



FannieMae®

2005 Annual Housing Activities Report (AHAR)

March 16, 2006



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March 16, 2006

The Honorable Alphonso Jackson
Secretary
U.S. Department of Housing and Urban Development
451 Seventh Street, SW
Washington, DC 20410-0001

Dear Mr. Secretary:

As required by Fannie Mae's Charter Act,¹ I hereby submit Fannie Mae's 2005 Annual Housing Activities Report (AHAR). In 2004, the Department of Housing and Urban Development ("HUD") established by regulation, new percent of business goal levels for Fannie Mae applicable through 2008. For 2005, the low- and moderate-income housing goal was set at 52 percent of the dwelling units financed by Fannie Mae's mortgage purchases; the central cities, rural areas, and other underserved areas housing goal was set at 37 percent; and the special affordable housing goal at 22 percent. In addition, HUD established a multifamily special affordable housing goal that requires an investment minimum of \$5.49 billion. In 2005, with the help of our partners, Fannie Mae met each of these goals. Of the units we financed, 55.13 percent met the low- and moderate-income goal, 41.39 percent met the underserved goal, and 26.32 percent met the special affordable housing goal. Our total investment in multifamily special affordable housing was \$9.76 billion.

Furthermore, in 2004, HUD's regulation also established three owner-occupied home purchase sub-goals set at a percent of the total number of mortgages purchased by Fannie Mae in metropolitan areas. For 2005, the low- and moderate-income home purchase sub-goal was set at 45 percent; the central cities, rural areas, and other underserved areas home purchase sub-goal was set at 32 percent; and the special affordable home purchase sub-goal at 17 percent. For 2005, Fannie Mae met two of the home purchase sub-goals and fell slightly short on the third. Fannie Mae's home purchase sub-goal performance was as follows: 44.62 percent of our home purchase mortgage purchases served low- and moderate-income families, 32.56 percent of our home purchase mortgage purchases were located in underserved areas, and 17.04 percent of our home purchase mortgage purchases satisfied the special affordable home purchase sub-goal.

We also continue to support President George W. Bush's call to increase minority homeownership rates. Since we pledged to support the President's effort in June 2002 by helping to create homeownership opportunities for 4.6 million minority households through 2009, Fannie Mae has provided home financing to 3.9 million minority families.

¹ 12 U.S.C. § 1723a(n)

The AHAR includes several data tables, in the format specified by HUD, that provide information about each goal and our performance under each goal and subgoal. Included in the tables are dollar volumes and unit numbers related to owner-occupied and rental properties financed by Fannie Mae's mortgage purchases. As with previous AHAR submissions and under agreement with HUD, we are forwarding under separate cover data cartridges, relating to mortgage purchases on single-family and multifamily housing units pursuant to 12 U.S.C. § 1723a(n), and confidential AHAR tables. I am also submitting the certification required by HUD's regulations.²

Very truly yours,

A handwritten signature in black ink, appearing to read "R. J. Levitt", with a long horizontal flourish extending to the right.

Robert J. Levitt

cc: Brian Montgomery, Assistant Secretary/Federal Housing Commissioner
Sandra Fostek, Director, Office of GSE Oversight

² 24 C.F.R. § 81.102(b)

FANNIE MAE'S
2005 ANNUAL HOUSING ACTIVITIES REPORT

SUBMITTED TO:

**U.S. DEPARTMENT OF HOUSING
AND
URBAN DEVELOPMENT
(HUD)**

**PURSUANT TO P.L. 102-550 AND
THE SECRETARY OF HUD'S REGULATION OF THE
FEDERAL NATIONAL MORTGAGE ASSOCIATION
(FANNIE MAE)
AND
THE FEDERAL HOME LOAN
MORTGAGE CORPORATION
(FREDDIE MAC)**

24 C.F.R. § 81.63

MARCH 16, 2006

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INTRODUCTION

Fannie Mae's Charter Act requires the company to submit an Annual Housing Activities Report (AHAR) to its oversight committees in the House of Representatives and the Senate and to the Secretary of the U.S. Department of Housing and Urban Development (HUD). In compliance with this requirement, Fannie Mae submits this AHAR for 2005.

Section 309(n) of the Charter Act lists the subjects that Congress requires the company to include in this AHAR.¹ The AHAR is organized by these Charter requirements and includes, where appropriate, examples of Fannie Mae's business activities that address these requirements. These are illustrative examples that do not define every activity that Fannie Mae engages in under each Charter requirement. The text in italics sets out the information that the Charter Act requires that Fannie Mae cover in the AHAR.

Fannie Mae is also attaching tables specified by HUD to provide detailed information about the company's performance in achieving each of the housing goals. The data cartridges relating to Fannie Mae's mortgage purchases of both single-family and multifamily loans will be forwarded under separate cover.

HUD is required by law² to establish three affordable housing goals for Fannie Mae and Freddie Mac: a low- and moderate-income housing goal, an underserved areas housing goal, and a special affordable housing goal. Since 1995, HUD has expressed these goals as a percentage of the dwelling units financed by Fannie Mae's mortgage purchases and securitizations.³ HUD regulations also established a multifamily special affordable housing subgoal expressed by multifamily dollar volume.⁴ On November 2, 2004, HUD published a new housing goals rule that governs the period from 2005 through 2008. In addition to setting new levels for HUD's three affordable housing goals, the rule established three home purchase subgoals.⁵ Fannie Mae operated under HUD's new housing goals structure for the first time in 2005.

In addition to pursuing HUD's regulatory housing goals, Fannie Mae's mission-focused activities include efforts to raise the minority homeownership rate, expand mortgage financing for first-time homebuyers, increase the supply of affordable housing and work with partners to develop communities. As a supporter of President George W. Bush's initiative to "increase the number of minority homeowners by at least 5.5 million by the end of the decade,"⁶ Fannie Mae committed, among other things, to provide \$700 billion in financing through 2009 that would help create homeownership opportunities for 4.6 million minority households. By year-end

¹ 12 U.S.C. § 1723a(n).

² The Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (the 1992 Act), 12 U.S.C. § 4561-4564.

³ 24 C.F.R. §§ 81.12(c), 81.13(c), 81.14(c) (2004).

⁴ 24 C.F.R. §§ 81.12(c), 81.13(c), 81.14(c) (2004).

⁵ The Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (the 1992 Act) specifically provides that subgoals established with respect to the Low- and Moderate-Income Goal and the Underserved Areas Goal are not enforceable. The 1992 Act is silent as to whether HUD has authority to establish enforceable subgoals under the Special Affordable Goal. HUD, therefore, has taken the position that subgoals under the Special Affordable Goal are enforceable.

⁶ Office of the President of the United States, "A Home of Your Own, Expanding Opportunities for All Americans" June 2002.

2005, Fannie Mae invested \$585.4 billion to provide financing to 3.9 million minority families under the President's Minority Homeownership Initiative.

Fannie Mae is a private, shareholder-owned company operating in the secondary mortgage market. The company makes funds available to primary market lenders to support the overall liquidity of mortgage credit and to make loans more affordable for home buyers. Fannie Mae achieves this through: 1) the purchases of mortgage loans directly from lenders and other mortgage sellers and the purchase of securities; and 2) the assembly of pools of mortgages acquired from lenders and issuance of Mortgage-Backed Securities (MBS), which lenders and sellers then hold or sell to investors.

I. FANNIE MAE'S 2005 HOUSING GOALS PERFORMANCE

In accordance with 12 U.S.C. § 1723a(n)(2)(A), Fannie Mae's AHAR is required to include, in aggregate form and by appropriate category, statements of the dollar volume and number of mortgages on owner-occupied and rental properties purchased which relate to each of the annual housing goals established under each subpart. Fannie Mae submits the information below addressing this report requirement.

Affordable Housing Goals Results for 2005

Goal Summary	2005 Goal	2005 Result	Ahead/Behind⁷
Base Goals			
Low- and Moderate-Income	52%	55.13%	+ 113,261
Underserved Areas	37%	41.39%	+ 163,029
Special Affordable	22%	26.32%	+ 156,642
Home Purchase Subgoals			
Low- and Moderate-Income	45%	44.62%	- 4,282
Underserved Areas	32%	32.56%	+ 6,311
Special Affordable	17%	17.04%	+ 459
Multifamily Special Affordable Subgoal	\$5.49 billion	\$9.76 billion	+ \$4.27 billion

As the table above shows, in 2005, Fannie Mae met its three base affordable housing goals: the low- and moderate-income goal, the underserved areas goal, and the special affordable housing goal. Fannie Mae also met three subgoals: the special affordable home purchase subgoal, the underserved areas home purchase subgoal, and the special affordable multifamily subgoal. The company fell slightly short of the low- and moderate-income home purchase subgoal.

