service facilities . . . which in conjunction with affordable housing activities implement a concerted strategy to stabilize or revitalize a low-income area or underserved rural area." *Id.* § 4569(c).

crisis.[54] Even more importantly, the framework for setting the goals suffers from a lack of transparency and accountability to taxpayers. There is limited publicly available information as to the costs of the various possible goal targets in terms of increased credit losses and forgone guarantee fees or as to the social benefits, whether in terms of lower borrowing costs for, or additional mortgage loans made to, low- and moderate-income borrowers and borrowers in low-income areas. Accountability is also lacking, as FHFA has wide discretion to set the targets.

An alternative approach would be to collect a periodic assessment from guarantors that Congress would make available through an appropriation to administer on-budget affordable housing programs. These programs could support affordable rental housing as well as down-payment assistance, interest rate buy-downs, and other forms of support for first-time homebuyers and low- and moderate-income, rural, and other historically underserved borrowers, with perhaps some or all of these programs administered by HUD.

Pending legislation, FHFA should focus on increasing the efficiency of the means employed by the GSEs to achieve the statutory affordable housing goals. The GSEs currently rely to a significant degree on the underpricing of their guarantee fees on mortgage loans to certain borrowers to achieve these goals and other mission-related objectives. This mission-related cross-subsidization in large part occurs where the GSEs collect above-cost guarantee fees from lower credit risk borrowers to subsidize below-cost guarantee fees collected from higher credit risk borrowers. Credit risk is not necessarily a good proxy for borrower income, with the implication that alternatives to credit risk-based cross-subsidy could provide more efficient mechanisms for the GSEs to deliver tailored support to low- and moderate-income borrowers and achieve their statutory affordable housing goals.

Treasury recommends:

- Congress should replace the GSEs' statutory affordable housing goals with a more efficient, transparent, and accountable mechanism for delivering tailored support to first-time homebuyers and low- and moderate-income, rural, and other historically underserved borrowers, with a portion of the associated funding potentially transferred to HUD to expand its affordable housing activities. (legislative)

- Pending legislation, FHFA should consider more efficient mechanisms for the GSEs to achieve the statutory affordable housing goals. (administrative)

[54] FCIC REPORT at 323 ("Affordable housing goals imposed by [HUD] did contribute marginally to these practices."); FCIC Commission, Telephonic Interview with James B. Lockhart, III former Director of OFHEO (Mar. 19, 2010) ("But both CEOs were majorly concerned about not meeting their goals. It was a major issue for both companies."); *see generally* FCIC REPORT at 495-522 (dissenting statement of Peter J. Wallison). "From 1997 to 2000, 42% of GSE purchases were required to meet goals for low-and moderate-income borrowers. In 2001, the goal was raised to 50%." *Id.* at 183. "In 2004 HUD announced that starting in 2005, 52% of the GSEs' purchases would need to satisfy the low- and moderate-income goals. The targets would reach 55% in 2007 and 56% in 2008." *Id.* "By 2005, Fannie and Freddie were stretching to meet the higher goals . . . ." *Id.* at 184.

3. *Duplication of Support*

The Presidential Memorandum directs Treasury to "defin[e] the GSEs' role in promoting affordable housing without duplicating support provided by the [FHA] or other Federal programs." Consistent with the Presidential Memorandum, FHA and Ginnie Mae have primary responsibility for providing housing finance support to low- and moderate-income families that cannot be fulfilled through traditional underwriting. In furtherance of that policy, FHA may set its premiums below the amounts that would be required by private sources of capital.[55]

While there inevitably will be some incidental overlap between the GSEs and FHA's support for affordable housing, the duplication of support for affordable housing has unnecessarily increased with the conservatorships, particularly in the last several years. For example, the GSEs have increased their acquisitions of higher LTV and higher debt-to-income ratio ("DTI") loans since 2014,[56] while FHA has increased its originations of cash-out, conventional-to-FHA, and other refinancing loans, while also supporting repeat borrowers of FHA loans.[57]

Consistent with its charter, each GSE's role should be to perform "activities relating to mortgages on housing for low- and moderate-income families involving a reasonable economic return that may be less than the return earned on other activities."[58] Ending the conservatorships will be important to reinstating market discipline so as to ensure that the GSEs are focused on mortgage loans that entail a reasonable economic return. After the conservatorships end, FHFA should continue to consider the risk of duplicating support when setting the GSEs' statutory affordable housing goals or otherwise exercising its affordability-related regulatory authorities, and FHFA, FHA, and Ginnie Mae should regularly coordinate to identify and mitigate areas of duplication of Government support for affordable housing.

Treasury recommends:

- FHFA and HUD should develop and implement a specific understanding as to the appropriate roles and overlap between the GSEs and FHA, for example, with respect to the GSEs' acquisitions of high LTV and high DTI loans and FHA's underwriting of cash-out, conventional-to-FHA, and other refinancing loans and loans to repeat FHA borrowers. (administrative)

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55 Under the Federal Credit Reform Act ("FCRA"), the budgetary cost of a federal credit program is determined using a discount rate equal to the Federal Government's borrowing cost for a similar term to maturity, *i.e.*, not a market risk-adjusted discount rate. That generally enables FHA to price mortgage-related risks at amounts lower on average than private sector entities would. *See* U.S. CONG. BUDGET OFFICE, FAIR-VALUE ACCOUNTING FOR FEDERAL CREDIT PROGRAMS 1 (The FCRA-based cost method "makes the reported cost of federal direct loans and loan guarantees in the federal budget lower than the cost that private institutions would assign to similar credit assistance based on market prices.").

56 *See generally*, infra, at 33.

57 The total number of FHA endorsements with cash-out refinance mortgages increased 250.47% since 2013, from 43,052 in fiscal year 2013 to 150,883 in fiscal year 2018. Mortgagee Letter 2019-11 (Aug. 1, 2019). FHA moved in August 2019 to reduce some of this duplication of support by lowering its maximum LTV for cash-out refinancings from 85% to 80%, in line with the GSEs' limit. *Id.*

58 12 U.S.C. §§ 1451 note, 1716.

E. ENDING THE CONSERVATORSHIPS

It is, after 11 years, time to bring the conservatorships to an end. Although HERA does not prescribe a specific end point for the conservatorships, no conservatorship is meant to be permanent. Through its management of the GSEs, FHFA as conservator has far-reaching influence over who gets a mortgage loan, the pricing and terms of the loan, how it is originated, how it is serviced, what happens upon a borrower default, and which market participants may participate in the housing finance system. Ending the conservatorships is a critical step to reducing that Government influence.

1. Preconditions for Ending the Conservatorships

The guiding principle for ending the conservatorships should be that each GSE should remain in conservatorship until FHFA determines that that particular GSE can operate safely and soundly and without posing an undue systemic risk. The specific preconditions for FHFA considering a particular GSE's exit from conservatorship should include, at a minimum, that:

- FHFA has prescribed regulatory capital requirements for both GSEs;
- FHFA has approved the GSE's capital restoration plan, and the GSE has retained or raised sufficient capital and other loss-absorbing capacity to operate in a safe and sound manner;
- The PSPA between Treasury and the GSE has been amended to: (i) require the GSE to fully compensate the Federal Government in the form of an ongoing payment for the ongoing support provided to the GSE under the PSPA; (ii) focus the GSE's activities on its core statutory mission and otherwise tailor Government support to the underlying rationale for that support; (iii) further limit the size of the retained mortgage portfolio of the GSE; (iv) subject the GSE to heightened prudential requirements and safety and soundness standards, including increased capital requirements, designed to prevent a future taxpayer bailout and minimize risks to financial stability; and (v) ensure that the risk posed by the GSE's activities is calibrated to the amount of the remaining commitment under the PSPA;
- Appropriate provision has been made to ensure there is no disruption to the market for the GSE's MBS, including its previously issued MBS;
- FHFA, after consulting with the Financial Stability Oversight Council ("FSOC"), has determined that the heightened prudential requirements incorporated into the amended PSPAs are, together with the requirements and restrictions imposed by FHFA in its capacity as regulator, appropriate to minimize risks to financial stability; and
- Any other conditions that FHFA, in its discretion, determines are necessary to ensure that the GSE would operate in a safe and sound manner after the conservatorship, including as

to the GSE's compliance with FHFA's directives or other requirements and also as to the build out of FHFA's supervisory function.[59]

Treasury recommends:

- Pending legislation, FHFA should exercise its authority as conservator to begin the process to end each GSE's conservatorship in a manner consistent with the preconditions set forth in this plan. (administrative)

2. Recapitalizing the GSEs

As described above, each GSE should remain in conservatorship until it has retained or raised sufficient capital or other loss-absorbing capacity to operate in a safe and sound manner. Potential approaches to recapitalizing a GSE could entail one or more of the following, among other options:

- Eliminating all or a portion of the liquidation preference of Treasury's senior preferred shares or exchanging all or a portion of that interest for common stock or other interests in the GSE;

- Adjusting the variable dividend on Treasury's senior preferred shares so as to allow the GSE to retain earnings in excess of the $3 billion capital reserve currently permitted;

- Issuing shares of common or preferred stock, and perhaps also convertible debt or other loss-absorbing instruments, through private or public offerings, perhaps in connection with the exercise of Treasury's warrants for 79.9% of the GSE's common stock;

- Negotiating exchange offers for one or more classes of the GSE's existing junior preferred stock; and

- Placing the GSE in receivership, to the extent permitted by law, to facilitate a restructuring of the capital structure.

