

November 23, 2021

Acting Director Sandra L. Thompson
Federal Housing Finance Agency
400 Seventh Street, SW
10th Floor
Washington, DC 20219

Re: RIN 2590-AB17, Notice of Proposed Rulemaking -
Enterprise Regulatory Capital Framework

Dear Acting Director Thompson:

The undersigned civil rights, housing policy, and consumer advocacy organizations are writing in response to the Federal Housing Finance Agency’s (“FHFA”) Request for Comment on the Notice of Proposed Rulemaking (“Proposed Rule”) regarding the Enterprise Regulatory Capital Framework.¹ This topic is critically important because it affects the pricing and availability of mortgage credit at a time when the Black/White homeownership gap is as wide as it was prior to passage of the Fair Housing Act. We applaud FHFA’s direction in this Proposed Rule as it is likely to provide greater access to credit for borrowers of color and other protected groups consistent with the GSEs’ mission and fair lending obligations. Our organizations believe that the responses below will help inform FHFA’s rulemaking.

The Final Rule Should Be Consistent with the GSE’s Mission to Serve The Whole of The Market

Given the GSE’s statutory mandates and extensive government support, the final rule should reflect the requirement that the GSEs serve the whole of the market, including communities of color.² Consistent with the statutory mission of the GSEs, one of FHFA’s principal duties is to ensure that “the operations and activities of each regulated entity foster liquid, efficient, competitive, and resilient national housing finance markets (including 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).”³ It is also FHFA’s duty to ensure “the activities of each regulated entity and the manner in which such regulated entity is

¹ FHFA, *Notice of Proposed Rulemaking: Enterprise Regulatory Capital Framework*, 86 Fed. Reg. 53230 (Sept. 27, 2021), <https://www.federalregister.gov/documents/2021/09/27/2021-20297/enterprise-regulatory-capital-framework-rule-prescribed-leverage-buffer-amount-and-credit-risk>.

² The purpose of the GSEs includes: “Provid[ing] ongoing assistance to the secondary market for residential mortgages (including 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) by increasing the liquidity of mortgage investments and improving the distribution of investment capital available for residential mortgage financing; [and] Promot[ing] access to mortgage credit throughout the Nation (including central cities, rural areas, and underserved areas) by increasing the liquidity of mortgage investments and improving the distribution of investment capital available for residential mortgage financing. . . .” Fannie Mae Charter, 12 U.S.C. § 1716; Freddie Mac Charter, 12 U.S.C. § 1451 note (Statement of Purpose). Although communities of color do not necessarily consist of low- and moderate-income families, there can be overlap between these communities. However, “underserved areas” would include communities of color, regardless of income.

³ 12 U.S.C. § 4513 (a)(1)(B).

operated are consistent with the public interest.”⁴ In October 2020, FHFA issued its Strategic Plan: Fiscal Years 2021-2024 (“Strategic Plan”), which emphasized the mandate to serve the whole of the market by stating: “Achieving a liquid, resilient housing finance market throughout the country also requires improved access to responsible mortgage credit across different market segments of creditworthy borrowers.”⁵ The final rule should be consistent with the statutory mission and strategic plan.

The Proposed Rule Should Be Reviewed for Fair Lending Risk

The GSEs are subject to the fair lending laws, including the Fair Housing Act,⁶ the Equal Credit Opportunity Act (“ECOA”),⁷ and the Federal Housing Enterprises Financial Safety and Soundness Act (“Safety and Soundness Act”).⁸ The GSEs have long had an abysmal record of purchasing mortgages from borrowers of color, and even those that were purchased often had higher costs for these borrowers than the mortgages for White borrowers.⁹ For example, in 2019, only 4.8% of Fannie Mae and 3.6% of Freddie Mac home purchase loans and only 4.1% and 3.7% of Fannie Mae and Freddie Mac refinance loans, respectively, were for Black borrowers. The GSEs have not been as effective as they could be in purchasing loans for Black borrowers, and this fact should be taken into account as part of the strategy for the regulatory capital framework.

FHFA must ensure that the regulatory capital framework avoids discriminatory outcomes and also promotes equitable treatment of borrowers and communities of color. As described more fully below, there is a close nexus between the GSEs’ approach to raising capital and managing financial risk and race/ethnicity, which raises the risk that any regulatory capital initiatives will lead to adverse outcomes for communities of color. As the regulator of the GSEs, FHFA has a responsibility to identify and address any potentially discriminatory outcomes as well as promote financial inclusion and affirmative initiatives that help communities of color mitigate their risk. FHFA must not assume that policies such as this proposed rule that do not explicitly contain race-based criteria or other standards tied to protected class characteristics are compliant with fair lending laws. Because our society is deeply inequitable and because of structural barriers like residential segregation, restrictive zoning policies, the dual credit market, and biased technologies, even seemingly race-neutral policies can perpetuate discriminatory outcomes.