Low- and Moderate-Income⁸ Goal and Subgoal

HUD's regulations define low- and moderate-income families based on family income and area median income. Of the dwelling units Fannie Mae financed with eligible mortgage purchases in 2005, 55.1 percent served low- and moderate-income families. The home purchase mortgage

⁷ Base housing goals are measured in units. Home purchase subgoals are measured in mortgages and the multifamily subgoal includes a minimum financing requirement "totaling not less than 1.0 percent of the average dollar volume of combined (single-family and multifamily) mortgages purchases by [Fannie Mae] in 2000, 2001 and 2002...." 24 C.F.R. section 81.14(c)(1).

⁸ HUD has established the low- and moderate-income housing goal for 2005 at 52 percent of the total number of dwelling units financed by eligible mortgage purchases annually. *Id.* § 81.12(c)(2). "Low-income" and "moderate-income" are defined in HUD's regulations at section 81.17.

low- and moderate-income subgoal represents the percentage of the total number of Fannie Mae's purchases of owner-occupied home purchase mortgages in metropolitan areas that meet the low- and moderate-income goal. Of the eligible home purchase mortgages that Fannie Mae financed in metropolitan areas in 2005, 44.6 percent served low- and moderate-income families.

Underserved Areas⁹ Goal and Subgoal

Fannie Mae's mortgage finance activities in underserved areas accounted for 41.4 percent of the housing units it financed with eligible mortgage purchases. The home purchase mortgage underserved areas subgoal represents the percentage of the total number of Fannie Mae's purchases of owner-occupied home purchase mortgages in metropolitan areas that meet the underserved areas goal. Of the eligible home purchase mortgages that Fannie Mae financed in metropolitan areas in 2005, 32.6 percent served families living in underserved areas.

Special Affordable Housing¹⁰ Goal and Subgoals

Fannie Mae's special affordable mortgage finance activities accounted for 26.3 percent of the housing units financed by eligible mortgage purchases in 2005. In addition, Fannie Mae provided \$9.76 billion in multifamily financing that qualified under the special affordable housing goal. The special affordable home purchase subgoal represents the percentage of the total number of Fannie Mae's purchases of owner-occupied home purchase mortgages in metropolitan areas that meet the special affordable goal. Fannie Mae's total share of these types of mortgages represented 17.0 percent of eligible home purchase mortgages in 2005.

Housing Goal Performance by Property Type

In 2005, Fannie Mae acquired 3,286,766 single-family mortgages with an unpaid principal balance of \$559.9 billion dollars, for an aggregate of 3,425,474 units. A total of 2,975,996 mortgages for \$511.8 billion were owner-occupied 1-unit properties and 54,985 mortgages for \$12.9 billion were owner-occupied 2-4 unit properties. The remaining 255,784 mortgages for \$35.2 billion were for investor-owned 1-4 unit properties.

In aggregate, our single-family housing goals performance for both owner-occupied and investor-owned properties, including proxies and other adjustments for the low- and moderate-income, underserved areas and special affordable housing goals are 49.8 percent, 38.4 percent, and 21.4 percent, respectively.

In 2005, Fannie Mae acquired 1,142,307 owner-occupied home purchase mortgages located in metropolitan statistical areas with an unpaid principal balance of \$202.3 billion. The low-and moderate-income, underserved areas, and special affordable performance of these mortgages is 44.6 percent, 32.6 percent and 17.0 percent respectively, when accounting for proxy and other adjustments.

⁹ HUD has established the underserved areas housing goal for 2005 at 37 percent of the total number of dwelling units financed by eligible mortgage purchases annually. *Id.* § 81.13(c)(2). "Underserved area" is defined in HUD's regulation at section 81.2.

¹⁰ HUD has established the special affordable housing goal for 2005 at 22 percent of the total number of dwelling units financed by eligible mortgage purchases annually to address the needs of low-income families in low-income areas and very low-income families. *Id.* § 81.14(c)(2). "Very low-income" is defined in HUD's regulations at section 81.17(c). "Low income area" means: a census tract or block numbering area in which the median income does not exceed 80 percent of the area median income. *Id.* § 81.2.

In 2005, Fannie Mae acquired 8,573 multifamily mortgages with an unpaid principal balance of \$21.8 billion, for an aggregate of 476,249 units. Of these units, 90.6 percent, 61.8 percent, and 59.4 percent met the low- and moderate-income, underserved areas and special affordable housing goals respectively, when accounting for missing data proxies and other adjustments. Of the aggregate volume of multifamily mortgages, \$9.76 billion met the special affordable multifamily subgoal, with a total of 280,740 units.

In accordance with 12 U.S.C. § 1723a(n)(2)(B), Fannie Mae's AHAR is required to: *include, in aggregate form and by appropriate category, statements of the number of families served by the corporation¹¹, the income class, race, and gender of homebuyers served, the income class of tenants of rental housing (to the extent such information is available), the characteristics of the census tracts, and the geographic distribution of the housing financed.* Fannie Mae submits the information below addressing this report requirement.

In 2005, Fannie Mae's eligible housing goals mortgage purchases served 3.9 million families across the country. Under the low- and moderate-income goal, Fannie Mae served approximately 2.0 million families, while approximately 501,800 families were served through the low- and moderate- income home purchase subgoal. The company's housing goals purchases in underserved areas helped approximately 1.5 million families. The underserved areas home purchase subgoal resulted in Fannie Mae mortgage purchases that served approximately 366,400 families. In meeting the special affordable goal, Fannie Mae served approximately 954,000 families. Under the special affordable home purchase subgoal, the company served approximately 191,800 families. Finally, financing through the special affordable multifamily subgoal in 2005 helped serve approximately 280,700 families. More detailed characteristics of the borrowers and renters that Fannie Mae served in 2005 including, but not limited to, income class, race and gender are provided in the tables attached to this AHAR.¹²

¹¹ Where Fannie Mae refers to "families" or "households" served by its mortgage purchases through this document, the company is defining families and households based upon the number of units financed by mortgage purchases.

¹² Fannie Mae refers HUD to the following tables for specific borrower and renter information: for income class see Table 2; for race see Table 7a; for gender, see Table 10. The income class of tenants by affordability of rent can be found on Table 4. Tables 11, 12 and 13 illustrate the characteristics of the census tracts in which Fannie Mae purchased single-family and multifamily mortgages under each affordable housing goal. The geographic distribution of Fannie Mae's single-family and multifamily mortgages by state and territory can be found in Table 14.

II. FANNIE MAE'S ACTIVITIES WITH FEDERAL SUBSIDY PROGRAMS

In accordance with 12 U.S.C. § 1723a(n)(2)(C), Fannie Mae's AHAR is required to: *include a statement of the extent to which the mortgages purchased by the corporation have been used in conjunction with public subsidy programs under Federal Law.* Fannie Mae submits the information below addressing this report requirement.

Fannie Mae's affordable financing activities are used in conjunction with a wide variety of federal subsidy programs to serve the housing needs of low-income households and communities.¹³ Fannie Mae also partners with organizations—including community-based nonprofits and state and local public entities—to help them leverage federal funds to increase their capacity to carry out their affordable housing and community development activities. A range of public subsidy programs is sometimes included in Fannie Mae affordable housing transactions. Our transactions may include mortgages where the borrower has received downpayment assistance from the federal **Community Development Block Grant** program or the **Section 8 Housing Assistance Vouchers** program administered by the **Department of Housing and Urban Development (HUD)**. Transactions may also include substantial direct investments in federal **Low Income Housing Tax Credits (LIHTC)** and the provision of multifamily financing using in conjunction with **LIHTC** and **Section 236 Interest Reduction Payments**. Through its secondary market activities, Fannie Mae may also purchase federally-guaranteed loans such as mortgages insured by the **Federal Housing Administration (FHA)** or rural housing loans insured by the **U.S. Department of Agriculture (USDA)**. In 2005, Fannie Mae purchased, invested and/or guaranteed approximately \$14 billion in conjunction with federal public subsidy programs.¹⁴

A sample of some of the mortgages purchased by Fannie Mae that have been used in conjunction with federal housing subsidy programs in 2005 is described below.