Each of these options poses a host of complex financial and legal considerations that will merit careful consideration as Treasury and FHFA continue their effort, already underway, to identify and assess these and other strategic options.

Treasury recommends:

- Treasury and FHFA should develop a recapitalization plan for each GSE after identifying and assessing the full range of strategic options. (administrative)

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[59] FHFA has relied primarily on its conservatorship authorities to oversee the safety and soundness of the GSEs over the last 11 years. With the end of the conservatorship, FHFA will instead rely on its supervisory and regulatory authorities, which include authorities to conduct examinations of the GSEs. FHFA could determine that it should specify conditions with respect to the hiring and training of examiners or other aspects of the buildout of its supervisory function.

- Pending that recapitalization plan, and as an interim step toward the eventual PSPA amendment contemplated by this plan, Treasury and FHFA should consider permitting each GSE to retain earnings in excess of the $3 billion capital reserve currently permitted, with appropriate compensation to Treasury for any deferred or forgone dividends. (administrative)

IV. PROTECTING TAXPAYERS AGAINST BAILOUTS

A. CAPITAL AND LIQUIDITY REQUIREMENTS

1. Capital Requirements

Deficiencies in the GSEs' regulatory capital framework were a root cause of the GSEs' growth, risk taking, and near insolvency. As described in the Background section, the GSEs' regulatory capital requirements were too low relative to their risks, which undermined market discipline and gave the GSEs a competitive advantage over banks and other market participants. In July 2018, the previous FHFA Director proposed a new framework to address these issues by increasing the GSEs' regulatory capital requirements.[60] The proposed rule would assign specific credit risk capital charges to different mortgage loans. It also would provide for separate capital requirements for market risk and operational risk, as well as a going concern buffer.

Given the GSEs and their potential successor guarantors' central role in the housing finance system and the potential taxpayer exposure with respect to PSPA-backed or Government-guaranteed MBS, each GSE or guarantor should be subject to FHFA-prescribed regulatory capital requirements that require it to be appropriately capitalized by maintaining capital sufficient to remain viable as a going concern after a severe economic downturn and also to ensure that shareholders and unsecured creditors, rather than taxpayers, bear losses. To foster a level playing field with private sector competition, similar credit risks generally should have similar credit risk capital charges across market participants. To manage the limitations of risk-based capital requirements, the regulatory capital framework also should contemplate a simple, transparent, non-risk-based leverage restriction that is calibrated to act as a credible supplementary measure to the risk-based capital requirements.

[60] Enterprise Capital Requirements, 83 Fed. Reg. 33,312 (proposed Jul. 17, 2018). FHFA has suspended the GSEs' existing capital requirements since the beginning of the conservatorship, but according to the proposed rule, "while the [GSEs] are in conservatorship, FHFA will expect Fannie Mae and Freddie Mac to use assumptions about capital described in the rule's risk-based capital requirements in making pricing and other business decisions." *Id.*

It is unclear based on publicly available information whether FHFA's proposed capital rule satisfies these principles.[61] The new FHFA Director should continue FHFA's effort already underway to re-assess the adequacy of the proposed capital rule. In addition, to ensure that the GSEs' creditors and counterparties will have the requisite confidence in the final rule, FHFA should disclose additional detail with respect to the calibration of the risk-based capital requirements, including the underlying models, data, and assumptions.

On a related note, certain statutory definitions in the laws governing FHFA's authority contain specific definitions relating to the GSEs' regulatory capital that are outdated or could otherwise restrict FHFA's discretion in prescribing regulatory capital requirements.[62] Those statutory definitions should be repealed and not incorporated into future legislation.

Treasury recommends:

- Congress should repeal the existing statutory definitions relating to the GSEs' regulatory capital that restrict FHFA's discretion in prescribing regulatory capital requirements, and those definitions should not be incorporated into future legislation. (legislative)

- FHFA's eventual regulatory capital requirements should require that each guarantor, or each GSE pending legislation, be appropriately capitalized by maintaining capital sufficient to remain viable as a going concern after a severe economic downturn and also to ensure that shareholders and unsecured creditors, rather than taxpayers, bear losses. FHFA's eventual regulatory capital requirements also should include a simple, transparent leverage restriction that supplements the risk-based capital requirements. (administrative)

- In connection with the new FHFA Director's ongoing re-assessment of the proposed capital rule, FHFA should disclose additional information on the calibration of the regulatory capital requirements. (administrative)

2. Credit Risk Transfers

In 2013, the GSEs began to develop programs to transfer credit risk on their acquisitions of single-family mortgage loans. These CRT programs have expanded significantly and have become a core part of the GSEs' single-family businesses. Most of the GSEs' CRT has been arranged through debt issuance structures – namely Fannie Mae's Connecticut Avenue Securities ("CAS") and Freddie Mac's Structured Agency Credit Risk ("STACR") securities – that track the performance of a reference pool of mortgage loans that have been securitized into the GSEs'

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[61] There is perhaps even some basis for doubt on that score. FHFA has projected that, had each GSE been in compliance with the proposed capital rule in the lead up to the financial crisis, Fannie Mae and Freddie Mac would have had only, respectively, \$3 billion (10 basis points) and \$12 billion (50 basis points) of regulatory capital remaining after the peak cumulative capital losses incurred during the crisis. *Id.* at 33,327 (presenting in Table 1 Fannie Mae's capital requirement in comparison to peak capital losses), 33,328 (presenting in Table 3 the same information for Freddie Mac).

[62] *See* FED. HOUS. FIN. AGENCY, ANNUAL REPORT TO CONGRESS 2018, cover letter.

MBS. However, insurance and reinsurance transactions, as well as lender risk sharing and other front-end transactions, are also a growing share of these CRT.

The GSEs' CRT programs enhance taxpayer protection and foster price discovery and market discipline, and in light of these features, FHFA should continue to support efforts to expand these programs. In particular, the reduction in retained credit risk that is achieved through CRT generally should be reflected in FHFA's regulatory capital requirements. At the same time, each of the existing CRT structures has strengths and weaknesses, and it remains unclear how CRT will function over the long term. FHFA should therefore encourage the GSEs to continue to engage in a diverse mix of economically sensible CRT, including by increasing reliance on institution-level capital.

Treasury recommends:

- FHFA should, in prescribing regulatory capital requirements, provide for appropriate capital relief to the extent that a guarantor, or a GSE pending legislation, transfers mortgage credit risk through a diverse mix of approved forms of CRT. (administrative)

3. Liquidity Requirements

During the financial crisis, many financial companies experienced liquidity difficulties despite apparently adequate capital levels. The GSEs themselves saw their funding costs increase in the summer of 2008 despite the perception of an implied Government backing of their liabilities, leading to concerns about the GSEs' ability to refinance their debt that eventually were an impetus for the conservatorships.[63] The GSEs have significantly reduced their reliance on debt funding since the financial crisis as they have wound down their retained mortgage portfolios, and the GSEs continue to transfer a significant portion of the funding risk on their mortgage loan acquisitions through their sales of MBS. However, the GSEs still do maintain more than $400 billion in outstanding debt, and they also retain meaningful liquidity risk with respect to the funding needs that relate to their cash window operations and their purchases of non-performing loans out of securitization pools. The latter funding need is a particularly notable liquidity risk, as it should be expected to increase significantly during a period of economic stress when funding markets might cease to function. In light of these liquidity risks, FHFA should continue to enhance the GSEs' liquidity risk management requirements, including with respect to any funding needs associated with purchases of non-performing loans out of securitization pools.

Treasury recommends:

- FHFA should prescribe liquidity requirements that require each guarantor, or each GSE pending legislation, to maintain high quality liquid assets sufficient to ensure it operates in a safe and sound manner. (administrative)

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[63] FCIC REPORT at 316 ("In July and August 2008, Fannie suffered a liquidity squeeze, because it was unable to borrow against its own securities to raise sufficient cash in the repo market."); *see id.* at 16 ("By June 2008, the spread [between the yield on the GSEs' long-term bonds and rates on Treasuries] had risen 65% over the 2007 level; by September 5, just before regulators parachuted in, the spread had nearly doubled from its 2007 level to just under 1%, making it more difficult and costly for the GSEs to fund their operations.").

B. Resolution Framework

A credible resolution framework can ensure that shareholders and unsecured creditors bear losses, thereby protecting taxpayers against bailouts, enhancing market discipline, and mitigating moral hazard and systemic risk. The importance of a credible resolution framework for the GSEs is heightened by the historical precedent set by the decision to place the GSEs in conservatorship instead of receivership and also by the statutory exclusion of the GSEs from the Federal Deposit Insurance Corporation's ("FDIC") orderly liquidation authority under Title II of the Dodd-Frank Act.[64] In light of these considerations, and to facilitate a credible resolution framework, each large guarantor should maintain a minimum amount of total loss-absorbing capacity that could be "bailed in" in the event of financial distress.

