

FHFA REO Initiative: RFI Response Summary

FHFA is exploring new approaches to the disposition of foreclosed properties (real estate owned, or REO) owned by Fannie Mae and Freddie Mac (the Enterprises). The Enterprises' REO portfolios are now stable and their individual retail sales are achieving close to fair market values for the properties. But as more nonperforming loans move through the foreclosure process and into REO inventories, we need more disposition strategies.

To launch its REO Initiative, FHFA issued a Request for Information (RFI) to solicit ideas for approaches to help current and future disposition of REOs, improve loss recoveries compared to individual retail REO sales, help stabilize neighborhoods and local home values, and where feasible and appropriate, expand the supply of rental housing. FHFA developed the request in consultation with the U.S. Department of the Treasury and the U.S. Department of Housing and Urban Development, taking into consideration broad government interest in REO disposition, including the disposition of properties owned by the Federal Housing Administration (FHA).

FHFA received comments from a wide range of market participants, stakeholders, community groups and industry observers with specific suggestions for improving market conditions in the disposition of REO properties. Many respondents also demonstrated their technical and financial capability to engage in large-scale transactions with the Enterprises and FHA. The range of respondents reflected widespread interest and numerous affected stakeholders. Respondents included:

- Academics
- Asset Management Companies
- Commercial and Investment Banks
- Data and Analytics Firms
- Developers
- Housing Advocacy Groups
- Nonprofits
- Private Equity Firms
- Private Individuals
- Property Managers
- Real Estate Firms
- Trade Groups

FHFA received more than 4,000 submissions. Of these, approximately 10 percent responded fully to questions posed in the request. FHFA also received numerous business solicitations or brief expressions of personal opinion we did not consider responsive.

Summary of Submissions

Respondents to the RFI offered a range of transaction principles, guidelines, structures, and strategies. These will inform the scope, magnitude, and policy choices FHFA will consider as we continue to develop initial pilot transactions and as the basis for broader programs.

Respondents supported many of the strategies and structures used by the Federal Deposit Insurance Corporation (FDIC) today, and earlier by the Resolution Trust Corporation, to address the savings and loan crisis and dispose of assets of failed savings institutions. Those approaches included joint venture partnerships, outright sales, and auction methods. The Resolution Trust Corporation pioneered these broad-based asset management and disposition strategies to maximize recoveries to taxpayers and other government objectives.

Other respondents recommended that FHFA adopt approaches similar to the Treasury Department's Public-Private Investment Partnership program. That program, which included risk sharing with the U.S. government, involved the use of Treasury financing, along with private equity, to purchase troubled loans from banks.

Finally, some respondents proposed the use of Real Estate Investment Trust (REIT) structures. REIT structures give investors unique tax advantages, support longer term investment capital, and require controls to prevent practices such as property "flipping."

Disposition Strategy Components

The lessons learned from these approaches are numerous, but respondents generally emphasized four primary components the government should consider in any disposition strategy:

- Transaction structure
- Geographic targeting of sales
- Available and low-cost financing
- Importance of oversight and monitoring

Most respondents suggested disposition strategies that involved renting properties for a period of time. Many suggested offering tenants an opportunity to purchase the properties. Some pointed out that, in some cases, demolition is the best option and suggested that properties should be analyzed to determine the relative value of rehabilitation and subsequent sale or rental versus demolition. Respondents also recognized that large scale transactions must include internal and external controls addressing how potential government partners are qualified, how properties are managed with and without tenants, and how to work cooperatively with community groups and nonprofits. While many respondents recommended the Enterprises focus on certain geographic regions, others took a more nationwide approach.

There is also broad agreement that "seller financing" provided or guaranteed by Fannie Mae, Freddie Mac, or the government is likely important to execute large-scale transactions, at least in the early stages of a disposition program. Only a few market participants have developed the necessary infrastructure and capabilities to manage dispersed single-family rental properties. With assurance of a continued flow of new REOs, respondents suggested additional firms will make the necessary investment and develop that capability. Availability of attractive financing will encourage that investment. As more firms develop the capacity to participate, competition will increase, resulting in higher bids and reducing the need for financing assistance. Respondents cite the Resolution Trust Corporation and FDIC experience and indicate that such a feature will expand the investor base.

Nonprofits and Trade Groups

RFI nonprofit respondents included

- national, state, and local affordable housing advocates;
- legal services agencies;
- trade groups representing large public housing authorities and state housing finance agencies;
- environmental advocates;
- city governments; and
- labor unions.

Many emphasized that stabilizing neighborhoods is vital to protecting the interests of taxpayers. They expressed the view that the benefits of neighborhood stabilization must be taken into consideration when analyzing any disposition strategy. In addition, they pointed to community groups' knowledge of individual communities, their track records for successful development, and the importance of using their expertise in any disposition strategy.

Responsive groups suggested a set of principles to broadly govern FHFA's REO dispositions. Comments generally requested that transactions be managed to achieve certain performance metrics. The following principles suggest how a prospective transaction should be managed and monitored over the long term to ensure the achievement of policy objectives:

- 1) **Support neighborhood stabilization.** Document partnership structures to ensure the activities of private investors promote local neighborhood stabilization efforts as they are given greater access to bulk transactions.
- 2) **Ensure responsible ownership.** Manage the entire portfolio of assets over their life cycles and put in place the appropriate controls to ensure buyers with a poor management track record do not have access to REO properties
- 3) **Ensure quality property management.** Establish standards for post acquisition monitoring of properties and ensure that new owners and their vendors have the financial capacity and demonstrated track record to rehabilitate, maintain, and operate properties to a high standard.
- 4) **Facilitate nonprofit participation.** Adopt strategies to integrate nonprofits into the overall asset disposition strategies undertaken by the asset managers and partnerships that acquire the assets.
- 5) **Integrate housing counseling.** Adopt strategies to promote housing counseling for homebuyers and renters in lease-to-own or rental scenarios.
- 6) **Enhance long-term affordability.** Adopt controls that support long-term affordability of properties sold or rented.

Looking Ahead

Based on the input of RFI responders, we understand the magnitude of the task at hand. FHFA is sharing RFI responses with other federal agencies. FHFA is proceeding prudently but with a sense of urgency to lay the groundwork for the development of good initial pilot transactions. FHFA is grateful for the time and effort that so many people put into their responses to the RFI. FHFA's learning from this process will substantially enhance the REO disposition process.