Written Testimony of Sandra L. Thompson
Director
Federal Housing Finance Agency

Before the U.S. House of Representatives
Committee on Financial Services
"FHFA Oversight: Protecting Homeowners and Taxpayers"

May 23, 2023

Chairman McHenry, Ranking Member Waters, and distinguished members of the Committee, thank you for the invitation to appear at today's hearing.

Congress established the Federal Housing Finance Agency (FHFA or Agency) to protect the safety and soundness of the housing finance system and promote affordable and sustainable access to mortgage credit nationwide through the regulation and supervision of our regulated entities—Fannie Mae, Freddie Mac (together, the Enterprises), and the Federal Home Loan Bank System, which includes the 11 Federal Home Loan Banks (FHLBanks) and the Office of Finance. Together, the Enterprises and the FHLBank System provide more than $8.6 trillion in funding for the U.S. mortgage markets and financial institutions and perform a vital function in the American economy by providing liquidity and stability to the secondary mortgage market.

Housing affordability challenges present significant barriers throughout the country to both renters and those seeking to purchase a home. House prices have soared in recent years and mortgage rates have climbed well above their prior historic lows. The unusually low supply of homes for sale has exacerbated affordability issues, which disproportionately impact creditworthy potential first-time homebuyers who are struggling to achieve homeownership and who often lack the resources to make a large down payment.

While FHFA cannot directly control these dynamics, the Agency and its regulated entities are addressing these challenges, in part, by focusing on ways to responsibly reduce costs, harness technology and innovation to improve underwriting, and support efforts to increase housing supply.

As regulator and, in the case of the Enterprises, conservator, FHFA ensures that each of these steps is undertaken in a manner that furthers the safety and soundness of the regulated entities. FHFA examiners monitor a variety of risks across business lines, products, and other areas in which the regulated entities engage. FHFA's regulations set requirements related to prudential standards, market activities, and corporate governance. The Enterprises have continued to build

capital and now maintain a combined net worth above $100 billion. FHFA also requires the Enterprises to engage in stress testing to better ensure they can withstand market shocks.

More broadly, the safety and soundness of the regulated entities is a key component of all policy decisions and other actions taken by FHFA. Neither FHFA nor the Enterprises and the FHLBank System can achieve their missions without a continued and unwavering focus on safety and soundness. As we learned during the Great Recession, it is damaging to put a borrower in a home if they will not be able to stay in the home.

My testimony includes updates on a number of critical issues advanced by FHFA since I last appeared before this Committee. Among the issues discussed in greater detail below are FHFA's updates to the Enterprises' single-family pricing framework, notably including the upfront fees charged by the Enterprises. As Representative Cleaver rightly pointed out at last week's subcommittee hearing on this topic, housing finance is a complex issue and the pricing grids underpinning this framework are not easily digestible.

Unfortunately, certain media reports have distorted basic facts by painting an incomplete and misleading picture of these pricing updates. These media reports often make the fundamental mistake of assuming that the pricing grids previously in place were perfectly aligned with the risks faced by the Enterprises. I would like to dispel that myth: in fact, the pricing grids in effect prior to these updates had not been updated in many years and were not fully reflective of the capital framework with which the Enterprises are required to comply.

I want to be very clear on one key point, and one that bears repeating: under the new pricing framework, borrowers with strong credit profiles are not being penalized to benefit borrowers with weaker credit profiles. That is simply not true.

Moreover, the Enterprises by law cannot purchase a loan with a loan-to-value (LTV) ratio greater than 80 percent unless there is an approved level and type of credit enhancement. In most cases, this credit enhancement takes the form of mortgage insurance (MI) provided commercially by private insurers. Borrowers pay for this insurance in addition to the guarantee fees that are passed on to them. If the borrower defaults on their mortgage, the MI provider absorbs the first loss, which limits overall losses for the Enterprises. In this way, MI protects the Enterprises from credit risk by transferring first loss risk to the private sector. The Enterprises' capital requirements include recognition for loans with MI to reflect lower exposure to unexpected losses. This dynamic is also reflected in the Enterprises' pricing framework. MI costs must be added to the guarantee fees charged by the Enterprises to fully understand the costs borne by the borrower. Factoring in MI costs and risk transfer is critical to the fee calculation.