Treasury recommends:

- Congress should authorize FHFA to require each large guarantor, or a holding company of the large guarantor, to maintain convertible debt or other similar loss-absorbing instruments sufficient to ensure there is adequate total loss-absorbing capacity to facilitate resolution. (legislative)

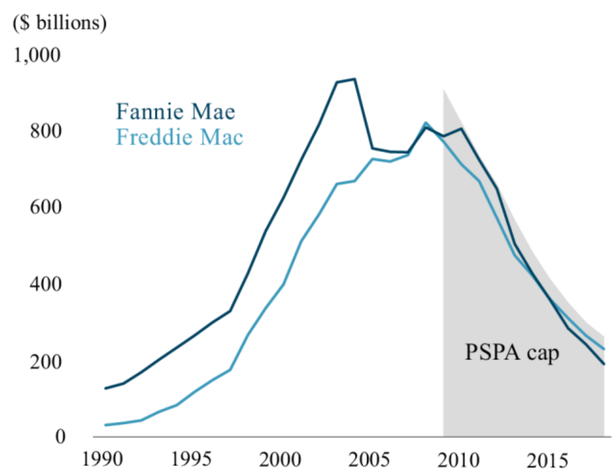
- Pending legislation, Treasury and FHFA should consider amending each PSPA to require each GSE to maintain convertible debt or other similar loss-absorbing instruments sufficient to ensure there is adequate total loss-absorbing capacity to facilitate resolution. (administrative)

C. Retained Mortgage Portfolios

In addition to acquiring mortgage loans for securitization, each GSE also acquires mortgage loans, MBS, and other mortgage assets for its own portfolio. These retained mortgage portfolios grew significantly in the 1990s and 2000s, increasing tenfold from $135 billion in 1990 to $1.56 trillion in 2003, and becoming the primary source of the GSEs' profits.[65] (Figure 9)

The growth and profitability of the retained mortgage portfolios were made possible in large part by the perception of an implicit Government guarantee, which permitted the GSEs to use subsidized borrowing to fund investments in

Figure 9. GSE Retained Mortgage Portfolios



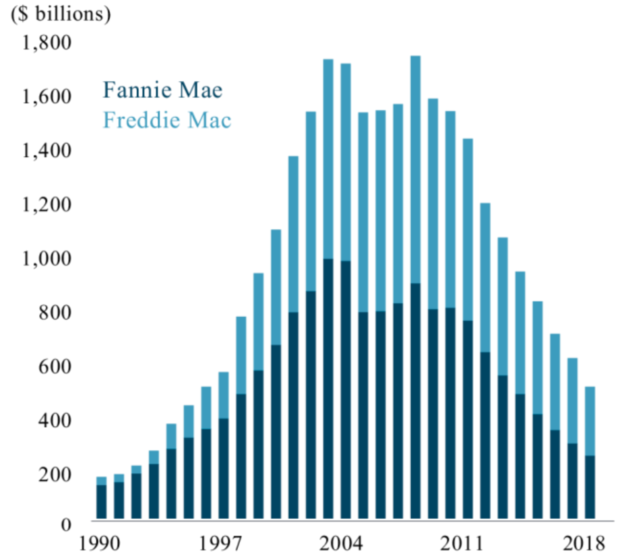
Source: FHFA, 2017 Report to Congress.

[64] *See* 12 U.S.C. § 5381(a)(11) (defining "financial company" for purposes of Title II of the Dodd-Frank Act to exclude any "regulated entity" as defined under section 1303(2) of the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (codified at 12 U.S.C. § 4502(20)), which is defined to include each GSE).

[65] Fed. Hous. Fin. Agency Office of Inspector General, The Continued Profitability of Fannie Mae and Freddie Mac Is Not Assured 10 (2015) ("Historically, net interest income from the Enterprises' retained portfolios has been their primary source of revenue. . . .").

these portfolios, profiting from the spread on these assets over what was close to a risk-free borrowing cost. Under this profitable dynamic, the GSEs' unsecured debt grew steadily, reaching $1.7 trillion in 2003, at a time when the Federal debt held by the public was $4.0 trillion. (Figure 10)

Figure 10. GSE Debt



Source: FHFA, 2017 Report to Congress; Fannie Mae and Freddie Mac's Annual Reports on Form 10-K.

Even at the time, the GSEs' retained mortgage portfolios raised systemic risk concerns.[66] These concerns were eventually validated, and a significant portion of the GSEs' early accounting losses in the financial crisis arose from the retained mortgage portfolios.[67] Each PSPA now caps each GSE's mortgage-related assets at $250 billion.

In light of this history, guarantors should be prohibited from maintaining investment portfolios except to the limited extent necessary to engage in the business of securitizing Government-guaranteed MBS. Guarantors should, for example, be permitted to hold mortgage loans to the extent necessary to operate a cash window or purchase non-performing loans out of securitization pools. Guarantors also should be permitted to invest in Government securities and other high quality liquid assets to the extent necessary to comply with the liquidity requirements prescribed by FHFA. Otherwise, guarantors' permissible investment activities should be narrowly construed.

Pending legislation, the PSPA caps on mortgage-related assets could be better tailored. Fannie Mae and Freddie Mac are subject to the same cap despite Freddie Mac's smaller size. Each PSPA's cap is also above the amount necessary to support the securitization business and could be further reduced over time, with a different cap for each GSE. Each PSPA should also be

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66 *See, e.g.*, *Proposals for Improving the Regulation of the Housing Government-Sponsored Enterprises: Hearing Before the S. Comm. on Banking, Housing, and Urban Affairs*, 108th Cong. 2 (2004) (statement of Alan Greenspan, Chairman, Federal Reserve Board) ("The unease relates mainly to the scale and growth of the mortgage-related asset portfolios held on their balance sheets. That growth has been facilitated, as least in part, by a perceived special advantage of these institutions that keeps normal market restraints from being fully effective."); *Regulatory Reform of the Government-Sponsored Enterprises: Hearing Before the S. Comm. on Banking, Housing, and Urban Affairs*, 109th Cong. 1 (2005) (statement of Alan Greenspan, Chairman, Federal Reserve Board) ("We at the Federal Reserve remain concerned about the growth and magnitude of the mortgage portfolios of the GSEs, which concentrate interest rate risk and prepayment risk at these two institutions and makes our financial system dependent on their ability to manage these risks."); *id.* (statement of John Snow, Secretary, Treasury) ("The potential for systemic risk is associated with Fannie Mae's and Freddie Mac's large portfolios of mortgages and mortgage-backed securities and other non-related assets, funded at extremely high rates of leverage.").

67 Fed. Hous. Fin. Agency Office of Inspector General, Fannie Mae and Freddie Mac: Where the Taxpayers' Money Went 21 (2012).

amended to expressly limit the retained mortgage portfolios going forward to the sole purpose of supporting the GSE's business of securitizing MBS.

Treasury recommends:

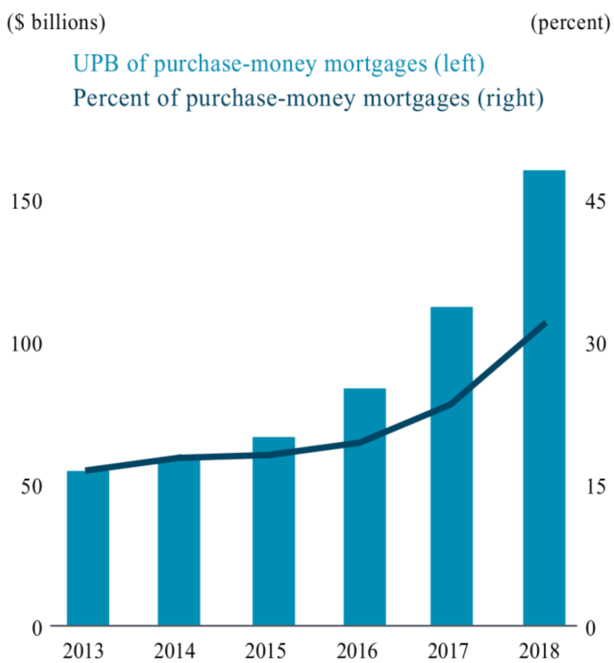
- Congress should prohibit each guarantor from investing in mortgage-related assets or other investments except to the limited extent necessary to engage in the business of securitizing Government-guaranteed MBS. (legislative)

- Pending legislation, Treasury and FHFA should amend each PSPA to further reduce the cap on the GSE's investments in mortgage-related assets, setting a different cap for each GSE, and also to restrict the GSE's retained mortgage portfolio to solely supporting its business of securitizing MBS. (administrative)