- Fannie Mae is a secondary market investor in HUD's reverse mortgage product, the **Home Equity Conversion Mortgage (HECM)**. **HECMs** allow seniors to convert the equity in their homes into monthly streams of income and/or a line of credit to be repaid when they no longer occupy the home. In 2005, Fannie Mae purchased 54,907 **HECMs** for a total value of \$4.7 billion, and provided \$1.1 billion in advances on existing loans. The company provides financing for this product to help ensure that the nation's elderly population has an alternative when making quality-of-life decisions.
- Fannie Mae made a \$1.4 million loan to the Blackfeet Tribe in Montana for construction of North Country Estates, a 25-unit **LIHTC** project. The company's loan provides the Tribe

¹³ For the purposes of this AHAR, Fannie Mae is defining "public subsidy programs" to include government programs that provide direct subsidies to borrowers for down payment and closing costs or to reduce interest-rates on first or second mortgages or to renters or rental housing developments to increase the affordability of these developments. The definition also includes direct loans, loans guaranteed or insured by the government, and tax expenditure programs such as mortgage revenue bonds, and tax credits which, although not necessarily a direct subsidy to the borrower or renter, reduce the cost of financing through features such as reduced mortgage interest rates and the provision of below market rents.

¹⁴ This total includes Fannie Mae's purchase of single-family mortgages insured and guaranteed by the federal government (see Table 9) and multifamily investments in various federal tax credit programs.

with needed short term financing that will bridge federal funds from the **Department of Health and Human Services' *Indian Health Service Program*** and the USDA's ***Rural 515 Program***.

- The federal *LIHTC* program directs private equity capital toward the creation of affordable rental housing. Investors receive the value of tax credits through leasing to qualified families at or below specified rent levels. A development eligible for consideration under the *LIHTC* program must be a residential rental property; meet one of two possible low-income occupancy threshold requirements; restrict rents, including utility charges, in low-income units; and operate under the rent and income restrictions for 30 years or longer as required by the state or local agency issuing the tax credits. In 2005, Fannie Mae committed over \$1.8 billion in *LIHTC* equity properties that resulted in 21,981 affordable rental housing units. Since 1987, when Fannie Mae started participating in the *LIHTC* program, using both direct investments and investments in equity funds, the company participated in the creation or preservation of over 405,000 units of affordable rental housing.
- In addition to investments in *LIHTC* equity properties, Fannie Mae purchased the permanent mortgage on **9 percent *LIHTC*** transactions and provided credit enhancement on **4 percent *LIHTC*** transactions. In 2005, Fannie Mae purchased the debt on 135 **9 percent *LIHTC*** properties totaling \$373 million that resulted in 13,334 affordable rental housing units. Fannie Mae also credit enhanced 4 percent tax-exempt bonds totaling approximately \$1.7 billion. This includes all new credit enhancement commitments and conversions that occurred throughout 2005.
- The federal ***Historic Tax Credit*** (HTC) program directs private equity capital toward the rehabilitation of certified historic landmarks and other designated historically significant properties as determined by the National Park Service's Department of Historic Preservation. Investors receive the value of tax credits through successfully restoring and rehabilitating the historic property and maintaining the historic integrity of the improvements. In 2005, Fannie Mae committed over \$53 million in *HTC* properties that were oriented toward affordable multifamily rental housing.
- Under the federal ***HOPE VI*** grant program which seeks to rehabilitate and/or create new public housing units, Fannie Mae equity, in the form of *LIHTCs* works as a source of funds to help complete a *HOPE VI* housing project. In 2005, Fannie Mae helped finance two *HOPE VI* transactions with \$34.2 million in equity. The developments provided 376 units of affordable housing. The same financing model is used by Fannie Mae and other partners to leverage federal ***Home Investment Partnerships (HOME)*** funds which also provide low cost financing in building new or rehabilitating affordable housing units.
- Fannie Mae works with lenders and Public Housing Agencies (PHAs) to finance homeownership for households participating in HUD's Section 8 Homeownership Program. With their Section 8 vouchers, borrowers may experience the benefits of homeownership in two ways. First, Fannie Mae's ***MyCommunityMortgage***TM allows lenders to use the value from these vouchers as "grossed up" qualifying borrower income. Second, Fannie Mae's Section 8 Homeownership Underwriting Experiment gives lenders several underwriting

options that can be used with most Fannie Mae products, including *MyCommunityMortgage*. In 2005, Fannie Mae helped 98 families with Section 8 vouchers become homeowners.

III. INCREASING HOMEOWNERSHIP OPPORTUNITIES FOR FIRST-TIME HOMEBUYERS

In accordance with 12 U.S.C. § 1723a(n)(2)(D), Fannie Mae's AHAR is required to: *include statements of the proportion of mortgages on housing consisting of 1 to 4 dwelling units purchased by the corporation that have been made to first-time homebuyers, as soon as providing such data is practicable, and identifying any special programs (or revisions to conventional practices) facilitating homeownership opportunities for first-time homebuyers.* Fannie Mae submits the information below addressing this report requirement.

In 2005, 35.7 percent of Fannie Mae's conventional owner-occupied purchase mortgages were made to first-time homebuyers.¹⁵ Further information about Fannie Mae's purchases of first-time homebuyer loans is provided in Table 9.

Although some of the tools and initiatives highlighted in this section are not exclusively for first-time homebuyers, by removing barriers to homeownership for underserved families—down payment, lack of affordability—they increase the ability for borrowers to purchase their first home. In addition, examples of partnerships focused on increasing first-time homebuyers are also highlighted.

Lack of Down Payment

Fannie Mae and its lender partners developed a suite of down payment mortgages under the *Flexible* mortgage product line. These products permit the borrower to obtain funds for a down payment and closing costs from the following sources: 1) a gift from a relative, domestic partner, fiancée or fiancé; 2) a grant from an employer, public agency, or nonprofit organization; 3) an unsecured loan from a relative, domestic partner, fiancée or fiancé, employer, or nonprofit organization; and 4) secured borrowed funds and *Community Seconds*.¹⁶ In 2005, Fannie Mae purchased \$21.6 billion in *Flexible* loans made to 150,370 households. Of that total, 75,726 *Flex* mortgages were made to families that were first-time homebuyers.

Fannie Mae's targeted product for low- and moderate-income households and underserved areas is *MyCommunityMortgage*, which includes lender-customized income-targeted mortgage products that are financed by Fannie Mae. Both the standard *MyCommunityMortgage* and these lender-customized products particularly assist first-time homebuyers. In 2005, Fannie Mae purchased or securitized more than \$5.5 billion of *MyCommunityMortgage* and lender-

¹⁵ Fannie Mae relied on information provided by its customers to identify units occupied by first-time homebuyers. Fannie Mae's Selling and Servicing Guide defines a first-time homebuyer as "an individual who: (1) is purchasing the security property; (2) will reside in the security property; and (3) had no ownership interest (sole or joint) in a residential property during the three-year period preceding the date of the purchase of the security property. In addition, an individual who is a displaced homemaker or single parent also will be considered a First-Time Homebuyer if he or she had no ownership interest in a principal residence (other than a joint ownership interest with a spouse) during the preceding three-year time period."

¹⁶ Community Seconds is a second lien mortgage typically provided by a federal, state or local government agency, an employer or a nonprofit organization. It may be forgivable, offer deferred payment or other special terms.

customized loans. More than 33,000 loans—over 70 percent—were made to first-time homebuyers.

In 2005, Fannie Mae introduced the following enhancements to *MyCommunityMortgage*.

- A significantly reduced mortgage insurance (MI) requirement that lowers monthly mortgage costs is now available for borrowers. With this enhancement, the required MI for *MyCommunityMortgage* is at the lowest percentage that satisfies the conventional mortgage insurance parameters in Fannie Mae's Charter. For example, for loans with an LTV range of 97.01 to 100, the MI coverage originally required was 35 percent, but was lowered to 20 percent. Similarly, for LTVs between 95.01 to 97 percent, the required MI was lowered from 35 to 18 percent and LTVs from 90.01 to 95 percent to 16 percent. These new MI levels reduce a borrower's MI cost by about one-third. For a \$150,000 mortgage loan, the MI savings could be between \$46 to \$64 dollars per month.¹⁷
- Cash-on-hand is now an acceptable source of funds under *MyCommunityMortgage*. Lenders may deliver mortgages with cash-on-hand as a source of funds for the borrower's down payment and/or for closing costs. This enhancement is targeted to borrowers who customarily use cash for expenses and have had limited or no prior use of traditional credit or bank accounts.
- To allow borrowers the advantage of second lien funding, *MyCommunityMortgage* includes the option of *CommunitySeconds*. With this product, a borrower can obtain a second lien mortgage typically funded by a federal, state, or local government agency, an employer or a nonprofit organization. This second may be forgivable over time. With the 2005 *MyCommunityMortgage* enhancement, borrowers now have the option to use traditional subordinate financing as well as *CommunitySeconds*.
- Fannie Mae expanded the eligible adjustable-rate mortgages (ARMs) under *MyCommunityMortgage* to include 5/1 fixed-period ARMs in addition to existing 7/1 and 10/1 options. After the initial fixed period, the mortgage note rate adjusts annually based on market interest rates and payments are adjusted accordingly. These ARMs have lower monthly payments during their initial fixed periods, helping borrowers with affordability.