Any narratives that ignore these simple facts are harmful to borrowers who could misunderstand the steps they should take to best position themselves for homeownership. The purchase of a home is a complicated transaction, and homebuyers should have accurate information to make the best decisions possible.

Given the admittedly complex nature of the pricing grids, it is important to offer some context so that the general public can better understand the changes FHFA made to the outdated pricing

grids. FHFA updated the Enterprises' pricing framework to both help creditworthy first-time homebuyers limited by income and wealth and to enhance safety and soundness by better aligning upfront fees with the risk exposures and the capital required to be held against these exposures. The updated pricing framework will enable the Enterprises to continue building capital, thereby reducing the risk to taxpayers who have borne the financial burden of supporting them since they were placed into conservatorship in 2008.

In fact, the updated pricing framework accomplishes both of the objectives highlighted in the title of today's hearing. First, the updated pricing framework supports American homeowners by eliminating the upfront fees for many creditworthy borrowers—first-time homebuyers with lower incomes, for example—and does so by increasing the fees on products that are less central to homeownership, such as second homes or vacation homes. These targeted changes promote homeownership that is both attainable and sustainable. Second, the updated pricing framework enables the Enterprises, both of which are taxpayer-supported, to build capital in a safe and sound manner.

The Committee's focus on protecting American homeowners and taxpayers is important for another reason. Housing comprises 16 percent of U.S. gross domestic product. And for most Americans, their home is their largest asset, and homeownership is the primary way in which families build wealth and pass it on to their children and grandchildren. The updated and improved pricing framework makes homeownership more attainable for creditworthy first-time homebuyers, which strengthens communities.

In addition to the updated Enterprise pricing framework, FHFA has announced a series of important initiatives since I last appeared before this Committee in July 2022 that I would like to highlight. These actions are consistent with FHFA's statutory mission of ensuring the safety and soundness of the regulated entities and promoting access to affordable and sustainable housing, including for first-time homebuyers and underserved communities.

Federal Home Loan Bank System at 100: Focusing on the Future

On August 31, 2022, FHFA announced the launch of a comprehensive review of the Federal Home Loan Bank System (the System). The purpose of the review was to ensure the FHLBanks remain positioned to meet the needs of the communities they serve—today and well into the future. FHFA began the review with no pre-determined outcomes and encouraged all stakeholders to participate in a robust public engagement process.

The project began with a three-day listening session followed by 19 regional roundtable discussions and, most recently, a wrap-up listening session. FHFA concluded the public input phase of the review earlier this year and is now working on a report, expected to be published in the second half of the year, which will summarize the feedback received and detail the Agency's recommendations.

FHFA asked for public feedback on a range of topics, including the mission and purpose of the System, the efficiency of its organization and operations, and its effectiveness in supporting affordable, sustainable, and equitable housing. In addition, we examined the System's role in

community and economic development, including addressing the unique needs of rural and financially vulnerable communities. Finally, we looked at the System's member products, services, and collateral requirements, as well as its membership eligibility requirements.

FHFA is still analyzing the feedback received, but I am happy to share some recurring themes heard throughout the public engagement portion of the review. Overall, FHFA heard that the System has been a stable and reliable source of liquidity for housing finance for its member institutions. Many stakeholders noted that the System has been serving this function well for the past 90 years, particularly for smaller members and during times of market stress.

This was made clear earlier this spring during a period of heightened volatility in the banking sector, when the FHLBanks provided a record amount of advances to ensure their members had the liquidity they needed in an uncertain market. To support this demand for advances, the System issued more debt than it has ever issued in a single day. Through this period of market stress, the FHLBanks remained in a safe and sound condition and continued to serve their critical role. The System's resiliency in the face of significant market volatility showed the effectiveness of the standards FHFA established for the FHLBanks to ensure they are appropriately prepared for stress events.

The FHLBanks also have the responsibility to support affordable, sustainable, resilient, and equitable housing and economic development, especially in underserved and financially vulnerable communities, including rural areas, tribal areas, and communities of color.

FHFA has received valuable feedback on how a number of FHLBank initiatives could be made more effective. Numerous responses focused on the FHLBanks' affordable housing and community investment programs, and the need for the FHLBanks and their members to conduct outreach efforts to ensure those who could benefit from the System's programs and products have greater awareness of these offerings. Some stakeholders also noted a need to clarify the mission and purpose of the FHLBanks.