D. CREDIT UNDERWRITING PARAMETERS

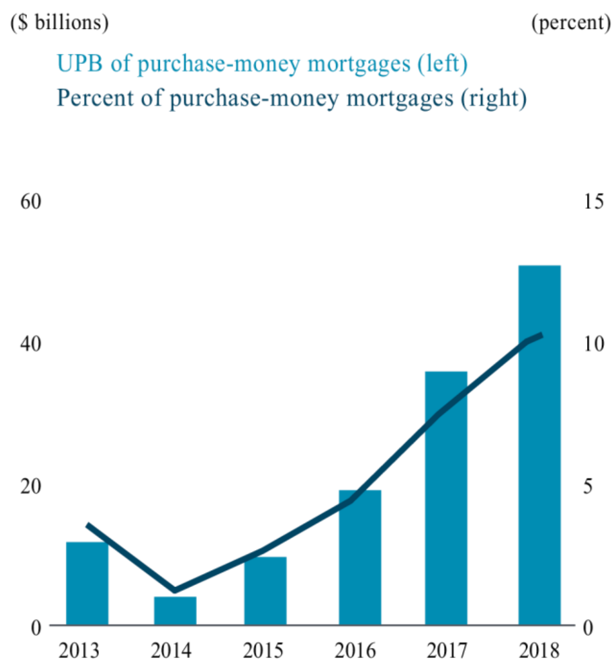
In the lead up to the financial crisis, mortgage lenders relaxed their underwriting standards as they began to originate subprime and other riskier mortgage loans to less creditworthy borrowers. The GSEs acquired many of these risky mortgage loans, eventually leading to significant credit losses. The GSEs have since improved their underwriting systems to better assess risk, reduce risk layering, and improve the use of compensating factors. FHFA has also directed each GSE to acquire only single-family mortgage loans that satisfy the points and fees, term, and amortization requirements for qualified mortgages under the CFPB's ability-to-repay

Figure 11. Purchase-Money Acquisitions Greater than 43% DTI



Source: FHFA.

Figure 12. Purchase-Money Acquisitions Greater than 95% LTV



Source: FHFA.

rule, which in effect has excluded some of the balloon payment, interest-only, negative amortization, and other riskier loans from GSE acquisitions.

While the GSEs' credit underwriting parameters have improved, there is no guarantee that the GSEs will not relax their underwriting requirements. Indeed, over the last few years the GSEs have increased their acquisitions of high DTI mortgage loans and high LTV loans, as well as mortgage loans with risk-layering. (Figures 11 and 12)

Treasury recommends:

- Congress should restrict the mortgage loans eligible to secure Government-guaranteed MBS to loans that have been originated in compliance with safe and sound underwriting restrictions approved or prescribed by FHFA, including as to responsible down payment requirements, DTI limits, insurance, and credit enhancement on high LTV loans. (legislative)

- FHFA should conduct an assessment of the credit and other risks posed by the GSEs' underwriting parameters, including acquisitions of single-family mortgage loans with greater risk characteristics such as high LTV, high DTI, or risk layering, and that assessment should guide underwriting restrictions to be prescribed by FHFA. (administrative)

V. PROMOTING COMPETITION IN THE HOUSING FINANCE SYSTEM

A. LEVELING THE PLAYING FIELD

As described in the Background section, approximately 65% of single-family mortgage loans are now supported in some way by the Federal Government, whether directly through FHA, VA, or the Department of Agriculture, or indirectly through the GSEs. Historically the Government footprint has been much smaller – around 40% as recently as 2007 and consistently well below that until the early 1980s. While the Federal Government's role might have been expected to increase during the financial crisis, the share of Government-supported mortgage lending has not scaled back since, notwithstanding 10 years of economic expansion. This leaves the system at risk of an even larger and more unprecedented role for the Federal Government in the housing finance system should there someday be another downturn.

As also described in the Background section, a driver of the GSEs' growth has been a regulatory framework that has become biased in favor of GSE-supported mortgage lending, with the GSEs' regulatory advantages actually having increased following the Dodd-Frank Act. The implementation of the Basel III reforms has increased the gap between the regulatory capital requirements of banking organizations and the GSEs. The adoption of the QM patch in 2014 provides mortgage lenders greater legal protections for GSE-eligible loans, particularly for conventional mortgage loans with DTI above the 43% qualified mortgage threshold. Similarly, the special treatment afforded to the GSEs under the disclosure, risk retention, and other regulations governing securitization transactions has heightened their competitive advantage over private sector securitizers.[68] Harmonizing the regulatory frameworks across market participants will be critical to establishing a level playing field that permits the private sector to resume its historical role as the primary source of funding in the housing finance system.

1. Harmonizing Regulatory Frameworks

While the various different regulatory frameworks should be tailored to the unique business models and risk profiles of the market participants subject to each framework's requirements, unwarranted differences in regulatory requirements between the GSEs and their private sector competitors should not create opportunities for regulatory arbitrage. In particular, similar credit risks generally should be subject to similar credit risk capital charges across market participants. The single best step FHFA can take to level the playing field with other market participants would be, consistent with the statutory requirement under the Temporary Payroll Tax Cut Continuation Act of 2011,[69] to more fully align the GSEs' credit risk capital charges with those of other fully private regulated financial institutions for holding similar assets.

Similarly, the capital treatment of securitizations and other similar transfers of mortgage credit risk to third parties is another potentially unwarranted gap between the regulatory capital requirements of banking organizations and the GSEs that merits scrutiny by FHFA and the federal banking regulators. While the GSEs' CRT provide meaningful capital relief under FHFA's proposed rule, there is considerable doubt as to whether the banking regulators' capital rules would permit a banking organization to achieve similar capital relief by structuring a CRT-like transaction as a synthetic securitization.[70] Even for securitizations that do conform to the banking regulators' capital rules, the credit risk capital charges on a banking organization's retained securitization exposures generally are considerably greater than the credit risk capital charges on the exposures retained by a GSE in connection with CRT, especially for the more senior interests.

More generally, FHFA should, in consultation with the other federal financial regulators, endeavor to ensure that differences in the regulatory frameworks between the GSEs and other market participants are tailored to differences in the underlying safety and soundness and systemic risks associated with these regulated entities and do not create opportunities for regulatory arbitrage. FSOC might potentially have a role in convening discussions on these

[68] *See, e.g.*, 12 U.S.C. § 1455(g) (exempting Freddie Mac's securities from the SEC's registration requirements, which includes the Regulation AB II disclosure requirements applicable to PLS), *id.* § 1723c (same with respect to Fannie Mae); 17 C.F.R. § 246.8 (providing that a securitization satisfies the risk retention requirements if it is guaranteed by a GSE).

[69] The Temporary Payroll Tax Cut Continuation Act of 2011 directed FHFA to require each GSE to increase its guarantee fees for 10 years to an amount that FHFA determined "to appropriately reflect the risk of loss, *as well the cost of capital allocated to similar assets held by other fully private regulated financial institutions* . . . ." (emphasis added) Temporary Payroll Tax Cut Continuation Act of 2011, Pub. L. No. 112-78, § 401, 125 Stat. 1280, 1287 (2011) (codified at 12 U.S.C. § 4547(b)). FHFA has implemented this to date by directing the GSEs to collect a 10 basis point assessment on GSE single-family acquisitions but without varying the assessment based on the underlying credit and other risks.

[70] That result is even despite a CRT-like transaction potentially posing less counterparty risk than the guarantees and credit derivatives that are credit risk mitigants eligible to satisfy the operational criteria for synthetic securitizations. *See* 12 C.F.R. § 3.41(b)(1).

interagency issues and identifying and remediating unwarranted differences in the regulatory frameworks.

Treasury recommends:

- FHFA should, in consultation with the other federal financial regulators, endeavor to harmonize the regulatory requirements applicable to the GSEs and other participants in the housing finance system, including with respect to the capital relief provided to GSEs and banking organizations for their transfers of mortgage credit risk to third parties. (administrative)

2. QM Patch Replacement

The Dodd-Frank Act amended the Truth in Lending Act to provide that a creditor generally may not make a residential mortgage loan unless the creditor makes a reasonable and good faith determination, based on verified and documented information and after considering such factors as the borrower's income, assets, and debt, that the borrower has a reasonable ability to repay the loan.[71] The CFPB's implementing rule establishes a presumption of compliance with this ability-to-repay ("ATR") requirement for any loan that falls within one of several categories of "qualified mortgages."[72] One category of qualified mortgages requires, among other requirements, that the borrower's DTI, as calculated and verified in accordance with the procedures set forth in the CFPB's Appendix Q to the rule, is not more than 43%.[73] A second category, but one that was intended to be temporary, is loans eligible to be purchased or guaranteed by either GSE while it operates under conservatorship or receivership (or until January 10, 2021, if sooner).[74] Under this "QM patch," the 43% DTI limit is not applicable, and the borrower's ability to repay may be verified under a GSE's underwriting guide instead of the CFPB's Appendix Q.