Local housing finance agencies (HFAs) can also offer *MyCommunityMortgage* loans through their mortgage revenue bond programs that focus on serving first-time homebuyers.¹⁸ The HFA-related loans offer the standard *MyCommunityMortgage* features, allowing homebuyers to finance up to 100 percent LTV with a borrower contribution of as little as \$500 with the added benefit of reduced mortgage insurance coverage. In 2005, Fannie Mae purchased close to \$250.5 million in HFA-related *MyCommunityMortgage* loans.

¹⁷ The monthly savings depends on the loan amount and the MI rate for which the borrower qualifies.

¹⁸ 26 U.S.C. § 143.

Lack of Affordability

Increasing home prices make homeownership difficult to achieve. Fannie Mae is working with lenders to develop flexible loan terms and new guidelines that help facilitate the financing of affordable housing units that will help first-time homebuyers.

- After piloting the 40-year fixed rate mortgage with a small group of credit unions in 2004, Fannie Mae rolled out the **40-Year Mortgage** to all lenders in June 2005. The **40-Year Mortgage** has similar underwriting eligibility criteria to the standard 30-year fixed-rate and hybrid ARM products, and appeals to borrowers who want an uncomplicated mortgage that provides lower monthly payments than 30-year terms provide. The **40-Year Mortgage** carries the same mortgage insurance coverage requirements and follows the same **Desktop Underwriter® (DU™)** guidelines as certain standard 30-year fixed- and adjustable-rate mortgages.
- Condominiums are often considered a first step to homeownership and an affordable alternative to single-family detached homes.¹⁹ In 2005, Fannie Mae substantially revised its condominium review and acceptance guidelines. The guideline changes include enabling lenders to determine project acceptance for more projects; broadening the eligibility criteria; and streamlining the project acceptance process by reducing the number of requirements and using technology.

Partnerships Focused on Increasing First-Time Homebuyers

Fannie Mae has partnered with lenders, state and local public housing finance agencies and other organizations to develop products that reach first-time homebuyers.

- In 2001, Fannie Mae, the **AFL-CIO** and **Countrywide Home Loans** joined together in a three-way national partnership to create "Hit Home," a single-family housing initiative to assist families in becoming first-time homebuyers. Approximately 50 percent of the borrowers participating in the initiative are historically underserved and include minorities and single-parent households. In 2005, Fannie Mae purchased more than \$42.6 million in mortgages originated by Countrywide. One-third of these loans were made to first-time homebuyers.
- Fannie Mae reaches first-time homebuyers through partnerships with state and local housing finance agencies (HFAs). By providing partner HFAs access to Fannie Mae's single-family and multifamily products, HFAs have more tools to help finance, develop, and preserve affordable housing. In 2005, Fannie Mae purchased 8,094 loans from 95 state and local HFAs totaling nearly \$776 million,²⁰ an increase of almost 50 percent from 2004 HFA mortgage purchases. Approximately 83 percent of these borrowers were first-time homebuyers.

¹⁹ Joint Center for Housing Studies, "The State of the Nation's Housing 2004," page 6, Harvard University, 2004.

²⁰ This volume includes the \$250.5 million purchased through the HFA *MyCommunityMortgage* feature described on the preceding page of this AHAR.

- In 2004, the **National Association of Hispanic Real Estate Professionals (NAHREP)** and Fannie Mae entered into a three-year partnership focused on increasing first-time homebuyers in underserved, minority, and immigrant communities. Working with NAHREP mortgage brokers and participating lenders, Fannie Mae's goal is to purchase up to 25,000 mortgages that are made to first-time homebuyers. Fannie Mae and its lender partners are also working to build the capacity of NAHREP brokers to originate loans and with NAHREP real estate professionals to reach underserved communities. Fannie Mae resources include technical assistance, flexible mortgage products, technology and marketing research.

In accordance with 12 U.S.C. § 1723a(n)(2)(E), *include, in aggregate form and by appropriate category, the data provided to the Secretary under subsection (m)(1)(B); (the loan-to-value ratios of purchased mortgages at the time of origination;)* Fannie Mae submits the information below addressing this charter requirement.

In 2005, 24.5 percent of Fannie Mae's low- and moderate-income mortgage purchases had a loan-to-value (LTV) between 95 and 100 percent. For the underserved goal, 22.3 percent of mortgage purchases had an LTV between 95 and 100 percent. In the final special affordable housing goals category, loans with LTVs between 95 and 100 percent made up 30.6 percent of Fannie Mae's mortgage purchases.

In accordance with 12 U.S.C. § 1723a(n)(2)(F), *compare the level of securitization versus portfolio activity.* Fannie Mae submits the information below addressing this charter requirement.

In 2005, Fannie Mae securitized \$481.3 billion in mortgages and purchased \$146.6 billion for its portfolio. This activity shows a decrease from 2004 when Fannie Mae purchased \$262.6 billion for its portfolio and securitized \$527.1 billion.

IV. UNDERWRITING STANDARDS, BUSINESS PRACTICES AND EFFORTS TO PROMOTE FAIR AND RESPONSIBLE LENDING

In accordance with 12 U.S.C. § 1723a(n)(2)(G), *assess underwriting standards, business practices, repurchase requirements, pricing, fees, and procedures, that affect the purchase of mortgages for low- and moderate-income families, or that may yield disparate results based on the race of the borrower, including revisions thereto to promote affordable housing or fair lending.* Fannie Mae submits the information below addressing this report requirement.

Fannie Mae's fair lending efforts are focused on ensuring that lenders have the tools to effectively and responsibly reach underserved markets and promote good lending practices throughout the industry. Underwriting standards are constantly evaluated to promote fair and responsible lending. In providing these guidelines, Fannie Mae helps set industry standards that promote fairness. To ensure compliance with Fannie Mae's responsible lending policies, Fannie Mae establishes lender selection criteria and conducts routine checks on the quality of loans Fannie Mae purchases. The company's fair lending compliance team also works closely with business units on initiatives such as those highlighted throughout this report, which support lenders' efforts to reach low- and moderate-income families and underserved borrowers.

Business Practices and Procedures Impacting the Purchase of Low- and Moderate- Income Mortgages

To keep lenders informed of policies and procedural requirements and keep them abreast of the company's efforts to promote responsible lending, Fannie Mae publishes a *Selling and Servicing Guide*. The *Selling and Servicing Guide* covers standard requirements for the origination, underwriting, and delivery to Fannie Mae of one- to four-family mortgages.

In response to changes in housing market affordability and at the request of lender partners, Fannie Mae's 2005 amendments to its *Selling and Servicing Guides* included the following: 1) expanding eligibility criteria to allow lenders to more easily determine project acceptance for condominium projects; 2) extending the maximum loan term on certain standard Fannie Mae mortgage products from 30 to 40 years; and 3) increasing the new maximum mortgage amount limits effective for 2006 for all conventional mortgages.

In 2000 and again in 2004, Fannie Mae set forth guidance on Fannie Mae's anti-predatory lending policies which are part of the company's efforts to help keep people in their homes and promote responsible lending practices. In 2000, Fannie Mae issued Lender Letter 03-00. In 2004, Fannie Mae issued Announcement 04-04. These lender letters establish policies with regards to the following practices.

- Prohibiting the purchase of loans with mandatory arbitration provisions;
- Prohibiting the purchase of balloon mortgages with terms less than seven years;
- Servicing policies aimed at preserving homeownership;
- Prohibiting the purchase of loans with prepayment premiums longer than 3 years;
- Prohibiting the purchase of loans with single-premium credit life and other single-premium insurance or single-premium debt cancellation agreements;
- Discouraging escrow waivers for blemished credit borrowers;

- Prohibiting the purchase of Home Ownership and Equity Protection Act (HOEPA) loans (Section 32 of Truth In Lending Act) and loans that are subject to certain state high-cost lending laws;
- Prohibiting the purchase of loans with excessive points and fees; and
- Requiring full-file credit reporting to credit repositories.

If Fannie Mae determines that a loan fails to comply with these policies, the company may pursue various options, including requiring repurchase of the loan or indemnification by the lender in lieu of immediate repurchase.

Underwriting Standards Impacting the Purchase of Low- and Moderate- Income Mortgages

Fannie Mae offers two underwriting methods a lender can use in making a decision about whether to approve or decline a mortgage application—automated underwriting through *Desktop Underwriter*® (*DU*TM) and manual underwriting. Both methods are based on Fannie Mae's understanding of default risk. Each underwriting method is designed to enable a lender to evaluate the overall credit risk of a mortgage application and to determine whether the mortgage is eligible for delivery to Fannie Mae. Under appropriate terms and conditions, Fannie Mae purchases mortgages that represent varying levels of risk, including those that have relatively higher risks because of such factors as a blemished credit history, limited savings, or low down payments. Fannie Mae's research and efforts to provide appropriate liquidity to lenders who serve borrowers who have these higher risk factors is another way that Fannie Mae serves low- and moderate-income borrowers.