This review has been an in-depth and far-reaching initiative, and FHFA is now in the process of analyzing these and other suggestions and preparing our report for publication later this year.

Credit Score Model Validation and Approval

When I last appeared before the Committee, I highlighted that FHFA supports the use of fair and accurate credit score models by the Enterprises, and that we were actively reviewing credit score models along with the Enterprises pursuant to the solicitation and approval process set forth by the law and our regulations. Last year, FHFA advanced two changes that I would like to note.

On October 24, 2022, FHFA announced the validation and approval of both the FICO 10T and the VantageScore 4.0 credit score models for use by the Enterprises. This policy represents an update to the use of the Classic FICO model, which the Enterprises have required for nearly 30 years. At the same time, FHFA also announced that the Enterprises will require two, rather than three, credit reports from the national consumer reporting agencies. These changes are expected to reduce costs and encourage innovation, without introducing additional risk to the Enterprises.

FHFA expects a multiyear transition, as credit scores interface with many elements of the mortgage ecosystem, including loan application and underwriting, risk management, capital, pricing, mortgage insurance, and investor disclosures, and many different stakeholders will be impacted, including borrowers, lenders, mortgage insurers, technology service providers, and investors.

The validation and approval of FICO 10T and VantageScore 4.0 was the result of a thorough and publicly inclusive effort which began in 2014 and followed legislation enacted in 2018 that required FHFA to create a process for validating and approving credit score models.

As a result of FHFA's announcement, borrowers, lenders, investors, and other stakeholders can expect:

- *More accurate credit scores*. The evaluation of new credit score models included extensive testing by the Enterprises to ensure that any validated and approved models met the necessary accuracy standards that are expected for widespread use in the market. Both FICO 10T and VantageScore 4.0 met those standards.
- *More inclusive credit scores*. While both Enterprises have already taken steps to expand equitable access to credit for those borrowers lacking extensive credit histories, such as through enhancements to their underwriting systems, both FICO 10T and VantageScore 4.0 include new payment history information such as rent, utilities, and telecommunications payments when available.
- *Enhanced safety and soundness in the housing finance system*. Promoting accuracy and innovation in credit score models will ultimately lead to better outcomes for borrowers, lenders, investors, insurers, guarantors, and the Enterprises. Additionally, because both FICO 10T and VantageScore 4.0 are more accurate than Classic FICO, the mortgage market will be provided with an improved view of risk from two different credit score models.
- *Sufficient time to transition*. FHFA and the Enterprises anticipate a multiyear transition and are committed to working with stakeholders to ensure a smooth process towards the use of the new credit score models and the new credit report requirements in a manner that avoids unnecessary costs and complexity. The transition timeline must be flexible enough to incorporate testing and unexpected events, but also efficient enough to ensure that consumers, the Enterprises, and others benefit from the more accurate credit score models.

Additionally, on March 23, 2023, FHFA announced proposed implementation timelines for the use of FICO 10T and VantageScore 4.0 and for the Enterprises' requirement to transition to a bi-merge credit report requirement. This announcement marked the beginning of a public engagement process to inform these changes and timelines. The public engagement process will allow stakeholders to provide critical feedback and input on the implementation process and to work with FHFA and the Enterprises to further refine the proposed implementation plan.

Prior Approval for Enterprise Products

The Enterprises, while continuing to serve their public missions, may seek out technological advances and pursue innovations to create opportunities to provide the public, the Enterprises' counterparties, and the market more access to, and options for, new products. However, in doing so the Enterprises may be exposed to additional risks or could alter the risks faced by other market participants, and the impact on achieving their missions should be carefully balanced against the risks that are introduced by any new activity or product.

On December 20, 2022, FHFA published a final rule that requires the Enterprises to provide advance notice to FHFA of new activities and obtain prior approval before launching new products. The rule was enacted after extensive public engagement. To facilitate implementation, the rule defines "activity" and clarifies which categories of activities would be considered to be "new." The rule establishes that FHFA will determine which new activities merit public notice and comment, and therefore should be treated as new products and subject to prior approval. In addition, the rule establishes a public disclosure requirement for FHFA to publish its determinations on new activity and new product submissions. The rule took effect on April 28, 2023.