In its Core Principles Reports – Banks and Credit Unions, Treasury found that "[t]he QM Patch for GSE-eligible loans creates an unfair advantage for government-supported mortgages, without providing additional consumer protection, exposes taxpayers to potential losses, and inhibits consumer choices by restricting private sector flexibility and participation."[75] Treasury recommended that "[t]he CFPB should engage in a review of the ATR/QM rule and work to align QM requirements with GSE eligibility requirements, ultimately phasing out the QM Patch and subjecting all market participants to the same, transparent set of requirements."[76] In January 2019, the CFPB published a statutorily required assessment of the ATR rule that found, among

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[71] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 1411, 124 Stat. 1376, 2142 (2010) (codified at 15 U.S.C. § 1639c).

[72] Ability-to-Repay and Qualified Mortgage Standards under the Truth in Lending Act, 78 Fed. Reg. 6,408 (Jan. 30, 2013) (codified as amended at 12 C.F.R. § 1026.43).

[73] *Id.* § 1026.43(e)(2).

[74] *Id.* § 1026.43(e)(4).

[75] U.S. DEP'T OF TREASURY, A FINANCIAL SYSTEM THAT CREATES ECONOMIC OPPORTUNITIES: BANKS AND CREDIT UNIONS 99 (2017).

[76] *Id.*

other things, that mortgage lenders continue to rely heavily on the QM patch to comply with the rule.[77] On July 25, 2019, the CFPB announced that the QM patch would expire in January 2021 or after a short extension, and it also sought comment on whether to propose revisions to the ATR rule in light of the planned expiration.[78]

Treasury supports the contemplated expiration of the QM patch. The QM patch gives the GSEs a competitive advantage over portfolio lenders and other market participants to the extent that mortgage lenders face lower risk under the ATR rule for underwriting GSE-eligible loans, particularly if they actually sell those loans to the GSEs.[79] These greater legal protections are especially pronounced for conventional mortgage loans with DTI above the generally applicable 43% limit for qualified mortgages. Similarly, the GSEs' eligibility criteria include requirements unrelated to the borrower's ability to repay – for example, conforming loan limits – with the result that lenders of jumbo loans and other GSE-ineligible loans cannot rely on the QM patch and do not have the benefit of a similar bright line rule. Besides conferring a competitive advantage on the GSEs, the QM patch also gives the GSEs a quasi-regulatory role in defining ATR requirements that, while arguably appropriate on a temporary basis while the GSEs were in conservatorship, would be inappropriate if continued on a permanent basis or after the end of the GSEs' conservatorships.

Treasury also supports further revisions to the ATR rule to ensure that mortgage lenders continue to have a bright line safe harbor after expiration of the QM patch. In particular, Appendix Q, which was adopted from the outdated manual underwriting guidelines once used by FHA, lacks the clarity and detail necessary to provide a bright line safe harbor and should be either revised or removed. Modernizing Appendix Q to address self-employed borrowers, borrowers with non-traditional sources of income, and similar issues would address some of these issues. That approach might, however, raise other issues, as subsequent and potentially frequent amendments might be necessary to adjust to the changing economy and new technologies for verifying income, and those amendments might be difficult or unlikely given the time and effort required to amend regulations. Amending Appendix Q to reference the relevant sections of the GSEs' selling guides could perhaps avoid this need for frequent amendments, but with the downside of continuing the competitive advantage conferred on the GSEs by incorporating by reference their underwriting guidelines into the ATR rule.

More fundamentally, there is reason to doubt whether even a substantially revised Appendix Q could address most of the diverse income and debt verification scenarios while also providing

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77 The CFPB found that "although the [CFPB] expected that loans with DTI above the 43 percent threshold would increasingly be originated outside the [QM patch] category, i.e., as non-QM loans, the available data suggests that the opposite is happening." CONSUMER FIN. PROT. BUREAU, ABILITY-TO-REPAY AND QUALIFIED MORTGAGE RULE ASSESSMENT REPORT 191 (2019). With respect to reliance on the GSEs' underwriting systems, the CFPB noted "the data do suggest a somewhat greater use of the GSEs' AUS in recent years, particularly for loans which do not fit within or are more difficult to document within the General QM underwriting standards, such as loans made to self-employed borrowers." *Id.* at 189.

78 Qualified Mortgage Definition under the Truth in Lending Act, 84 Fed. Reg. 37,155 (Jul. 31, 2019) (advance notice of proposed rulemaking).

79 According to the CFPB, "although technically the [QM patch] applies to loans that are eligible for purchase or guarantee by one of the GSEs, market participants believe that extra compliance certainty is assured for loans actually sold to the GSEs." CONSUMER FIN. PROT. BUREAU, ABILITY-TO-REPAY AND QUALIFIED MORTGAGE RULE ASSESSMENT REPORT 194.

mortgage lenders with the requisite bright line safe harbor. Enforcement proceedings or litigation challenging whether, in the case of any particular mortgage loan, the mortgage lender verified the borrower's income and debt in compliance with the revised Appendix Q would inevitably raise fact-intensive inquiries that would themselves entail lengthy and expensive enforcement or judicial proceedings. The inevitability of these proceedings to simply determine the applicability of the safe harbor would in effect render the safe harbor essentially meaningless.

Given these considerations, Congress and the CFPB should consider alternative approaches to establishing bright line safe harbors for ATR compliance that do not rely on prescriptive underwriting requirements. One approach might be to use the pricing of the mortgage loan as a proxy for the risk that a borrower does not have the ability to repay the loan – for example, by deeming any mortgage loan that has a financing cost below a specified threshold to conclusively be a qualified mortgage. There is precedent for tailoring regulation based on pricing – for example, the CFPB's regulations for higher priced mortgage loans.[80] Another approach, perhaps as a complement to the first, might be to provide that a mortgage loan conclusively becomes a qualified mortgage after a specified seasoning period under the rationale that most defaults after that period would be a result of a change in the borrower's circumstances and not due to the lender's initial assessment of the borrower's ability to repay.

Related to this, the "qualified mortgage" definition, and any proposal to expand that definition, should be construed by FHFA as only setting the outer limits on the GSEs' potentially permissible credit underwriting parameters, with FHFA prescribing additional limits within that "qualified mortgage" credit box. In other words, the GSEs, and any other guarantors after legislative reform, should not necessarily be permitted to acquire any and all qualified mortgages, particularly given the Government backing that would support those acquisitions.

Treasury recommends:

- Congress should amend the Truth in Lending Act to establish a clear bright line safe harbor for compliance with the required ability-to-repay determination. (legislative)

- Pending legislation, the QM patch should expire, as contemplated by the CFPB's July 2019 advance notice of proposed rulemaking, and the CFPB should amend its ability-to-repay rule to establish a clear bright line safe harbor that replaces the QM patch. FHFA and the CFPB should continue to coordinate their efforts to avoid market disruption in connection with the expiration of the QM patch and the implementation of any amendments to the CFPB's ability-to-repay rule. (administrative)

- Following any change to the CFPB's ability-to-repay rule, FHFA should revisit the determination as to which single-family mortgage loans should be eligible for acquisition by the GSEs (with appropriate amendments to the PSPAs) or, following legislation, should be eligible to secure Government-guaranteed MBS. (administrative)

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80 12 C.F.R. § 1026.35.

3. Private-Label Securitization

Since the financial crisis, PLS issuance has funded only a small share of mortgage originations, with PLS issuance largely concentrated in nonperforming and re-performing mortgage loans and prime jumbo mortgage loans. The GSEs' CRT securities have provided an avenue for investors to assume mortgage credit risk, with the success of the GSEs' CRT programs possibly contributing to the relative absence of PLS issuances. The special treatment afforded to the GSEs under the disclosure, risk retention, and other regulations governing securitization transactions has also heightened the GSEs' competitive advantage over private sector securitizers, particularly to the extent that regulatory impediments adopted following the Dodd-Frank Act might have prevented PLS from playing a larger role.[81] For example, as discussed in Treasury's Core Principles Reports, the federal banking regulators' capital treatment of exposures to PLS might not always be proportionate to the underlying credit risks,[82] the risk retention rules for securitization transactions might pose undue burdens on PLS,[83] and the risk of assignee liability under various federal consumer financial laws might be a factor in limiting investor demand for PLS.[84]

The Securities and Exchange Commission's ("SEC") regulations prescribing disclosure requirements for SEC-registered MBS and other asset-backed securities might also unduly restrict PLS issuances.[85] Under the SEC's Regulation AB II, a PLS issuer offering SEC-registered MBS must disclose 270 data elements for each of the underlying mortgage loans.[86] It is difficult to collect the required data for some of these fields – with the expense and burden of collection potentially outweighing the benefit to PLS investors, particularly for seasoned mortgage loans – and some of the related regulatory definitions are ambiguous. These requirements might also have adversely affected private placement activity because the FDIC's securitization safe harbor requires compliance with Regulation AB II, although the FDIC has recently moved to address this issue by proposing to eliminate the requirement where Regulation AB II by its terms would not apply to the issuance.[87] Critically, the GSEs' MBS issuances are not subject to these disclosure requirements, which has heightened the GSEs' competitive advantage over PLS issuers. Requiring each GSE to conform its disclosure to Regulation AB II could help level the playing field.