⁴ *Id.*

⁵ FHFA, *Strategic Plan: Fiscal Years 2021-2024* (Sept. 22, 2020), <https://www.fhfa.gov/AboutUs/Reports/Pages/FHFA-Strategic-Plan-Fiscal-Years-2021-2024.aspx>.

⁶ 42 U.S.C. § 3601 *et seq.* See also, 24 C.F.R. Part 100 (regulations promulgated by the U.S. Department of Housing and Urban Development (“HUD”) implementing the Fair Housing Act).

⁷ 15 U.S.C. § 1691 *et seq.* See also, 12 C.F.R. Part 1002 (regulations promulgated by the Consumer Financial Protection Bureau (“CFPB”) implementing the ECOA).

⁸ 12 U.S.C. § 4501 *et seq.* See also, 24 C.F.R. Part 81 (regulations promulgated by HUD implementing the Safety and Soundness Act).

⁹ See FHFA, *Annual Housing Report* at 11, Table 6 (October 2020), <https://www.fhfa.gov/AboutUs/Reports/ReportDocuments/Annual-Housing-Report-2020.pdf>. See also Jung Hyun Choi *et al.*, *Explaining the Black-White Homeownership Gap*, at 33 (Oct. 2019), https://www.urban.org/sites/default/files/publication/101160/explaining_the_black-white_homeownership_gap_a_closer_look_at_disparities_across_local_markets_0.pdf (finding that the GSEs’ portfolio share of loans to Black borrowers has remained well below 5 percent of total mortgage acquisitions despite several decades of housing goals).

We Support Lowering the Total Amount of Capital Required

We support the proposed rule's changes that would lower the total amount of capital required, and encourage FHFA to consider additional analysis regarding whether the amount could be safely lowered even further. Some research has shown that both the current rule and the proposed rule result in requiring a total amount of capital that is unnecessarily high.¹⁰ Accordingly, the proposed rule may still run counter to the public mission established in the charters of the GSEs and may harm access to credit by unnecessarily raising costs, particularly for borrowers of color.¹¹ As stated in a previous comment letter, unnecessarily high capital levels “run directly contrary to the GSEs’ charter mission to promote access to mortgage credit to underserved borrowers, to serve a countercyclical role in the mortgage market, and to FHFA’s duty to reasonably support the safety and soundness of the GSEs and U.S. housing finance system.”¹²

We Encourage Additional Analysis of the Prescribed Leverage Buffer Amount

We would encourage FHFA to consider further lowering the proposed prescribed leverage buffer amount (“PLBA” or “Leverage Buffer”) and conducting additional analysis to determine whether the PLBA should be linked to the stability capital buffer.¹³ The Proposed Rule would replace the current rule’s fixed requirement for a leverage buffer of 1.5 percent of a GSE’s adjusted total assets with a dynamic 50 percent of a GSE’s stability capital buffer, which is determined annually.¹⁴ This approach removes the requirement for an ineffective and unnecessarily high buffer. Under the current rule (based on a fixed amount), the leverage buffer is so high that it is almost always higher than the risk-based calculation, making the risk-based capital requirement nearly irrelevant.¹⁵ However, under the Proposed Rule, the leverage buffer would function as a backstop to a risk-based capital system, should the risk-based system fail to reflect significant risks. According to FHFA, this means that Fannie Mae’s leverage buffer would decrease from approximately \$62 billion to \$23 billion, and Freddie Mac’s leverage buffer would similarly

¹⁰ See, e.g., Don Layton, *Newly-Proposed Changes to the GSE Capital Rule Will Eliminate Harmful Distortions*, Harvard University Joint Center for Housing Studies (Sept. 21, 2021), <https://www.jchs.harvard.edu/blog/newly-proposed-changes-gse-capital-rule-will-eliminate-harmful-distortions> (estimating that the current rule results in the GSEs retaining about \$283 billion in total capital and the proposed rule results in requiring about \$250 billion, whereas a better target would be the \$150-\$175 billion range).