This process will promote safety and soundness as well as transparency, while balancing the importance of innovation with the need to ensure the Enterprises' actions remain consistent with their charters and the public interest.

Updates to the Enterprises' Single-Family Pricing Framework

As I discussed earlier, FHFA is first and foremost a safety and soundness regulator, and the Enterprises were chartered by Congress with a mission to support liquidity, stability, and affordability by facilitating responsible access to mortgage credit through their activities in the secondary market. To achieve this mission, the Enterprises charge fees to compensate them for guaranteeing securities collateralized by the mortgages they acquire, which in turn attracts investors across the globe to provide liquidity for the U.S. mortgage market and, ultimately, reduces interest rates for homeowners.

Since 2008, a portion of the Enterprises' single-family guarantee fees have been "upfront" fees that are based on risk characteristics of the borrowers and the loan and property attributes. Accordingly, the Enterprises engage in risk-based pricing to, among other things, better ensure their safety and soundness, protect taxpayers, and serve their missions.

As required by law, FHFA publishes an annual Guarantee Fee Report which analyzes the guarantee fees charged by the Enterprises, including the average guarantee fee by year. The report also provides detailed information on guarantee fees by product type, loan purpose, LTV ratio, borrower credit score, and seller size. The most recent report includes a timeline of changes to guarantee fees spanning the period from 2008 to 2021 (see Table 1). Taken together, this information provides additional transparency to the public regarding the level and structure of the guarantee fees charged by the Enterprises.

Table 1: Timeline of Changes in Guarantee Fees from 2008 to 2021

Date	Change
March 2008	The Enterprises increased ongoing fees and added two new upfront fees: a fee based on the borrower's LTV ratio and credit score, and a 25-basis point adverse market fee.
Late 2008 through 2011	The Enterprises gradually raised fees and refined their upfront fee schedules.
December 2011	Pursuant to the Temporary Payroll Tax Cut Continuation Act of 2011, FHFA directed the Enterprises to increase the ongoing fee for all loans by 10 basis points. The Enterprises pay this fee to the U.S. Department of the Treasury. This fee increase was effective with April 2012 deliveries and was set to expire after 10 years.
August 2012	FHFA directed the Enterprises to raise fees by an additional 10 basis points on average to better compensate for credit risk exposure. FHFA raised fees more on loans with terms longer than 15 years than on shorter-term loans to better align the gaps and made fees more uniform across sellers with varying loan delivery volumes. These changes were effective with December 2012 MBS deliveries.
December 2013	FHFA directed the Enterprises to increase ongoing fees by 10 basis points, change upfront fees to better align pricing with credit risk characteristics, and remove the 25-basis point adverse market fee for all but four states. However, in January 2014, FHFA suspended the implementation of these changes pending review.
April 2015	FHFA completed its fee review and directed the Enterprises to eliminate the adverse market fee in all markets and add targeted increases for specific loan groups effective with September 2015 deliveries. These changes were approximately revenue-neutral with little or no impact for most borrowers.
July 2016	Based on findings from FHFA's quarterly guarantee fee reviews, the Agency directed the Enterprises to set minimum ongoing guarantee fees by product type, effective in November 2016, consistent with FHFA's responsibility to ensure the safety and soundness of the Enterprises.
September 2018 & March 2019	The Enterprises implemented a 25-basis point upfront fee for loans on second homes where LTV exceeds 85 percent.
April 2020	FHFA allowed the Enterprises to purchase loans in forbearance, with an upfront fee add-on of 500 basis points for first-time home buyers and 700 basis points for all others, effective for loans closed through December 31, 2020, following multiple extensions.
August 2020	FHFA directed the Enterprises to introduce a 50-basis point upfront adverse market refinance fee, effective December 1, 2020, for cash-out and rate-term refinances. The Enterprises excluded loans with principal balance less than or equal to $125,000, those associated with HomeReady/Home Possible, and construction-to-permanent loans meeting certain criteria.
July 2021	FHFA announced that the Enterprises would eliminate the adverse market refinance fee for loan deliveries effective August 1, 2021.

November 2021	The Infrastructure Investment and Jobs Act extended to 2032 the existing 10-basis point ongoing fee arising from the Temporary Payroll Tax Cut Continuation Act of 2011, which was due to expire in 2022. The Enterprises remit the proceeds from this fee to the U.S. Department of the Treasury.

