November 18, 2014

The Honorable Melvin L. Watt
Director
Federal Housing Finance Agency
Constitution Center
400 7th Street, SW
Washington, DC 20024

Dear Director Watt:

We believe that the government conservatorship of Fannie Mae and Freddie Mac (the Enterprises) is not a long-term solution to provide access to mortgages, and that Congress should enact comprehensive housing finance reform. However, we also believe that, in the interim, the Federal Housing Finance Agency (FHFA) can and should take steps to build a housing finance infrastructure for the future, enhance the role of private capital in the agency mortgage-backed security (MBS) market, and responsibly increase access to mortgage credit.

We write to highlight six areas in which FHFA action can further these goals:

1. Single Security: We applaud your work to develop a single security for Fannie Mae and Freddie Mac MBS that would replace the two distinct securities the Enterprises currently use. As you know, a single security for the Enterprises will create more liquidity in the market, unify representations and warranties, and standardize due diligence processes. A single security would also save Freddie Mac the hundreds of millions of dollars it pays annually to lenders to equalize the price offered by Fannie Mae.

   While we appreciate your work to date, we urge you to make the process more transparent and to solicit additional input from industry participants as you seek to converge a long list of the Enterprises' policies and reduce execution risks. Creating a more formal advisory body of market participants may help the FHFA better anticipate and address potential problems with the transition to a single security.

2. Common Securitization Platform: We support efforts to create the Common Securitization Platform (CSP) as an independent, transparent, and more efficient securitization infrastructure for the future of our housing finance system. On October 20, you stated that FHFA would like the CSP to serve "most of [the Enterprises']

current securitization functions." We believe it would be a mistake to develop a CSP that was compatible with only the infrastructure of the Enterprises. The CSP could be an important tool for encouraging responsible private-label MBS activity—but only if private issuers can use the CSP.

We hope you will pay close attention to this issue in your role as conservator. As of December 31, 2013, the Enterprises had spent $65 million on the CSP, and yet there is no detailed timeline for completing the CSP or total cost estimate. We ask you to make this information public and to maintain close oversight of the CSP development process.

3. Risk-Sharing Pilot Programs: As we in Congress continue to work toward comprehensive housing finance reform, we appreciate your efforts to expand the successful risk-sharing pilot programs that encourage the private sector to take on a growing amount of credit risk in the agency MBS market. In its recent strategic plans, FHFA has directed the Enterprises to develop pilot programs to transfer credit risk to private-sector investors. We support your recent decision to direct the Enterprises to triple the expected annual volume of such risk transfers to $90 million in unpaid principal balance per Enterprise.

   However, we believe there are ways to responsibly expand the risk-sharing programs. First, while the Enterprises have expanded the range of loans in the reference pools for these transactions to include loans with loan-to-value (LTV) ratios over 80 percent, we encourage you to push the Enterprises to expand this range further. Second, we encourage you to push the Enterprises to pursue additional front-end credit risk transactions, rather than retaining a small first-loss piece. Both of these changes will provide valuable information about how private investors evaluate the credit risk of various loan pools. We generally support continued experimentation in the pilot programs to widen investor participation while there is an opportunity to identify and learn from obstacles in a controlled risk environment.

4. Private Mortgage Insurance Eligibility Requirements (PMIERs): Creating specific, uniform, and public regulations for private mortgage insurers that insure loans guaranteed by Fannie and Freddie is an important step in preventing another housing crisis, but we urge FHFA to avoid unduly restricting access to credit and creating regulatory discrepancies. As FHFA finalizes its rulemaking on PMIERs, we encourage you to include the value of insurance premiums within the definition of available capital assets. Accounting for premiums in this way acknowledges that premiums are real assets that have historically served as a source of capital, and such an approach creates parity with the Federal Reserve's stress tests process. Excluding insurance premiums would likely lead mortgage insurance companies to raise prices on policies for borrowers with higher LTVs or lower credit scores, making it even more difficult for these borrowers to buy a home. Moreover, excluding insurance premiums could push more borrowers to Federal Housing Authority (FHA) loans, which would increase taxpayer exposure and raise costs for many borrowers.

Additionally, FHFA currently adds loan-level price adjustments (LLPAs) to guarantee fees on loans regardless of mortgage insurance coverage. We believe that FHFA can responsibly increase access to credit for low- and moderate-income borrowers by adjusting its LLPAs to reflect the new buffers provided by its updated PMIERs policies.

5. First Look Program: We urge you to find ways to expand and improve the First Look program. As you know, FHFA created the First Look program to ensure that owner-occupants had an opportunity to bid on the Enterprises' repossessed homes before the process was opened up to investors. FHFA correctly recognized that its sale of such homes to owners, rather than investors, could help families struggling to recover from the housing crisis while it would help stabilize the hardest-hit neighborhoods.

   While we applaud FHFA for developing this program, we believe there are ways to strengthen it. We ask you to consider whether there are ways to further encourage purchases by owner-occupants, such as increasing the amount of time they have to bid on such properties or lowering the prices of the homes during the First Look period. We also urge you to consider whether—in the absence of eligible owner-occupant purchasers—there are ways to encourage the sale of such homes to investors whose business plans prioritize homeownership. Finally, we ask that you collect and publicly disclose detailed performance data about the First Look program so that Congress and the public can monitor its effectiveness.

6. Credit Scores: We support strong underwriting guidelines for mortgages guaranteed by Fannie and Freddie, but we are interested in the opportunities that additional competition in the credit scoring market could create. FHFA announced recently that the Enterprises are studying alternatives to the FICO score and will be updating the version of the FICO score that is used. We encourage you to use this update as an opportunity to determine whether mortgage originators should be able to use alternative scoring models by FICO and its competitors. Certain non-FICO score models—as well as more recent versions of the FICO score itself—incorporate the latest data on creditworthiness and better reflect the impact of the financial crisis on borrowers' credit histories. We urge you to work with lenders to update credit models as soon as possible and to provide the necessary training to minimize errors during the furnishing process. We also ask that you brief Congress as soon as the study and report are completed.

We look forward to working with you on these and other issues.

Sincerely,

Mark R Warner

Elizabeth Warren

Mark R. Warner
U.S. Senator

Elizabeth Warren
U.S. Senator