¹¹ See, e.g., Freddie Mac, *Comment Letter to FHFA regarding the Proposed Rule for the Enterprise Regulatory Capital Framework* (Aug. 28, 2020) (stating that the current rule may require Freddie Mac to increase guarantee fees by 15-35 basis points, which may increase housing costs for U.S. consumers).

¹² Center for Responsible Lending et al., *Comment to the Federal Housing Finance Agency on the Enterprise Regulatory Capital Framework* (Aug. 31, 2020), <https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-comment-gse-capital-rule-31aug20.pdf>.

¹³ A “leverage buffer” is an additional threshold that a GSE must meet in order to avoid limits on capital distributions and discretionary bonus payments. It is intended to act as a supplementary measure and credible backstop to a risk-based capital requirement. See FHFA, *Proposed Rule regarding the Enterprise Regulatory Capital Framework*, 85 Fed. Reg. 39274, 39301 (June 30, 2020).

¹⁴ Proposed 12 C.F.R. § 1240.11(a)(6).

¹⁵ See, Don Layton, *Newly-Proposed Changes to the GSE Capital Rule Will Eliminate Harmful Distortions*, Harvard University Joint Center for Housing Studies (Sept. 21, 2021), <https://www.jchs.harvard.edu/blog/newly-proposed-changes-gse-capital-rule-will-eliminate-harmful-distortions>

decrease from approximately \$46 billion to \$11 billion.¹⁶ Notably, this approach also reduces the incentives to hold high-risk assets, thereby decreasing the risk to the American taxpayer.¹⁷ The current system creates incentives to simply buy and hold high-risk assets. However, we encourage FHFA to conduct further analysis to ascertain whether the proposed PLBA is unnecessary given the leverage capital requirement of 2.5 percent of a GSE's total adjusted assets. We also suggest, should FHFA deem the PLBA to be necessary, considering the feasibility of tying the PLBA to a GSE's total adjusted assets as this might be a sounder approach and would not penalize the GSEs for performing their appropriate countercyclical role.

We Support the Changes to the Credit Risk Transfer Transactions

We support FHFA's proposed changes to Credit Risk Transfer ("CRT") transactions.¹⁸ The Proposed Rule would replace the prudential floor of 10 percent on the risk weight assigned to any retained CRT exposure with a prudential floor of 5 percent.¹⁹ The Proposed Rule would also remove the requirement that a GSE apply an overall effectiveness adjustment to its retained CRT exposure.²⁰ As FHFA notes, these two changes would encourage the GSEs to appropriately engage in CRTs and could lead to a significant increase in capital relief.²¹ The current rule has been broadly criticized for discouraging the GSEs from transferring risk across the system and providing the GSEs with strong incentives to hold on to their risk, thereby increasing the exposure to the American taxpayer.²² This proposal removes the market distortion and provides appropriate incentives for the transfer of risk.

We also support the Proposed Rule's emphasis on back-end CRT transactions. In back-end credit transfer structures, the GSEs pay the private entities for taking on the credit risk. Back-end credit risk structures allow for the pooling of loans and risk. By comparison, front-end CRT transactions incentivize segmentation of borrower pricing, such as by credit score, which has the potential to limit access to credit and, as a consequence, undermine the mission of the GSEs to increase liquidity in the market, especially for underserved populations. The emphasis on

¹⁶ Proposed Rule, 86 Fed. Reg. 53237.

¹⁷ Proposed Rule, 86 Fed. Reg. 53238.

¹⁸ The GSEs established the CRT program in 2013. The program is primarily used by the GSEs to transfer credit risk on 30-year fixed-rate mortgages with original loan-to-value ratios of over 60% to global investors. See Laurie Goodman, Jim Parrot, Bob Ryan, and Mark Zandi, *FHFA's Confused Critique of Fannie and Freddie's Transfer of Credit Risk*, Urban Institute (June 2021), https://www.urban.org/sites/default/files/publication/104381/fhfas-confused-critique-of-fannie-and-freddies-transfer-of-credit-risk_0.pdf.

¹⁹ Proposed 12 C.F.R. § 1240.44.

²⁰ *Id.*

²¹ Proposed Rule, 86 Fed. Reg. 53239.