It has been over eight years since FHFA undertook a comprehensive review of the Enterprises' pricing framework, and since that time, FHFA adopted and implemented a new capital regulation for the Enterprises—the Enterprise Regulatory Capital Framework (ERCF). Much of the updated pricing framework, as discussed below, is calibrated to the ERCF to help ensure that the Enterprises' capital requirements and pricing framework are more closely aligned.

For over a year, FHFA, as conservator of the Enterprises, has been conducting a holistic review of the Enterprises' guarantee fee pricing framework with a special focus on upfront fees. FHFA's objectives in updating the framework were expressed in both the 2022 and 2023 Conservatorship Scorecards for Fannie Mae, Freddie Mac, and Common Securitization Solutions. These objectives include increasing pricing support for many creditworthy first-time homebuyers, while ensuring a level playing field for small and large lenders, fostering capital accumulation at the Enterprises, and achieving viable returns on capital over time, which combine to help protect taxpayers.

FHFA, as conservator, has taken a series of steps since January 2022 to accomplish these goals. First, FHFA announced targeted fee increases for second and vacation home loans, high-balance loans, and, later, cash-out refinances. Next, FHFA announced the elimination of upfront fees for many creditworthy low- and moderate-income first-time homebuyers, as well as certain borrowers purchasing homes in rural communities or purchasing manufactured housing. While many loans made through the Enterprises' flagship affordable mortgage programs (HomeReady and Home Possible) already had zero upfront guarantee fees, upfront fees were fully eliminated for the following borrowers and programs:

- first-time homebuyers at or below 100 percent of area median income (AMI) in most of the United States and below 120 percent of AMI in high cost areas;
- HomeReady and Home Possible loans;
- HFA Preferred and HFA Advantage loans; and
- single-family loans supporting the Duty to Serve program.

These fee eliminations were primarily offset by the increased fees on second and vacation home loans, high-balance loans, and cash-out refinances.

In January 2023, FHFA announced a recalibration of the upfront fees for most purchase and rate-term refinance loans. The updated fee matrices increased transparency by separating the base grids across three loan purposes (i.e., purchase loans, rate-term refinance loans, and cash-out refinance loans), rather than combining purchase and rate-term refinance loans, as was the case with the prior grids. The redesigned matrices also further refined the credit score distribution to include more granular categories at the upper end of the spectrum (i.e., providing more

categories than the prior grids, in which all borrowers with a credit score of 740 or greater were grouped together). These changes better reflect the risks associated with various types of loans acquired by the Enterprises.

To ensure mortgage pipelines were not impacted, these updated fees took effect for loan deliveries to the Enterprises beginning on May 1, 2023. Notably, this means that most lenders began implementing these updated fees into the pricing offered to borrowers months earlier to ensure they delivered closed loans that aligned with the new framework by May 1, 2023.

A substantial part of the January 2023 fee recalibration is to align fees with the ERCF. As was noted in the Agency's 2022 Annual Guarantee Fee Report and in the request for input (RFI) on the Enterprises' single-family pricing framework published on May 15, 2023, the transition to the ERCF changed capital requirements across credit characteristics. The flatter risk gradients embedded in ERCF result in a lower and flatter return profile across the credit risk spectrum. Several features of the ERCF, including a minimum risk-weight floor for all mortgage exposures, and risk-insensitive capital buffers for stability, stress, and leverage, are applied evenly across all loans acquired by the Enterprises and thereby set a higher minimum level of capital that must be held against these loans.[1] This dynamic results in loans with stronger credit characteristics receiving more significant capital increases than loans with weaker credit characteristics, relative to the prior proposed capital requirements. This, in turn, impacts the return-on-capital targets set by FHFA for the Enterprises and served as the basis for much of the recalibration in the January 2023 updates.

On April 25, 2023, FHFA issued a public statement in response to several misconceptions that had been reported in certain media coverage of these updates. In this statement, FHFA made clear that no borrowers are being charged higher upfront fees based on their credit score in order to allow other borrowers to be charged lower upfront fees based on their credit score. The recalibrated upfront fees announced in January 2023 were set based on the capital required by the ERCF (as well as the return-on-capital thresholds set by FHFA), which in turn is predicated on the expected financial performance of each category of loan. Further, FHFA clarified that there is no incentive for borrowers to seek a lower credit score due to the updated fee structure. Risk-based pricing remains in effect, and the upfront fees are now more closely aligned with the return-on-capital targets set by FHFA.