Related to loan-level disclosures, although each GSE makes some loan-level data available as part of its CRT program, there remains still a considerable amount of loan-level data, for example, appraisal and other collateral data, that is not made available to market participants. Disclosing more of this loan-level data could enhance the ability of market participants to analyze and price mortgage credit risk and develop innovative underwriting systems that

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[81] *See* U.S. DEP'T OF TREASURY, A FINANCIAL SYSTEM THAT CREATES ECONOMIC OPPORTUNITIES: CAPITAL MARKETS 97-105 (2017).

[82] *Id.* at 97.

[83] *Id.* at 101-103.

[84] U.S. DEP'T OF TREASURY, A FINANCIAL SYSTEM THAT CREATES ECONOMIC OPPORTUNITIES: BANKS AND CREDIT UNIONS 101 (2017).

[85] Asset-Backed Securities Disclosure and Registration (Regulation AB II), 79 Fed. Reg. 57,184 (Sep. 24, 2014) (codified at 17 C.F.R. § 229.1100).

[86] *See* 17 C.F.R. § 229.1125.

[87] Securitization Safe Harbor, 84 Fed. Reg. 43,732 (Aug. 22, 2019) (notice of proposed rulemaking).

improve borrowers' access to mortgage credit and lower barriers to entry by potential guarantors or other private sector competitors.

Treasury recommends:

- The federal financial regulators should review the regulatory capital treatment of PLS exposures and the risk retention rules for securitizations, as recommended in Treasury's Core Principles Report – Capital Markets. (administrative)

- The CFPB should provide guidance or other regulatory comfort as to the extent and management of the assignee liability of passive secondary market investors under applicable federal consumer financial laws, as recommended in Treasury's Core Principles Report – Banks and Credit Unions. (administrative)

- The SEC should review Regulation AB II to assess the number of required reporting fields and to clarify the defined terms for registered PLS issuances. (administrative)

- FHFA should consider whether to require each GSE to conform its loan-level disclosures to Regulation AB II after the regulation is reviewed by the SEC. (administrative)

- FHFA should determine the extent and manner of the feasible disclosure of the GSEs' historical loan-level data and property valuation data to the public, taking into account any privacy and safety and soundness risks. (administrative)

B. COMPETITIVE SECONDARY MARKET

Consistent with several recent legislative proposals, FHFA asked Congress in June 2019 for authority to charter competitors to the GSEs.[88] A competitive secondary market would have several compelling benefits. First, ending the duopoly may help protect taxpayers against future bailouts. Having multiple guarantors could reduce the systemic importance of any single guarantor and enhance the resolvability of an insolvent guarantor, thereby mitigating moral hazard, increasing market discipline, and enhancing taxpayer protections. Second, the duopoly market structure has reinforced the perception of an implicit Government guarantee that has given the GSEs a competitive advantage over private sector competition. Ending the duopoly would be a step toward leveling the playing field. Third, there is some question as to whether the benefits of any subsidy conferred on the GSEs accrue to their shareholders instead of borrowers. A 1996 CBO report found the GSEs were a "spongy conduit—soaking up nearly $1 for every $2

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[88] *See* FED. HOUS. FIN. AGENCY, ANNUAL REPORT TO CONGRESS 2018, cover letter ("[T]he Enterprises' current duopoly undercuts competition in the market. Increased competition would reduce market reliance on either Enterprise and enhance market stability, as well as benefit home buyers. To promote competition, Congress should authorize additional competitors and provide FHFA chartering authority similar to that of the Office of the Comptroller of the Currency."). FHFA's request echoed a January 2018 FHFA reform vision that also contemplated competitors to the GSEs. *See* FED. HOUS. FIN. AGENCY, FEDERAL HOUSING FINANCE AGENCY PERSPECTIVES ON HOUSING FINANCE REFORM (Jan. 2018).

delivered. . . ."[89] More recently, a 2010 CBO study found that "[e]vidence from the spread between interest rates on jumbo and conforming loans suggests that the implicit federal guarantee lowered mortgage interest rates by no more than 0.25 percentage points in normal times."[90] Relative to the GSE market structure, a competitive secondary market should tend to ensure that any subsidy is passed through to the borrower. Fourth, a competitive secondary market could promote innovation and market dynamism, not just with respect to the underwriting and pricing of mortgage loans, but also with respect to the services provided to each guarantor's lender clients. That innovation—for example in the credit score methodologies used in the underwriting process—could help identify and extend mortgage credit to borrowers who, while creditworthy, might not be eligible under the GSEs' underwriting criteria.

It remains, however, an open question whether private sector entities would be competitive with the GSEs, and also whether the risk-adjusted returns would be sufficient to attract entrants. Congress could address some of these issues by supplementing FHFA's chartering authority with other authorities to foster a competitive secondary market, for example, by authorizing FHFA to set variable guarantor-specific fees for the Government guarantee of a particular guarantor's MBS or authorizing FHFA to lower barriers to entry by making the GSEs' loan-level and appraisal data and the source code for the GSEs' automated underwriting system available to new entrants.

The likelihood of achieving a competitive secondary market also will depend in part on the specifics of any legislation. Barriers to entry might be heightened, for example, if Congress requires guarantors to assume nationwide service requirements immediately after beginning business without some transition period, or if the legislation leads to significant economies of scale among guarantors. In light of these considerations, Congress should consider the implications for the likelihood of achieving a competitive secondary market when determining what legal requirements and restrictions should be applicable to newly chartered guarantors.

Treasury recommends:

- Congress should authorize FHFA to charter competitor guarantors to the GSEs and should direct FHFA to re-charter each GSE on the same charter available to these potential competitors. Effective as of its re-chartering, each GSE's statutory charter should be repealed. (legislative)

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[89] U.S. CONG. BUDGET OFFICE, ASSESSING THE PUBLIC COSTS AND BENEFITS OF FANNIE MAE AND FREDDIE MAC xiv (1996); *see also Federal Subsidies for the Housing GSEs: Hearing Before the Subcomm. on Capital Markets, Insurance, and Government Sponsored Enterprises of the H. Financial Services Comm.*, 107th Cong. 2 (2001) (statement of Daniel L. Crippen, Director, CBO) ("CBO estimates that a little more than half ($7.0 billion) of the total subsidy in 2000 passed through to conforming mortgage borrowers via interest rates that are estimated to be 25 basis points lower because of the subsidy. About 30 percent of the total subsidy was retained by Fannie Mae and Freddie Mac, and the remaining 20 percent was disbursed to customers and shareholders of member institutions of the Federal Home Loan Bank System.").

[90] U.S. CONG. BUDGET OFFICE, FANNIE MAE, FREDDIE MAC, AND THE FEDERAL ROLE IN THE SECONDARY MARKET 18 (2010).

- Congress should give FHFA appropriate authorities to foster competition with the re-chartered GSEs. (legislative)

- Congress should take into account the effects on secondary market competition when considering the legal requirements or restrictions it imposes on guarantors. (legislative)

C. Competitive Primary Market

1. *Equitable Access to the Secondary Market*

The GSEs were chartered to operate a secondary market facility that would, among other things, promote access to mortgage credit throughout the United States.[91] Central to that mission has been fostering access for small, rural, and other mortgage lenders to the secondary market. These community-based lenders play a particularly vital role in serving rural and other historically underserved borrowers. One of the ways in which the GSEs foster equitable access to the secondary market is through their cash windows. The GSEs' most common type of securitization transaction is a lender swap transaction under which a mortgage lender delivers a pool of mortgage loans to the GSE in exchange for GSE-guaranteed MBS backed by those loans. The cash window is an alternative to a lender swap under which the GSE purchases mortgage loans for cash consideration from a mortgage lender, aggregates those loans with acquisitions from other mortgage lenders, and then securitizes the larger and more diverse pool at a later date. This cash window-facilitated aggregation provides for better pricing to the smaller lenders than would be obtained in a relatively small lender swap transaction.

Legislative reform should preserve this practice by requiring single-family guarantors to offer a similar cash window for small lenders. As part of this cash window mandate, mortgage lenders should have the option to sell mortgage loans into the cash window with or without the servicing rights retained. The pricing for cash window delivery should be on parity with the pricing for lender swap or other transactions, with an appropriate adjustment for the value of any servicing rights released. Single-family guarantors should also be prohibited from offering volume-based pricing discounts or other incentives to their larger sellers so as to help ensure that the primary market remains competitive and is not dominated by a few large mortgage lenders.

In addition to operating a cash window, single-family guarantors generally should be required to offer to acquire mortgage loans from across the nation. A nationwide service requirement will foster equitable secondary market access, diversified Government-guaranteed MBS, and also affordable access to mortgage credit by underserved borrowers.