Automated Underwriting Through *Desktop Underwriter*

DU features fast and objective risk assessments, reduced data entry requirements, reduced documentation, and comprehensive underwriting reports.

DU is designed to assist lenders in processing mortgage applications in a more efficient and accurate manner. *DU* promotes fair lending by evaluating applications consistently and objectively. *DU* applies the same criteria to every loan it processes. *DU* does not consider prohibited factors such as a borrower's age, race, color, religion, gender, national origin, disability, familial status, or marital status in making a recommendation.

DU complements, it does not replace, the considered judgment of experienced underwriters. *DU* provides underwriting recommendations to lenders based on Fannie Mae's purchasing and securitization guidelines for single-family mortgage products. Lenders make the final decision regarding loan approval. If a lender originates a loan that is intended to be purchased or guaranteed by Fannie Mae, the lender must underwrite the loan using guidelines that are acceptable to Fannie Mae, and those guidelines are incorporated into *DU*.

Since 2000, Fannie Mae has made the mortgage process more transparent by disclosing the factors *DU* considers in its risk evaluation. These factors include both credit and non-credit risk factors. The credit factors include the borrower's credit history; delinquent accounts; mortgage accounts; revolving credit utilization; public records, foreclosures and collection accounts; and credit inquiries. The non-credit risk factors include the borrower's loan-to-value (LTV) ratio,

liquid reserves, loan purpose, loan term, loan/amortization type, occupancy type, total expense ratio, property type, co-borrowers, and self-employment.

Manual Underwriting and Underwriting through Lenders' Automated Systems

Lenders may also deliver loans to Fannie Mae that have not been processed through *DU*. In these cases, lenders must represent and warrant that the loan complies with the underwriting policies, guidelines, and eligibility criteria as described in the Fannie Mae *Selling Guide*. Subject to Fannie Mae's review and prior approval, Fannie Mae also purchases or securitizes mortgages underwritten to a lender's own underwriting guidelines, including loans that are underwritten with a lender's own proprietary automated underwriting system.

Repurchase Requirements Impacting the Purchase of Low- and Moderate- Income Mortgages

Fannie Mae generally relies on the selling lenders' representations and warranties that the mortgage loans being purchased or guaranteed conform to the applicable Fannie Mae guidelines. At the company's discretion, waivers or variances from these underwriting guidelines may be granted. After purchase, Fannie Mae performs quality control reviews of selected loans to monitor compliance with the guidelines. Fannie Mae's National Underwriting Center (NUC) performs Fannie Mae's underwriting reviews and provides loan quality information and analyses to Fannie Mae staff throughout the country. NUC focuses its resources on loans that represent a higher risk to the company but also randomly samples loan deliveries for quality assurance reviews. This helps ensure that loan reviews are done in an objective and consistent manner. The goal of each review is to identify any significant underwriting deficiencies, possible misrepresentations, or eligibility issues associated with the loan. In addition to loan-level quality assurance, the NUC performs anti-predatory lending screening on a targeted segment of loans. If it is determined that a loan should not have been delivered to Fannie Mae, the company may pursue various options, including requiring repurchase of the loan or indemnification by the lender in lieu of immediate repurchase.

Pricing and Fees Impacting the Purchase of Low- and Moderate- Income Mortgages

Fannie Mae's pricing policies and strategies are based on competitive market factors, the company's experience, capital requirements, and key determinants or indicators of loan performance. There are a number of factors that are used to predict loan performance. They include credit histories, mortgage loan and property characteristics, interest rate fluctuations, and housing prices. Fannie Mae continually updates its databases with current information.

Through various negotiated vehicles and lender agreements, Fannie Mae arrives at specific fees for accepting a certain amount of risk on mortgages purchased or guaranteed in MBS. A number of pricing structures are utilized based on lender needs, Fannie Mae's business and mission objectives, and competitive market factors. In making pricing decisions, Fannie Mae factors in its ability to meet strategic business goals and its ability to provide affordable mortgage credit and tear down barriers to homeownership.

Underwriting Revisions, Products and Other Activities to Promote Affordable Housing or Fair Lending

Fannie Mae conducts quarterly reviews of loan performance data to assess the loan default risk predictability of the *DU* model. The Fair Lending Compliance team in the Legal Department of Fannie Mae reviews all changes to *DU* to ensure that *DU* complies with fair lending laws.

In 2005, there were three major *DU* version releases that helped promote affordable housing.

- ***DU Version 5.4.2***

- implemented the lower down payment requirement for certain loans secured by manufactured homes as described in Fannie Mae Announcement 04-07;
- expanded the ***InterestFirst™*** guidelines to offer a ten-year interest-only period for new 3/1, 5/1, and 7/1 ARMs; and
- enhanced the system's ability to identify potential underwriting problems in the loan application to help alert the lender to possible mortgage fraud.

- ***DU Version 5.5***

- added 40-year mortgages to the standard product line;
- enhanced the *MyCommunityMortgage* product in *DU* by allowing cash-on-hand as an acceptable source of funds, lowering the required mortgage insurance coverage, permitting subordinate financing other than *Community Seconds*, and offering 5/1 ARM plans with 2/2/5 caps;
- relaxed the collection and charge off policy on principal residences and second home transactions to require the payoff of only those totaling more than \$5,000 (instead of \$1,000); and
- reflected Fannie Mae's updated condominium project acceptance guidelines enabling lenders to determine project acceptance for more condominium projects.

- ***DU Version 5.5.1***

- allowed underwriting flexibilities to meet the housing needs of borrowers impacted by Hurricanes Katrina and Rita.

In addition to the three major production releases of *DU*, in 2005 Fannie Mae conducted a limited *DU* pilot (version ***DU 6.0***) with two small lenders to evaluate a new credit risk/cost-based scoring model.

Fannie Mae also reviews and changes its underwriting guidelines to meet the needs of underserved populations. Results of these underwriting pilots are used to determine if an underwriting policy change is warranted. In 2005, Fannie Mae committed \$97.8 million to fund 20 underwriting pilots across the country.

In over 15 cities, Fannie Mae's Community Business Centers are working on ***Anti-Predatory Lending Refinance Initiatives*** that help borrowers refinance out of abusive loans and into

responsible ones. Each of these initiatives is designed to address the particular needs and conditions in a local community. In 2005, Fannie Mae launched 5 of these initiatives and committed to purchase \$61 million in loans originated through new and existing *Anti-Predatory Lending Refinance Initiatives*. Additionally, Fannie Mae launched three new ***Borrow with Confidence***[™] initiatives with REALTOR® associations in Florida, North Carolina and Mississippi. The campaign promotes responsible lending by providing real estate professionals with training on a host of flexible mortgage products that address the barriers that many of their clients face, such as lack of down payment funds, blemished credit and over-indebtedness. Since its inception in 2003, the *Borrow with Confidence* has been launched in 19 states.

Fannie Mae's ***Expanded Approval with Timely Payment Rewards***[®] (***EA/TPR***[™]) initiative, offered through *DU*, continues to provide an alternative for borrowers with blemished credit histories.

- With *EA*, borrowers may secure a mortgage rate that may be significantly lower than non-traditional financing. *EA* can also be combined with the *TPR* feature, which gives qualifying borrowers an interest rate reduction of up to one percentage point after making timely mortgage payments for a specified period, without having to refinance. And with certain 5-, 7-, and 10-year ARM plans that are available with *EA*, the borrower can have lower payments for the first 5, 7, or 10 years after which time the interest rate adjusts annually. In 2005, Fannie Mae purchased \$14 billion in *EA* loans to help 103,356 homebuyers lower the cost of home financing. In the same period, Fannie Mae purchased \$984 million of loans using the *TPR* feature enabling 7,578 additional homebuyers to benefit from further interest savings. Total *EA/TPR* volume for Fannie Mae in 2005 was \$15 billion.

Finally, in 2005, Fannie Mae hosted its ***Sixth Annual Fair Lending Conference*** in Washington, D.C. bringing together over 100 participants from the lending industry, government, housing and civil rights organizations, and academia. The conference was entitled: "What is Responsible Lending?" Conference topics included the new HMDA data, "exotic" mortgages such as Interest Only loans and Option ARMs, and foreclosure trends. Panelists included representatives from government, industry and public interest organizations.