Similarly, there is no incentive for borrowers to make a smaller down payment as a result of the new fee structure. The Enterprises' congressional charters require credit enhancement—primarily in the form of private MI—for loans with a down payment of less than 20 percent. As discussed earlier, this MI coverage absorbs first losses and reduces the total loss exposure of the Enterprises because the approved insurance providers bear much of these losses in the event of default. Absent MI, the Enterprises would assume a far greater proportion of the losses associated with defaults on these loans. For borrowers making a down payment smaller than 20

[1] For loans with stronger credit profiles, the presence of a risk-weight floor will generally increase the amount of capital the Enterprises must hold against those loans. In contrast, for loans with weaker credit profiles, the Enterprises generally were already required to hold capital against those loans in excess of that necessitated by the minimum risk weight floor. Therefore, the risk weight floor is more likely to be binding for loans with stronger credit profiles.

percent of the home's value, the costs of the required credit enhancement, such as MI, contribute to the overall cost of their loan. As such, any analysis of guarantee fees without consideration of MI or other credit enhancement costs is incomplete—both from the perspective of the borrower and from the perspective of the Enterprises.

FHFA has continued to engage with stakeholders on specific issues related to the pricing framework to ensure it meets our stated objectives of fostering capital accumulation at the Enterprises, achieving viable returns on capital, and increasing support for creditworthy first-time homebuyers. FHFA received numerous comments, for example, related to operational and other challenges associated with an upfront fee based on a borrower's debt-to-income ratio and subsequently removed the fee on May 10, 2023. In addition, and as noted above, to promote transparency and ensure stakeholders can share their perspectives on a variety of issues related to the Enterprises' pricing framework, FHFA published a public RFI on May 15, 2023.

Since entering conservatorship in 2008, the Enterprises have remained undercapitalized, and taxpayers, through the Treasury Department, continue to provide a financial backstop should the Enterprises confront significant losses. The updated pricing framework will better protect taxpayers in the long term and put the Enterprises on more durable footing, which will allow them to support affordable, sustainable mortgage credit across the economic cycle to the benefit of all Americans. And they will do so with a pricing framework that is more accurately aligned to the expected financial performance and risks of the loans they back.

Enhanced Payment Deferral Policies for Borrowers Facing Financial Hardship

FHFA and the Enterprises are examining lessons learned from the pandemic to inform the existing loss mitigation framework, with the goal of improving the ability of mortgage servicers to assist struggling homeowners in retaining their homes, while minimizing losses to the Enterprises and taxpayers. On March 29, 2023, FHFA announced that the Enterprises would enhance their payment deferral policies to allow borrowers facing financial hardship to defer up to six months of mortgage payments as part of the standard loss mitigation framework. The enhanced payment deferral policies will promote sustainable homeownership and further support the safety and soundness of the Enterprises.

Payment deferral allows borrowers who are able to resolve a temporary financial hardship to retain the same monthly mortgage payment by moving past-due amounts to the end of the loan as a non-interest bearing balance, due and payable at maturity, sale, refinance, or payoff. During the pandemic, the Enterprises' payment deferral policies were expanded to allow borrowers with COVID-19 hardships to utilize this solution.

The Enterprises have successfully completed over 1 million COVID-19 payment deferrals since the onset of the pandemic in March 2020. In addition to its benefits to borrowers, payment deferral has the added benefit of allowing the Enterprises to keep the loans in mortgage-backed securities and mitigating growth to their retained portfolios.

Throughout conservatorship, FHFA and the Enterprises have worked to develop policies to help servicers better resolve mortgage payment delinquencies with the goal of keeping struggling

borrowers in their homes whenever possible, while minimizing losses to the Enterprises and taxpayers. The payment deferral option is another important step towards improving borrower and taxpayer outcomes.

The Enterprises will work with servicers to implement the enhanced payment deferral policies, with a voluntary adoption date of July 1, 2023, and mandatory adoption by October 1, 2023.