Cash window and nationwide service requirements could, however, pose a barrier to entry to new single-family guarantors, and Congress might wish to consider a phased-in transition period for newly chartered single-family guarantors. Careful attention should be devoted to the drafting of the nationwide service requirement so as to not confer on FHFA the authority to in effect dictate underwriting or pricing terms for single-family guarantors – for example, the authority to

[91] 12 U.S.C. § 1716(4) ("The Congress declares that the purposes of this subchapter are to establish secondary market facilities for residential mortgages, . . . and to authorize such facilities to . . . promote access to mortgage credit throughout the Nation (including central cities, rural areas, and underserved areas) . . . ."); *id.* § 1451 note (providing a similar purpose for Freddie Mac).

require a single-family guarantor to acquire mortgage loans from a geographic area that the single-family guarantor has determined to have home prices that are not supported by market fundamentals.

FHFA has undertaken several initiatives during the conservatorships to ensure that the GSEs offer equitable access to the secondary market. For example, in the fall of 2012, FHFA required the GSEs to increase guarantee fees for lender swap transactions relative to those charged for cash window transactions. Because larger lenders tend to elect swap transactions while smaller lenders tend to sell into the cash window, the effect of these changes was to level the playing field for small and large lenders.[92] Pending legislation, these conservatorship-era protections against volume-based discounts should be incorporated into the amended PSPAs, along with a requirement that each GSE continue to operate a cash window.

Treasury recommends:

- Each single-family guarantor should be required to operate a cash window for small lenders, should be prohibited from offering volume-based pricing discounts or other similar incentives, and should be required to maintain a nationwide presence. (legislative)

- Pending legislation, Treasury and FHFA should amend each PSPA to require each GSE to maintain a nationwide cash window for small lenders and to prohibit volume-based pricing discounts or other similar incentives. (administrative)

2. FHLBank Support of the Primary Market

When the FHLBank Act was enacted in 1932, Congress limited FHLBank membership to thrift institutions of various types and to insurance companies, many of which were active mortgage lenders at the time. As the housing finance system has evolved and other types of financial institutions have become important sources of mortgage lending, Congress has expanded membership to include federally insured depository institutions in 1989, non-depository community development financial institutions in 2008, and non-federally insured credit unions in 2015. Some non-bank and other types of mortgage lenders, however, still do not have access to FHLBank advances, despite now playing a larger role in the housing finance system.

Related to this, from time to time, FHFA has amended its membership rule to ensure "a nexus between [FHLBank] membership and the housing and community development mission of the

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[92] FED. HOUS. FIN. AGENCY, FANNIE MAE AND FREDDIE MAC SINGLE-FAMILY GUARANTEE FEES IN 2014 14 (2015) ("With the December 2012 guarantee fee increase, FHFA also sought to reduce pricing differences between smaller lenders and larger lenders. . . . The December 2012 increase raised ongoing guarantee fees for swap executions by more than those for cash window executions. This resulted, on average, in fees paid by small lenders increasing less than those paid by larger lenders."); *see also Creating a Housing Finance System Built to Last: Ensuring Access for Community Institutions: Hearing Before the Subcomm. on Securities, Insurance, and Investment of S. Comm. on Banking, Housing, and Urban Affairs*, 113th Cong. 1 (2013) (statement of Sandra Thompson, Dep. Dir., FHFA).

[FHLBanks].”[93] The most recent was a 2010 review that culminated in a final rule in 2016 that excluded captive insurance companies from membership, subject to a transition period for those that were already members.[94]

With the continued evolution of the housing finance system, there might be some question as to whether the current statutory and regulatory restrictions on FHLBank membership continue to be well-tailored to the housing and community development mission of the FHLBanks. The collateral eligible to secure FHLBank advances is already limited by law to mortgage and other assets that generally have a close nexus to the FHLBanks’ mission, such that broader membership eligibility should not necessarily detract from that mission. While there might be unique counterparty or other safety and soundness risks posed by advances to mortgage lenders that are not subject to comprehensive prudential regulation, those risks potentially could be managed through enhanced collateral haircuts, capital requirements, or other counterparty risk management practices (e.g., bankruptcy-remote funding structures). In light of these considerations and the continued evolution of the housing finance system, Congress and FHFA should revisit the FHLBank membership eligibility restrictions to consider whether captive insurers and other types of financial institutions should be eligible for membership.

Treasury recommends:

- Congress should consider permitting additional classes of mortgage lenders to become FHLBank members. (legislative)

- Pending legislation, FHFA should revisit its rule excluding captive insurance companies from FHLBank membership in light of the continued evolution of the housing finance system. (administrative)

VI. CONCLUSION

Treasury reiterates its preference and recommendation that Congress enact comprehensive housing finance reform. Congress can address this last unfinished business of the financial crisis in a way that preserves what works in the current system, protects taxpayers, and reduces the influence of the Federal Government in the housing finance system. To that end, Treasury recommends that Congress authorize Ginnie Mae to offer an explicit, paid-for guarantee of the timely payment of principal and interest on MBS backed by eligible conventional loans and eligible multifamily mortgage loans and also that Congress authorize FHFA to charter competitors to the GSEs as guarantors of these Government-guaranteed MBS. That legislation should also allow for enhancements to the regulatory framework of the GSEs and any newly chartered competitors to safeguard their safety and soundness, minimize risks to financial stability, protect equitable access for all mortgage lenders, and support affordable housing for both borrowers and renters.

Pending legislation, Treasury will continue to support FHFA’s administrative actions to lay the foundation for eventual legislation, enhance the regulation of the GSEs, promote private sector

93 Members of Federal Home Loan Banks, 75 Fed. Reg. 81,145 (Dec. 27, 2010) (requesting comments on potential changes to the rule governing FHLBank membership eligibility).

94 Members of Federal Home Loan Banks, 81 Fed. Reg. 3,246 (Jan. 20, 2016) (final rule).

competition, and satisfy the preconditions for ending the GSEs' conservatorships. FHFA should begin the process of ending the decade-long conservatorships of the GSEs – including by beginning the process of recapitalizing the GSEs. In parallel, FHFA should continue to implement reforms that promote private sector competition in the housing finance system by leveling the playing field across market participants. Implementing these reforms will accomplish the housing reform goals set forth in the Presidential Memorandum and strengthen the United States' growing and dynamic economy, while expanding affordable homeownership.

Appendix

Legislative and Administrative Recommendations

Recommendation		Type	Timeline
Defining a Limited Role for the Federal Government			
Clarifying Existing Government Support			
1.	Congress should authorize an explicit, paid-for guarantee by Ginnie Mae of qualifying MBS that are collateralized by eligible conventional mortgage loans.	Legislative	N/A
2.	Pending legislation, to avoid market disruption, Treasury should continue to maintain its ongoing commitment to support each GSE's single-family MBS through the PSPAs, as amended as contemplated by this plan.	Administrative	Ongoing pending legislation
3.	Congress should authorize an explicit, paid-for guarantee by Ginnie Mae of qualifying MBS that are collateralized by eligible multifamily mortgage loans.	Legislative	N/A
4.	Pending legislation, to preserve support for low- and moderate-income and other historically underserved renters, Treasury should continue to maintain its ongoing commitment to support each GSE's multifamily MBS through the PSPAs, as amended as contemplated by this plan.	Administrative	Ongoing pending legislation
5.	Congress should condition the availability of the Government guarantee of qualifying MBS on a GSE or other FHFA-approved guarantor taking the first-loss position on the Government-guaranteed MBS through specified credit enhancement on the mortgage collateral securing the MBS.	Legislative	N/A
6.	Pending legislation, each GSE should be recapitalized so that private capital takes the first-loss position on the GSE's exposure to risk and loss.	Administrative	As promptly as practicable
7.	FHFA and Ginnie Mae should identify and assess the operational and other issues posed by authorizing Ginnie Mae to guarantee the timely payment of principal and interest on qualifying MBS, including any necessary enhancements to existing securitization and bond administration infrastructure.	Administrative	As promptly as practicable
8.	Congress should authorize FHFA to set and from time to time adjust fees for Government guarantees of qualifying MBS so that the compensation paid to the Federal Government is, to the extent it might be feasible, consistent with the pricing of similar risk by private sector market participants (accounting for Government support in other market segments).	Legislative	N/A
9.	Pending legislation, each PSPA should be amended to compensate the Federal Government for the continued support of the GSEs through an appropriately priced periodic commitment fee.	Administrative	PSPA amendment