V. PROVIDING AFFORDABLE RENTAL HOUSING

In accordance with 12 U.S.C. § 1723a(n)(2)(H), *describe trends in both the primary and secondary multifamily housing mortgage markets, including a description of the progress made, and any factors impeding progress toward standardization and securitization of mortgage products for multifamily housing.* Fannie Mae submits the information below addressing this report requirement.

Despite increasing homeownership rates, the need for affordable rental housing remains strong. Fannie Mae helps increase the supply of affordable rental housing through the purchase of debt investments, credit enhancement of multifamily housing bonds targeted at low- and moderate-income families, multifamily equity (including **Low-Income Housing Tax Credits (LIHTC)**), and multifamily mortgage revenue bonds. Multifamily Business' book includes multifamily mortgages purchased for cash, multifamily Mortgage-Backed Securities (MBS), credit enhancements of bonds, investments in LIHTC, and other assets, which total \$124 billion.²¹

In 2005, the U.S. economy continued strengthening, adding about 2 million new jobs. Inflation remained under control with the Federal Reserve increasing short-term interest rates. As a result, the multifamily property sector continued improving during 2005. Real estate fundamentals for the sector improved with vacancies declining by the end of the year to about 6 percent nationally for institutional-type properties. Asking rents kept increasing all year, and more importantly, with fewer concessions being offered to prospective tenants.

Due to Hurricanes Katrina and Rita, some of the markets located in the Gulf region experienced tight housing conditions during the latter part of 2005. Baton Rouge experienced nearly 100 percent occupancy levels. Houston, Austin and metropolitan areas as far away as Atlanta also saw multifamily occupancies quickly increase. The after-effects of the hurricanes on the state of the housing market in New Orleans and other hard-hit areas are still being fully assessed. There is concern that rebuilding of damaged or destroyed lower-income housing may be problematic due to higher replacement costs.

The multifamily originations market during 2005 experienced intense competition and high demand. As a result, more collateral from further down the credit spectrum is making its way into the market as many lenders continue to relax credit standards to gain market share.

In an effort to enhance product standardization in the marketplace, Fannie Mae created the **Delegated Underwriting and Servicing (DUSTM)** product line in 1988 for purchasing individual multifamily loans. DUS is Fannie Mae's principal network whereby underwriting is delegated to the DUS lenders, enabling them to move quickly to arrange financing for borrowers. The majority of loans purchased through Fannie Mae's DUS

²¹ This does not include multifamily mortgage revenue bonds or other issuers' multifamily securities held in Fannie Mae's portfolio.

lender network are secured by properties with units that are largely affordable to families earning at or below the median income in their area.

Multifamily Products and Activities

Fannie Mae's product innovations in 2005 focused on providing lenders and borrowers with more flexibility in arranging financing and easier processing and underwriting. Highlights include the following:

- the availability of a new **Structured ARM** product for large loans (greater than \$25 million) and structured transactions that are designed to provide a more competitive execution than standard ARM offerings by: using an externally purchased interest rate cap in lieu of periodic and lifetime caps in the loan structure, applying a 1-day look back to rate changes and eliminating the grace period for borrower remittances;
- the availability of 2 percent and 2.5 percent lifetime cap options on **DUS ARM** executions and increased maximum loan-to-value requirements for 7- and 10-year term loans from 77.5 percent to 80 percent;
- the replacement of the underwriting floor test that was applicable to 5-, 7- and 10-year balloon mortgages with a **Stressed Refinance Test** that eliminates duplication and simplifies the exit strategy analyses used to underwrite balloon mortgages;
- the availability of a new **DUS Plus** product that combines the standard **DUS fixed-rate mortgage** loan with mezzanine financing, secured by a pledge of partnership interest, that is sold to a third party investor in order to provide more competitive loan sizing without increasing the risk tolerance;
- the development of streamlined underwriting requirements and an extended rate lock period to 18 months in order to simplify and reduce the cost for borrowers who are refinancing loans that are in portfolio;
- the increased usage of the **Actual/360 interest accrual** option to loans that have either partial or full term interest-only periods and are funded through the issuance of an MBS; and
- release of an **Unfunded Forward** structure that provides a rate lock for the permanent financing of new construction or substantial rehabilitation loans financed with 9 percent *Low Income Housing Tax Credits*.

VI. DELINQUENCY AND DEFAULT RATES FOR LOW- AND MODERATE-INCOME FAMILIES

In accordance with 12 U.S.C. § 1723a(n)(2)(I), *describe trends in the delinquency and default rates of mortgages secured by housing for low- and moderate-income families that have been purchased by the corporation, including a comparison of such trends with delinquency and default information for mortgage products serving households with incomes above the median level that have been purchased by the corporation, and evaluate the impact of such trends on the standards and levels of risk of mortgage products serving low- and moderate- income families.* Fannie Mae submits the information below addressing this report requirement.

Delinquency and Default Trends Based on 2004 Performance Data

Analysis of the performance of mortgage loans serving low- and moderate-income families (defined as a unit occupied by a household earning less than or equal to the median area income) shows consistently poor performance relative to loans on units serving households with incomes above the median level. *The analysis presented here does not control for other risk dimensions, such as LTV or credit history, only income relative to the area median.*

The attached table displays serious delinquency performance and default performance over time. Fannie Mae defines early serious delinquency as being 90 days or more delinquent within 12 months of acquisition. Default is defined as foreclosure sale, deed-in-lieu of foreclosure, pre-foreclosure sale, or third party sale at anytime in the life of the loan.

The analysis demonstrates that loans to low- and moderate-income borrowers on average performed about 1.75 times worse than mortgages to higher income borrowers with respect to early serious delinquency for years 1996-2001. Since 2001, as eligibility for higher risk products has expanded through such offerings as *My Community Mortgage* and *Expanded Approval*, performance on these loans to low- and moderate- income borrowers has become worse. For 2004 acquisitions, loans to low- to moderate-income borrowers were delinquent 2.4 times more often than loans to higher income borrowers. The relative default rate performance is also consistently worse for low- to moderate-income borrowers than for higher income borrowers. Fannie Mae continues to use this performance information to define prudent underwriting and eligibility standards that expand access to the housing market through a broad range of affordable product options, while maximizing the possibility of sustained homeownership for borrowers.

Relative Serious Early Delinquency and Ever Default Rates Between Single Family Loans Serving Low- and Moderate-Income Families and Loans Serving Households with Incomes Above the Median Level by Year

Sample: Unseasoned, conforming, conventional, forward amortizing, first liens, non GEMs/GPMs

Acquisition Year	Relative Serious Early Delinquency Performance	Relative Ever Default Performance
1996	1.8	1.7
1997	1.7	1.7
1998	1.8	1.8
1999	1.7	1.9
2000	1.7	2.0
2001	1.6	2.0
2002	2.0	2.5
2003	2.4	3.1
2004	2.4	3.6

Notes:

- 1) Relative Performance equals the delinquency (default) rate for loans serving low- and moderate-income families divided by the delinquency (default) rate of loans serving households with incomes above the median level.
- 2) Serious Early Delinquency is defined as ever 90 or more days delinquent within 12 months of acquisition.
- 3) Default is defined as a foreclosure, deed-in-lieu of foreclosure, or third party sale at any point in the loans life.
- 4) The analysis presented here was performed on unseasoned loans by acquisition year to avoid commingling different aged loans for the purposes of displaying a trend over time.
- 5) The analysis presented here does not control for other risk dimensions, such as LTV or credit history, only income relative to the area median.

VII. FANNIE MAE'S SELLER AND SERVICER NETWORK

In accordance with 12 U.S.C. § 1723a(n)(2)(J), *describe in the aggregate the seller and servicer network of the corporation, including the volume of mortgages purchased from minority-owned, women-owned, and community-oriented lenders, and any efforts to facilitate relationships with such lenders.* Fannie Mae submits the information below addressing this report requirement.

Fannie Mae has selling and servicing relationships with over three thousand single-family and multifamily primary market lenders under which the company both purchases loans for its portfolio and issues MBS.

Selling and Servicing Network

Fannie Mae's selling and servicing network includes small and large lenders, minority and women-owned lenders and smaller, community-oriented lenders. In addition, in late 2000, Fannie Mae created the National Business Center to focus dedicated resources to address the needs of small and mid-sized lenders.