Updated Minimum Financial Eligibility Requirements for Enterprise Seller/Servicers

An important tool for counterparty risk management at the Enterprises is the use of minimum financial eligibility requirements for approved seller/servicers. These requirements promote safety and soundness by strengthening the capacity of seller/servicers to meet the financial responsibilities associated with originating and servicing mortgages acquired by the Enterprises.

Beginning with proposed updates in early 2020, FHFA and the Enterprises have been examining the framework for issues related to seller/servicer net worth, capital, and liquidity requirements. This work was further informed by the experience of both the Enterprises and seller/servicers in managing challenges that arose as a result of the COVID-19 pandemic. FHFA has worked closely with Ginnie Mae throughout this process, as many Enterprise seller/servicers are also approved Ginnie Mae issuers.

On August 17, 2022, after multiple rounds of public comment, FHFA and Ginnie Mae jointly announced updates to their respective minimum financial eligibility requirements. These updates improve upon the prior framework by strengthening seller/servicer net worth, capital, and liquidity requirements and better tailoring the minimum requirements associated with different types of loans and risk exposures. Most of the updated requirements for Enterprise seller/servicers will take effect in late 2023.

Equitable Housing Finance Plans and Duty to Serve Update

On April 5, 2023, FHFA announced updates to the Enterprises' Equitable Housing Finance Plans for 2023. The updates build upon the inaugural plans first announced in 2022 and include adjustments based on initial research and findings. The Equitable Housing Finance Plans are designed to complement the initiatives outlined in FHFA's strategic plan that promote the Enterprises' safety and soundness and foster housing finance markets that provide equitable access to affordable and sustainable housing.

FHFA's reason for requiring the Enterprises to develop Equitable Housing Finance Plans is clear. Even after passage of the landmark Fair Housing Act of 1968, the racial homeownership gap persists, with homeownership rates for households of color more than 24 percentage points lower than the rate among white households. Accordingly, the Enterprises developed and published plans to identify and address barriers to sustainable housing opportunities, as well as the Enterprises' goals and actions to advance equity in housing finance, for the next three years.

Updates to the Enterprises' 2022-2024 Plans include, but are not limited to:

- the inclusion of the Latino Housing Journey and actions to remove barriers experienced by Latino renters and homeowners in Fannie Mae's plan;
- an enhanced focus on ensuring existing borrowers receive fair loss mitigation support and outcomes through monitoring and developing strategies to close any gaps;
- the provision of financial capabilities coaching to build credit and savings;
- support for locally-owned modular construction facilities in communities of color; and
- increases to the reach of Enterprise Special Purpose Credit Programs to support homeownership attainment and housing sustainability in underserved communities.

All plan activities are subject to FHFA's review and oversight of any risks to, or impacts on, safety and soundness.

In addition, the Enterprises released performance reports that outline progress made under their Equitable Housing Finance Plans during 2022 and actions they are taking to advance equity in their automated underwriting systems, such as the inclusion of rental payments and cash flow underwriting and the use of advanced statistical techniques to improve model fairness. In total, the Enterprises, through programs associated with their Equitable Housing Finance Plans, have helped more than 834,000 American families.

FHFA also recently released a proposed rule that would codify the process and standards for the Equitable Housing Finance Plans in the future. The proposed rule addresses many of the questions from stakeholders on the initial program, and FHFA welcomes public comments from all stakeholders.

Later this year, FHFA will conduct a public engagement session to build on last year's listening session and request for input. The initial engagement with the public yielded thoughtful responses that were incorporated into the Enterprises' final plans. In future years, I expect the Enterprises will focus on other underrepresented communities, such as Asian American and Pacific Islander communities.

Other issues affect many underserved communities' access to affordable and sustainable housing throughout the country, such as the availability of small balance loans. There is limited access to mortgage credit for small balance loans on modestly priced homes. This is a barrier to homeownership for many Americans, and unfortunately the void is often filled with non-mortgage products that do not offer an affordable and sustainable path to homeownership. It is also a barrier to refinancing in low interest rate environments. The fixed costs associated with a refinancing often make it uneconomical to refinance lower balance loans, even though that opportunity could reduce monthly costs for owners of modestly priced homes. I believe this is an area in which further work is needed to develop solutions that make small balance mortgage loans more affordable and available to support all communities throughout the Nation.