²² See, e.g., Don Layton, *Newly-Proposed Changes to the GSE Capital Rule Will Eliminate Harmful Distortions*, Harvard University Joint Center for Housing Studies (Sept. 21, 2021), <https://www.jchs.harvard.edu/blog/newly-proposed-changes-gse-capital-rule-will-eliminate-harmful-distortions>; Laurie Goodman, Jim Parrot, Bob Ryan, and Mark Zandi, *FHFA's Confused Critique of Fannie and Freddie's Transfer of Credit Risk*, Urban Institute (June 2021), https://www.urban.org/sites/default/files/publication/104381/fhfas-confused-critique-of-fannie-and-freddies-transfer-of-credit-risk_0.pdf; Center for Responsible Lending et al., *Comment to the Federal Housing Finance Agency on the Enterprise Regulatory Capital Framework* (Aug. 31, 2020), <https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-comment-gse-capital-rule-31aug20.pdf>.

back-end CRT transactions makes it more likely that creditworthy families of modest means can afford a mortgage.²³

We Continue to Urge FHFA to Eliminate LLPAs and to Promote a More Equitable Housing Finance Market

Although Loan Level Pricing Adjustments (“LLPAs”) are not directly addressed in the Proposed Rule, they do represent a key component of the GSEs’ current approach to raising capital and managing financial risk. LLPAs are based on certain attributes of the borrower or the loans, including credit score and loan-to-value ratio.²⁴ Because borrowers of color tend to have less wealth to apply to a down payment due to exclusionary federal housing policies, this type of pricing scheme tends to have a disparate impact on them.²⁵ Moreover, borrowers of color are disproportionately impacted by bias in our financial markets and that bias can be reflected in credit scoring systems.²⁶ The combination of two factors that are highly correlated to race as a crude mechanism for determining risk and affixing price has discriminatory impacts²⁷. Accordingly, this LLPA pricing framework is inherently unfair as it places the burden of the GSEs’ financial recovery and future catastrophic risk on Black, Latino, Asian American and Pacific Islander, and Native American borrowers, even though they were the victims of the financial crisis, not the cause.²⁸ The failures of regulators, the GSEs, and lenders to identify risk and prevent foreclosures -- even after repeated warnings from civil rights and consumer advocates -- should not fall on the shoulders of the borrowers most burdened by the financial fallout and historic and current structural discrimination produced by federal housing policies and private market bad actors. LLPAs are not necessary for safety and soundness reasons or to

²³ See Center for Responsible Lending et al., *Comment to the Federal Housing Finance Agency on the Enterprise Capital Requirements* at 33-34 (Nov. 16, 2018), https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl_fhfa_capitalrequirements-nov2018.pdf.

²⁴ See, e.g., Fannie Mae Risk, *LLPA Matrix*, <https://singlefamily.fanniemae.com/media/9391/display>.

²⁵ See Nikitra Bailey, Tucker Bartlett, Mike Calhoun, Keith Corbett, Debby Goldberg, Deborah Momsen-Hudson, Lisa Rice, and Eric Stein, *First Generation: Criteria for a Targeted Down Payment Assistance Program*, *National Fair Housing Alliance and Center for Responsible Lending* (May 21, 2021), <https://nationalfairhousing.org/wp-content/uploads/2021/06/crl-nfha-first-generation-jun21.pdf>.

²⁶ See Missing Credit: How the U.S. Credit System Restricts Access to Consumers of Color, Hearing before the U.S. House Committee on Financial Services, *Testimony of Lisa Rice, President and CEO, National Fair Housing Alliance* (Feb. 26, 2019), <https://financialservices.house.gov/uploadedfiles/hhrg-116-ba00-wstate-ricel-20190226.pdf>.

²⁷ See Civil Rights and Consumer Protection Groups, *Comment in Response to FHFA’s Policy Statement on Fair Lending*, https://nationalfairhousing.org/wp-content/uploads/2021/09/NFHA-et-al-Comment-on-FHFA-Policy-Statement-on-Fair-Lending_FINAL_2021-09-07.pdf.

²⁸ See Michelle Aronowitz, Edward L. Golding, and Jung Hyun Choi, *The Unequal Costs of Black Homeownership* (Oct. 1, 2020), <https://gcfp.mit.edu/wp-content/uploads/2020/10/Mortgage-Cost-for-Black-Homeowners-10.1.pdf>. See John Griffith, *Seven Things You Need to Know about Fannie Mae and Freddie Mac*, Center for American Progress (Sept. 6, 2012), <https://www.americanprogress.org/issues/economy/reports/2012/09/06/36736/7-things-you-need-to-know-about-fannie-mae-and-freddie-mac/>; Sustainable Housing Finance: Private Sector Perspectives on Housing Finance Reform, Hearing before the Subcommittee on Housing and Insurance, U.S. House Committee on Financial Services, *Testimony of Nikitra Bailey, Executive Vice President, Center for Responsible Lending* (Oct. 25, 2017), <https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-bailey-remarks-written-hfs-c-subcommittee-housinginsurance-oct2017.pdf>.

recoup the GSEs' lost capital. Now that the GSEs have fully repaid the government for the 2008 bailout, FHFA should eliminate the LLPAs as they are a barrier that unnecessarily and unfairly increases the cost of homeownership for communities of color.