Community-oriented lenders with assets less than \$1 billion include banks, thrifts, mortgage bankers, credit unions and housing finance agencies.²² According to annual data, volume for 2005 from community-oriented lenders totaled \$31.9 billion. In 2005, Fannie Mae purchased a total of \$4 billion in mortgages from minority- and women-owned lenders. Of that total, \$802 million was purchased from sellers and servicers identified by Fannie Mae as women-owned lenders.²³

Efforts to facilitate relationships with these lenders include formal business alliances or affinity agreements in which lenders receive benefits that streamline or reduce the cost of doing business in the secondary market with Fannie Mae.²⁴ Similar to business alliances, Fannie Mae also establishes agreements or memoranda of understanding (MOU) with housing advocacy groups, community-based groups and industry groups such as the National Bankers Association, a trade association whose members include banks owned by African-Americans, Native-Americans, American-Indians, East-Indians, Hispanic-Americans, Asian-Americans and women. Fannie Mae also reaches out to lenders by providing financing to Community Development Financial Institutions (CDFIs) through the **American Communities Fund® (ACF®)**. A sampling of the outreach Fannie Mae conducts to reach minority, women-owned and community-based lenders is discussed in the next pages.

²² For the purposes of this AHAR, Fannie Mae is using a definition of a small bank that is consistent with the regulations implementing the Community Reinvestment Act (CRA). Under these regulations, small banks are defined as banks with total assets of less than \$1 billion.

²³ Some of these women-owned lenders also identified as another minority group such as African-American, Hispanic, Asian-Pacific or Indian-Alaskan.

²⁴ These agreements do not preclude members from doing business through other secondary market channels.

Community Lending Alliances

To specifically increase affordable finance opportunities for low- and moderate- income families and support lender's Community Reinvestment Act (CRA) goals, Fannie Mae forges single-family Community Lending Alliances with lender partners. In 2005, Fannie Mae executed 8 new Community Lending Alliances, while continuing to manage 17 existing alliances. Lender commitments through these community lending alliances totaled \$558 billion by year-end 2005 for loans expected to be delivered by 2010. The Community Lending Alliance menu offers lenders customized strategies that bring together products, technology, market outreach and analysis, bilingual marketing materials, diversity training and national partnerships that are appropriate for the lender's targeted markets. As a part of the alliance agreements, the lender and Fannie Mae also work together to identify opportunities to work with faith-based and other organizations that target immigrant communities, women-headed households, rural borrowers, and other underserved communities.

Alliances with Community Banks and Credit Unions

To reach community banks in 2005, Fannie Mae negotiated Affinity Agreements with the major banking trade associations, including **America's Community Bankers (ACB)**, **American Bankers Association (ABA)**, the **Independent Community Bankers Association (ICBA)**, and the **National Bankers Association (NBA)**. With their strong focus on housing and community development, member institutions share a common mission with Fannie Mae. Under the agreements, members who participate and are Fannie Mae seller/servicers have access to Fannie Mae's business and technology solutions. By year-end 2005, 396 institutions were participating in one of these four alliances.

Fannie Mae also recognizes the value credit unions bring in serving the needs of low- and moderate- income families and has forged an alliance with the **National Association of Federal Credit Unions**. By year-end 2005, 120 institutions were participating in this alliance. In addition, Fannie Mae customized a selling and servicing platform with **Prime Alliance Solutions, Inc.**, the largest single network—over 1,000—of credit union lenders.

Outreach to Community Development Financial Institutions (CDFI)

CDFIs are community-based financial institutions that support affordable housing development in underserved markets. As part of ACF, Fannie Mae provides investment capital to help such institutions—which include community banks, low-income designated credit unions,²⁵ affordable housing lending consortia, and housing related nonprofits—finance the development of affordable housing in neighborhoods traditionally underserved by the housing-finance industry. In 2005, Fannie Mae funded \$28.5 million in CDFIs, including debt and equity equivalent loan transactions totaling \$6.5 million, and deposit transactions and Certificate of Deposit Account Registry

²⁵ Credit unions receiving this special designation from the National Credit Union Administration must establish that a majority of potential members have a median household income less than 80 percent of the national household income or they make less than 80 percent of the average for all wage earners.

Service (CDARS) deposits of \$22 million. By year-end 2005, Fannie Mae had over \$67.6 million in outstanding balances to CDFIs.

Fannie Mae's outreach to minority-owned lenders is also conducted through partnerships as evidenced in the following examples:

- In 2005, Fannie Mae continued working with the **National Association of Real Estate Brokers (NAREB)**, a national trade association of minority real estate professionals, in a lending initiative with United International Mortgage and other lenders. Under this partnership, targeting minority borrowers, Fannie Mae purchased over \$237.3 million in loans that served 1,321 families in 2005. The NAREB initiative links NAREB members to affordable mortgage products and Fannie Mae's mortgage technology resources.
- In partnership with the **National Bankers Association (NBA)**, a trade association for minority- and women-owned banks, Fannie Mae helps provide access to secondary mortgage market products and services to support the expansion of business opportunities for NBA-member banks in order to increase homeownership opportunities for minority and underserved households. In 2005, Fannie Mae purchased \$1.4 billion and almost 13,000 loans under this partnership.

VIII. FANNIE MAE WORKS WITH PARTNERS TO INCREASE AFFORDABLE HOUSING OPPORTUNITIES

In accordance with 12 U.S.C. § 1723a(n)(2)(K), *describe the activities undertaken by the corporation with nonprofit and for-profit organizations and with State and local governments and housing finance agencies, including how the corporation's activities support the objectives of comprehensive housing affordability strategies under section 105 of the Cranston-Gonzalez National Affordable Housing Act*²⁶.

Fannie Mae submits the information below addressing this report requirement.

Because Fannie Mae does not do business directly with borrowers, partnerships are important in helping the company increase affordable housing opportunities. Some of the national organizations that the company partnered with in 2005 were **AARP, The Enterprise Foundation, United Cerebral Palsy, The Neighborhood Reinvestment Corporation, The National Council of La Raza**, and the **American Federation of Labor-Congress of Industrial Organizations**. In 2005, Fannie Mae purchased or securitized \$3 billion in mortgages with these national partners.

In addition to these groups, Fannie Mae also partnered with state and local governments, HFAs and for-profit organizations. The following pages illustrate some of the activities Fannie Mae undertook in 2005 with various types of partners. In some cases, the company's affordable housing activities with these partners—the provision of affordable housing, rental opportunities and rehabilitation, and the development of homeless strategies—aligned with a locality's housing affordability strategy as defined in the Cranston-Gonzalez National Affordable Housing Act.

- To serve people with disabilities, Fannie Mae in 2005 developed a national partnership with **United Cerebral Palsy (UCP)**. The initiative focuses on increasing housing opportunities through the UCP national affiliate network. Fannie Mae is providing support to the "HomeAbility" initiative to reach consumers and work with lenders to address barriers to homeownership. The sites selected in 2005 include: UCP Birmingham, UCP Rhode Island, UCP Southern Arizona, UCP South Florida, UCP East Central Florida, UCP Northwest Florida, and UCP South Central Pennsylvania. In addition, Fannie Mae is providing support to lenders that are offering the *Community Living Product* to affiliates that own and operate group homes.

²⁶ Under section 105, comprehensive housing affordability strategies include, among other things, efforts to address homelessness and meet the needs of homeless persons; the provision of housing for different categories of residents, such as very low-income, low-income, and moderate-income families, the elderly, single persons, large families, residents of non metropolitan areas, families who are participating in an organized program to achieve economic independence and self-sufficiency, and other categories of persons; combined efforts with private industry, nonprofit organizations and public institutions to deliver safe and adequate housing; encouraging public housing residents to become homeowners; and efforts to provide affordable housing through the production of new units, rehabilitation, or acquisition of existing units.

- In 2005, as part of a faith-based initiative, Fannie Mae entered into a three-year partnership with **Catholic Charities, USA (CCUSA)**, the largest private social services organization in the United States. CCUSA is a nonprofit national housing counseling intermediary organization headquartered in Alexandria, Virginia with 40 home counseling affiliate members in 21 states. Under the partnership, Fannie Mae is helping CCUSA build its capacity to provide home counseling services using Fannie Mae's *Home Counselor Online*TM and increase homeownership opportunities. CCUSA's objective is to provide home counseling to 6,000 individuals and help 900 families become homeowners. In addition, CCUSA is assisting Fannie Mae in identifying hurricane evacuees to be housed in Fannie Mae's Real Estate Owned properties. In 2005, \$17 million in loans were delivered by lenders working with CCUSA-counseled borrowers to Fannie Mae for purchase, helping 194 families become homeowners. Over 5,800 individuals received home counseling and education through CCUSA affiliates.
- In 2005, Fannie Mae partnered with **Countrywide Home Loans (CHL)** to help the lender grow and enhance its 2006 National Faith-Based Initiative. As part of this commitment, Fannie Mae's Community Business Centers are working with CHL local offices to identify local faith and community based groups and provide assistance as needed. The goals of this partnership in 2006 are to help 660 families secure mortgage financing. Key markets for 2006 include: Nashville, Tennessee; Los Angeles, California; Phoenix, Arizona; Seattle, Washington; and Baltimore, Maryland. In its first year, this partnership helped 21 families become homeowners. Fannie Mae purchased the \$3.25 million in mortgages associated with these loans.
- Fannie Mae committed \$100 million in 2005 to develop the *Nonprofit Developer Renovation Pilot*. This three-year pilot enables a qualified non-profit organization experienced in housing rehabilitation to purchase and renovate a 1- to 4- unit family residence for the purpose of having a low- to-moderate income home-buyer acquire the residence and assume the mortgage. The pilot has been launched in limited geographic locations and allows qualified home-buyers to reduce their closing costs due to loan assumption. The advantages for qualified participating nonprofit borrowers (following assumption of the nonprofit's mortgage) include: 1) attractive low cost financing that supports community revitalization efforts; 2) a single finance option for the acquisition, rehabilitation, and assumption of residential properties; and 3) attractive one-time assumable loan provisions for low- and moderate-income home-buyers.