Many challenges to affordable and sustainable homeownership exist for tribal lands in Native American communities throughout the country. These challenges include legal complexities, infrastructure for housing development, and a lack of access to mortgage products, especially

conventional loan products. As a result of these long standing and serious issues, fewer than 1,000 mortgage loans are made annually on tribal lands. Under the Duty to Serve program, the Enterprises are working to develop new solutions to some of these challenges through the expansion of access to conventional loans and the provision of support to Native Community Development Financial Institutions (CDFIs).

Multifamily Market

The multifamily market experienced volatility in 2022 and the first half of 2023, but fundamentals have remained strong. Throughout this period, the Enterprises have continued to serve as a consistent source of liquidity without compromising credit standards. This year, FHFA instructed the Enterprises to develop and implement strategies to support and advance the multifamily market by identifying ways to facilitate greater affordable housing supply, exploring options to expand energy efficiency and resiliency, exploring the feasibility of expanding tenant protections at Enterprise-backed properties, and increasing Enterprise support for workforce housing.

- *Low-Income Housing Tax Credit (LIHTC) program.* One of the primary mechanisms for the Enterprises to create incentives for production and investment in affordable housing is through the LIHTC program. These investments can also support housing in Duty to Serve-designated rural areas, preserve affordable housing, support mixed-income housing, provide supportive housing, or meet other affordable housing objectives. In September 2021, FHFA increased the Fannie Mae and Freddie Mac LIHTC investment caps to $850 million annually. Previously, each Enterprise was limited to $500 million of investments annually. Within this $850 million annual cap, any investments above $425 million in a given year are required to be in areas that have been identified by FHFA as markets that have difficulty attracting investors. LIHTC investments are a meaningful way for the Enterprises to support affordable housing supply. In 2022, both Enterprises were able to fully deploy all allowable LIHTC investment dollars, the majority of which supported transactions that traditionally have difficulty attracting investors.
- *Multifamily loan purchase caps*. In November 2022, FHFA also made several changes to the Enterprises' multifamily housing loan purchase caps for 2023, which are set at $75 billion, for a combined total of $150 billion, to support the multifamily market. To ensure a strong focus on affordable housing and traditionally underserved markets, FHFA requires that at least 50 percent of the Enterprises' multifamily business be mission-driven affordable housing as defined in the Conservatorship Scorecard's Appendix A. FHFA added a new mission-driven category for workforce housing properties to increase Enterprise support of the "missing middle" by providing incentives for multifamily borrowers to voluntarily ensure rents are affordable for those renters at or below 120 percent of AMI. In addition, FHFA will allow loans to finance energy or water efficiency improvements with units affordable at or below 80 percent of AMI to be classified as mission-driven, up from 60 percent of AMI in 2022. This increase will allow the Enterprises to expand their efforts related to energy and water conservation measures at workforce housing properties.

- *Increased multifamily radon testing requirements*. FHFA has also adopted more robust radon testing requirements for multifamily properties backed by the Enterprises. This policy enhancement ensures that properties financed by the Enterprises continue to provide safe and sustainable housing for tenants across the country.
- *Multifamily tenant protections*. FHFA announced that the Agency would conduct a public stakeholder engagement process to identify tangible solutions for addressing the challenges renters are facing nationwide, particularly among underserved communities. FHFA's determination to evaluate the Enterprises' tenant standards is based on lessons learned from the COVID-19 pandemic, rising rents, and a shortage of safe and affordable housing. The Agency has committed to a transparent stakeholder engagement process that includes broad participation from diverse voices. Additionally, FHFA instructed the Enterprises to explore the feasibility of expanding multifamily tenant protections for properties they finance and to identify strategies and activities that could facilitate a greater amount of affordable rental housing supply. FHFA expects to issue an RFI on multifamily tenant protections by the end of this month.

* * *

We at FHFA will continue to focus on our safety and soundness mission and on the mission that Congress gave the entities that FHFA regulates and supervises: providing liquidity for the secondary mortgage market across the Nation, including underserved markets such as rural and tribal areas, manufactured housing, the preservation of affordable housing, and other underserved populations such as communities of color. This mission extends not only to homeownership, but also to affordable rental housing.

Thank you again for the opportunity to testify before you today, and I look forward to working with the Members of this Committee and answering any questions you may have.