Notably, the LLPAs create an unfair burden on communities of color, while other recent housing policies disproportionately benefit wealthier, White homeowners, which has further exacerbated the homeownership and wealth gaps. Since the start of the COVID-19 pandemic, the Federal Reserve Board's \$120 billion in monthly bond purchases, including \$40 billion per month in agency mortgage-backed securities, has allowed current homeowners to see their home equity grow by more than \$2.9 trillion dollars since the second quarter of 2020.²⁹ Additionally, the Federal Reserve's actions to mitigate the economic impacts of COVID-19 resulted in lowering the federal funds rate, which helped mortgage interest rates remain at historic lows and stimulated home purchasing and refinancing. However, Federal Reserve researchers found that these benefits did not benefit the whole housing market equally.³⁰ The analysis showed that the median Black and Latino mortgage borrowers accumulated significantly less equity. Moreover, only six percent of Black borrowers and nine percent of Latino borrowers refinanced, as compared to 12 percent of White borrowers.

Given these continued disparities in the housing finance market and the statutory mandates, FHFA's Proposed Rule should not allow the GSEs to emerge from conservatorship with the existing low levels of loan purchases to borrowers of color, even though the Federal Reserve's support caused the GSEs' balance sheets to expand considerably. Ensuring a fair and equitable national housing finance market is consistent with FHFA's obligation to Affirmatively Further Fair Housing³¹ and also makes good business sense. The demographics of the nation are undergoing a dramatic shift and the majority of new households formed over the next decade will be households of color.³² In other words, future housing demand will be driven by people of color. A robust housing market, both for new homebuyers seeking to purchase homes and for existing homeowners seeking to refinance or sell their homes, cannot exist in the absence of access to mortgage credit on fair and equitable terms for all creditworthy borrowers.

²⁹ See CoreLogic, *Homeowners Gained \$2.9 Trillion in Equity in Q2 2021*, CoreLogic Reports, (Sept. 23, 2021) <https://www.corelogic.com/press-releases/homeowners-gained-2-9-trillion-in-equity-in-q2-2021-corelogic-reports/>.

³⁰ Kristopher Gerardi, Lauren Lambie-Hanson, and Paul Willen, *Racial Differences in Mortgage Refinancing, Distress, and Housing Wealth Accumulation during COVID-19*, Federal Reserve Banks of Atlanta, Philadelphia, and Boston (June 2021), <https://www.atlantafed.org/-/media/documents/research/publications/policy-hub/2021/06/22/06-racial-differences-in-mortgage-refinancing.pdf>.

³¹ See the Fair Housing Act, 42 U.S.C. § 3608(d).

³² See Laurie Goodman and Jun Zhu, *The Future of Headship and Homeownership*, Urban Institute (Jan. 2021), <https://www.urban.org/sites/default/files/publication/103501/the-future-of-headship-and-homeownership.pdf> (estimating that between 2020 and 2040, there will be 6.9 million net new homeowners comprised of 4.8 million more Latino homeowners, 2.7 million more Asian and other homeowners, and 1.2 million more Black homeowners but 1.8 million fewer White homeowners); Janie Boschma, et al., *Census Release Shows America Is More Diverse and More Multiracial Than Ever*, CNN (Aug. 12, 2021), <https://www.cnn.com/2021/08/12/politics/us-census-2020-data/index.html>.

Thank you for considering our views. If you have any questions, please contact Nikitra Bailey, Senior Vice President of Public Policy (nbailey@nationalfairhousing.org), or Maureen Yap, Senior Counsel (myap@nationalfairhousing.org), at the National Fair Housing Alliance.

Sincerely,

Asian Real Estate Association of America
Color of Change
Leadership Conference on Civil and Human Rights
Long Island Housing Services, Inc.
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National Association for Latino Community Asset Builders
National Association of Real Estate Brokers
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National Consumer Law Center (on behalf of its low-income clients)
National Fair Housing Alliance
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