Recommendation		Type	Timeline
Support of Single-Family Mortgage Lending			
10.	Congress should restrict the permissible activities of guarantors to the business of securitizing Government-guaranteed MBS.	Legislative	N/A
11.	Pending legislation, FHFA should assess whether each of the current products, services, and other single-family activities of each GSE is consistent with its statutory mission and should continue to benefit from support under Treasury's PSPA commitment (with appropriate amendments to the PSPA), and in particular, FHFA should solicit information on whether to tailor support for cash-out refinancings, investor loans, vacation home loans, higher principal balance loans, or other subsets of GSE-acquired mortgage loans.	Administrative	Before the PSPA amendment
12.	FHFA should implement a policy and process for approval of the GSEs' new pilot programs and other new activities or products, with that process soliciting public input.	Administrative	As promptly as practicable
Support of Multifamily Mortgage Lending			
13.	Congress should implement a framework to limit the aggregate footprint of multifamily guarantors.	Legislative	N/A
14.	Congress should limit the multifamily mortgage loans that are eligible to secure Government-guaranteed multifamily MBS to ensure a close nexus to a specified affordability mission.	Legislative	N/A
15.	Pending legislation, Treasury and FHFA should consider amending each PSPA to limit support of each GSE's multifamily business to its underlying affordability mission, including potentially through a revised framework for capping each GSE's multifamily footprint.	Administrative	PSPA amendment
Additional Support for Affordable Housing			
16.	FHFA should revisit the GSEs' underwriting criteria for acquisitions of multifamily loans secured by properties in jurisdictions that adopt rent-control laws or other undue impediments to housing development.	Administrative	As promptly as practicable
17.	Congress should replace the GSEs' statutory affordable housing goals with a more efficient, transparent, and accountable mechanism for delivering tailored support to first-time homebuyers and low- and moderate-income, rural, and other historically underserved borrowers, with a portion of the associated funding potentially transferred to HUD to expand its affordable housing activities.	Legislative	N/A
18.	Pending legislation, FHFA should consider more efficient mechanisms for the GSEs to achieve the statutory affordable housing goals.	Administrative	As promptly as practicable

Recommendation		Type	Timeline
19.	FHFA and HUD should develop and implement a specific understanding as to the appropriate roles and overlap between the GSEs and FHA, for example, with respect to the GSEs' acquisitions of high LTV and high DTI loans and FHA's underwriting of cash-out, conventional-to-FHA, and other refinancing loans and loans to repeat FHA borrowers.	Administrative	Before the PSPA amendment
Ending the Conservatorships			
20.	Pending legislation, FHFA should exercise its authority as conservator to begin the process to end each GSE's conservatorship in a manner consistent with the preconditions set forth in this plan.	Administrative	As promptly as practicable
21.	Treasury and FHFA should develop a recapitalization plan for each GSE after identifying and assessing the full range of strategic options.	Administrative	As promptly as practicable
22.	Pending that recapitalization plan, and as an interim step toward the eventual PSPA amendment contemplated by this plan, Treasury and FHFA should consider permitting each GSE to retain earnings in excess of the $3 billion capital reserve currently permitted, with appropriate compensation to Treasury for any deferred or forgone dividends.	Administrative	Before the PSPA amendment
Protecting Taxpayers against Bailouts			
Capital and Liquidity Requirements			
23.	Congress should repeal the existing statutory definitions relating to the GSEs' regulatory capital that restrict FHFA's discretion in prescribing regulatory capital requirements, and those definitions should not be incorporated into future legislation.	Legislative	N/A
24.	FHFA's eventual regulatory capital requirements should require that each guarantor, or each GSE pending legislation, be appropriately capitalized by maintaining capital sufficient to remain viable as a going concern after a severe economic downturn and also to ensure that shareholders and unsecured creditors, rather than taxpayers, bear losses. FHFA's eventual regulatory capital requirements also should include a simple, transparent leverage restriction that supplements the risk-based capital requirements.	Administrative	As promptly as practicable
25.	In connection with the new FHFA Director's ongoing re-assessment of the proposed capital rule, FHFA should disclose additional information on the calibration of the regulatory capital requirements.	Administrative	As promptly as practicable
26.	FHFA should, in prescribing regulatory capital requirements, provide for appropriate capital relief to the extent that a guarantor, or a GSE pending legislation, transfers mortgage credit risk through a diverse mix of approved forms of CRT.	Administrative	As promptly as practicable

Recommendation		Type	Timeline
27.	FHFA should prescribe liquidity requirements that require each guarantor, or each GSE pending legislation, to maintain high quality liquid assets sufficient to ensure it operates in a safe and sound manner.	Administrative	As promptly as practicable
Resolution Framework			
28.	Congress should authorize FHFA to require each large guarantor, or a holding company of the large guarantor, to maintain convertible debt or other similar loss-absorbing instruments sufficient to ensure there is adequate total loss-absorbing capacity to facilitate resolution.	Legislative	N/A
29.	Pending legislation, Treasury and FHFA should consider amending each PSPA to require each GSE to maintain convertible debt or other similar loss-absorbing instruments sufficient to ensure there is adequate total loss-absorbing capacity to facilitate resolution.	Administrative	PSPA amendment
Retained Mortgage Portfolios			
30.	Congress should prohibit each guarantor from investing in mortgage-related assets or other investments except to the limited extent necessary to engage in the business of securitizing Government-guaranteed MBS.	Legislative	N/A
31.	Pending legislation, Treasury and FHFA should amend each PSPA to further reduce the cap on the GSE's investments in mortgage-related assets, setting a different cap for each GSE, and also to restrict the GSE's retained mortgage portfolio to solely supporting its business of securitizing MBS.	Administrative	PSPA amendment
Credit Underwriting Parameters			
32.	Congress should restrict the mortgage loans eligible to secure Government-guaranteed MBS to loans that have been originated in compliance with safe and sound underwriting restrictions approved or prescribed by FHFA, including as to responsible down payment requirements, DTI limits, insurance, and credit enhancement on high LTV loans.	Legislative	N/A
33.	FHFA should conduct an assessment of the credit and other risks posed by the GSEs' underwriting parameters, including acquisitions of single-family mortgage loans with greater risk characteristics such as high LTV, high DTI, or risk layering, and that assessment should guide underwriting restrictions to be prescribed by FHFA.	Administrative	Before the PSPA amendment

Recommendation		Type	Timeline
Promoting Competition in the Housing Finance System			
Leveling the Playing Field			
34.	FHFA should, in consultation with the other federal financial regulators, endeavor to harmonize the regulatory requirements applicable to the GSEs and other participants in the housing finance system, including with respect to the capital relief provided to GSEs and banking organizations for their transfers of mortgage credit risk to third parties.	Administrative	Ongoing
35.	Congress should amend the Truth in Lending Act to establish a clear bright line safe harbor for compliance with the required ability-to-repay determination.	Legislative	N/A
36.	Pending legislation, the QM patch should expire, as contemplated by the CFPB's July 2019 advance notice of proposed rulemaking, and the CFPB should amend its ability-to-repay rule to establish a clear bright line safe harbor that replaces the QM patch. FHFA and the CFPB should continue to coordinate their efforts to avoid market disruption in connection with the expiration of the QM patch and the implementation of any amendments to the CFPB's ability-to-repay rule.	Administrative	January 2021 (or with a short extension)
37.	Following any change to the CFPB's ability-to-repay rule, FHFA should revisit the determination as to which single-family mortgage loans should be eligible for acquisition by the GSEs (with appropriate amendments to the PSPAs) or, following legislation, should be eligible to secure Government-guaranteed MBS.	Administrative	Following any amendment to the ATR rule
38.	The federal financial regulators should review the regulatory capital treatment of PLS exposures and the risk retention rules for securitizations, as recommended in Treasury's Core Principles Report – Capital Markets.	Administrative	As promptly as practicable
39.	The CFPB should provide guidance or other regulatory comfort as to the extent and management of the assignee liability of passive secondary market investors under applicable federal consumer financial laws, as recommended in Treasury's Core Principles Report – Banks and Credit Unions.	Administrative	As promptly as practicable
40.	The SEC should review Regulation AB II to assess the number of required reporting fields and to clarify the defined terms for registered PLS issuances.	Administrative	As promptly as practicable
41.	FHFA should consider whether to require each GSE to conform its loan-level disclosures to Regulation AB II after the regulation is reviewed by the SEC.	Administrative	Following the SEC's review of the rule
42.	FHFA should determine the extent and manner of the feasible disclosure of the GSEs' historical loan-level data and property valuation data to the public, taking into account any privacy and safety and soundness risks.	Administrative	As promptly as practicable

Recommendation		Type	Timeline
Competitive Secondary Market			
43.	Congress should authorize FHFA to charter competitor guarantors to the GSEs and should direct FHFA to re-charter each GSE on the same charter available to these potential competitors. Effective as of its re-chartering, each GSE's statutory charter should be repealed.	Legislative	N/A
44.	Congress should give FHFA appropriate authorities to foster competition with the re-chartered GSEs.	Legislative	N/A
45.	Congress should take into account the effects on secondary market competition when considering the legal requirements or restrictions it imposes on guarantors.	Legislative	N/A
Competitive Primary Market			
46.	Each single-family guarantor should be required to operate a cash window for small lenders, should be prohibited from offering volume-based pricing discounts or other similar incentives, and should be required to maintain a nationwide presence.	Legislative	N/A
47.	Pending legislation, Treasury and FHFA should amend each PSPA to require each GSE to maintain a nationwide cash window for small lenders and to prohibit volume-based pricing discounts or other similar incentives.	Administrative	PSPA amendment
48.	Congress should consider permitting additional classes of mortgage lenders to become FHLBank members.	Legislative	N/A
49.	Pending legislation, FHFA should revisit its rule excluding captive insurance companies from FHLBank membership in light of the continued evolution of the housing finance system.	Administrative	As promptly as practicable