Local Partnerships Working to Support Affordability Strategies Under the Cranston-Gonzalez Act

Fannie Mae seeks partners in cities, towns and states that will work with the company to bring housing opportunities to families across the country. Below are some examples that illustrate how these efforts with state and local governments support localities' affordable housing objectives under Section 105 of the Cranston-Gonzalez Act.

- ***The provision of housing for minorities in Minnesota.*** The **Emerging Markets Homeownership Initiative (EMHI)** was initiated by the state in response to the state's growing diversity and its minority homeownership gap. Partners in this effort include Fannie Mae, the **Federal Reserve Bank of Minneapolis** and the **Minnesota Housing Finance Agency**, as well as 50 other stakeholders representing the real estate industry and community groups. Throughout 2005, the group conducted and reviewed extensive quantitative and qualitative research on homeownership barriers and nationwide best practices and held thirteen focus groups and listening sessions across the state with successful and prospective homeowners to learn what strategies would best work to increase Minnesota's emerging market homeownership rate. The result of this effort is the creation of a business plan identifying strategies to create 40,000 new emerging market homeowners by 2012.

- ***Encouraging public housing residents to become homeowners and providing affordable housing through the production of new units, rehabilitation, or acquisition of existing units in Alexandria, Virginia.*** **Shiloh of Alexandria Federal Credit Union** is a faith-based credit union that provides affordable home financing options to those who live, work, and worship in Alexandria's Parker Gray community, including many low-income and minority families and others who live in Section 8 and public housing. Under this partnership, and with access to Fannie Mae's affordable lending products, Shiloh, the **City of Alexandria** and the **Alexandria Redevelopment and Housing Authority (ARHA)** are working to encourage public housing residents to become homeowners. Fannie Mae also provided a \$2.5 million dollar bridge loan to ARHA for its *Hope VI* Chatham Square development, and through a CDFI deposit, provided \$100,000 to support Shiloh's financial capacity to provide affordable housing opportunities for its members.

- ***Efforts to address homelessness and meet the needs of homeless persons.*** In 2005, Fannie Mae executed multi-year initiatives aimed at increasing the supply of permanent supportive housing for the chronically homeless and advancing the national goal of ending chronic homelessness. In addition to working with state and local governments through Fannie Mae's Community Business Centers, Fannie Mae partnered with groups such as the **Enterprise Social Investment Corporation**, the **National Equity Fund**, the **Corporation for Supportive Housing (CSH)** and the **National Alliance to End Homelessness (NAEH)**.
 - Fannie Mae provided \$2 million in grants to CSH and NAEH. This funding helped the two organizations build the capacity of more than 190 state and local government agencies and nonprofit organizations. Both organizations have advanced important policy and research agendas including the development of a baseline from which to measure progress toward ending homelessness at the state and local level and an analytic framework for evaluating the success of state and local government efforts to integrate and coordinate housing and human services funding.

- Community Business Centers engaged with local partners in various ways: supporting the development and implementation of local plans to end homelessness; leveraging expertise and partnerships to build the capacity of nonprofits and government to develop supportive housing; and advancing local supportive housing projects with financial investments and/or technical assistance. Highlights of this work are provided below.
- In Utah, Fannie Mae worked with two PHAs to create two major supportive housing projects for chronically homeless individuals.
- With the **City of Dallas** and the Mayor's Task Force to End Homelessness, Fannie Mae participated in the implementation phase of the city's *Ten Year Plan to End Homelessness*. Fannie Mae also joined **Central Dallas Ministries** and **The Urban League of Greater Dallas** to help create a development plan and finance options for new Single Room Occupancy housing in Dallas.
- To provide a wider range of housing options to homeless people with special needs, the **Kentucky Housing Corporation**, Fannie Mae and local nonprofit organizations worked together and identified supportive housing development opportunities.
- Fannie Mae provided technical assistance to the State of New York and **CSH** as they worked to create a new financing mechanism for supportive housing through the state Office of Mental Health. The financing allows the replacement of general obligation bonds with private activity bonds which allows the state and developers access to an additional 4 percent in tax credits. This benefit will generate significant savings for reinvestment in capital and service needs.

The American Communities Fund

The American Communities Fund[®] (ACF[®]) increases the supply of affordable rental and for-sale housing through short-term debt and equity investments and public finance bond purchases. The following are examples of ACF activities.

- **Acquisition, Development, and Construction.** Working with lenders, Fannie Mae provides enhanced liquidity by providing secondary market support through purchasing participations in acquisition, development, and construction loans, mini-perm loans, and letters of credit for residential housing.
 - ACF invested \$20.2 million through an acquisition, development and construction loan participation in Madrone at Empire Ranch, a 13-building, 219-unit condominium development in Folsom, California. Madrone's average projected price per unit is \$269,497 and includes 33 set-aside units, affordable to households earning between 58 percent and 66 percent of the area median income (AMI).

- **Public Finance & Preservation.** To help further the development and preservation of affordable housing, Fannie Mae partners with public entities including state and local Housing Finance Agencies (HFAs), as well as public housing authorities. Some of the company's financing tools for these developments include term loans, revolving and non-revolving lines of credit, and bridge loans.
 - With the use of *Modernization Express*[™], PHAs can leverage their future federal Capital Funds in order to accelerate the rehabilitation or redevelopment of their public housing stock. In 2005, ACF provided a \$2.3 million *Modernization Express* loan to the Housing Authority of the City of Newnan, Georgia to completely renovate a 51-unit property built in 1952. According to the Housing Authority, this development will be completed within 2 years with the ACF loan versus 12 years without the loan.

- **Equity Investment.** Working with residential builders and developers, ACF provides equity for single-family for-sale and multifamily rental housing developments.
 - In 2005, ACF invested \$5.7 million of equity in Oxford Trail, a new 204-unit rental townhouse development in Hampton, Virginia. Upon completion in the spring of 2007, Oxford Trail will increase the supply of quality rental housing in a community targeted for revitalization and be affordable to families with incomes at or below 100 percent of AMI.

IX. ADDITIONAL INFORMATION

In accordance with 12 U.S.C. § 1723a(n)(2)(L), *include any other information that the Secretary considers appropriate.* Fannie Mae submits the information below addressing this report requirement.

Given HUD's focus on helping borrowers affected by Hurricanes Katrina, Rita and Wilma, Fannie Mae is providing to the HUD Secretary, an update on the company's hurricane relief efforts.

Shortly after Katrina, Fannie Mae created the ***Katrina Task Force*** to work with partners in the region in providing housing solutions to affected communities.

Some highlights in 2005 include:

- communication of a mortgage relief policy to provide mortgage forbearance to borrowers facing hardship and uncertain financial circumstances;
- creation of underwriting flexibilities that will help people whose homes were destroyed or severely damaged acquire new homes;
- making available 1,500 properties for use as temporary shelter for displaced families;
- establishment of the Renaissance fund to support nonprofits who are helping evacuees with housing—\$942,500 awarded in 2005;
- new corporate policies encouraging Fannie Mae employees to support relief efforts in the region, including a donation policy, adopt-a-family program and extended volunteer leave to be used for relief efforts;
- efforts to keep lenders from reporting delinquencies related to Hurricane Katrina and Hurricane Rita to credit reporting agencies;
- repayment plans and modifications to help borrowers resume making their mortgage payments; and
- the opening of a loss mitigation office in Louisiana to assist servicers helping homeowners with decisions relating to property damage and their mortgage obligation.

X. CONCLUSION

In accordance with section (n)(1) of the Federal National Mortgage Association Charter Act, this AHAR was distributed to the House Committee on Financial Services and the Senate Banking, Housing and Urban Affairs Committee. Additionally, it will be available to the public at the company's headquarters located in Washington, D.C., and at the five Fannie Mae offices in Philadelphia, Pennsylvania; Atlanta, Georgia; Chicago, Illinois; Dallas, Texas; and Pasadena, California.