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August 14, 2023

The Honorable Sandra L. Thompson
Director
Federal Housing Finance Agency
400 Seventh Street SW
Washington, DC 20024

RE: Fannie Mae and Freddie Mac Single-Family Mortgage Pricing Framework

Dear Director Thompson:

The Credit Union National Association (CUNA) represents America's credit unions and their more than 135 million members. On behalf of our members, we are writing in response to the Federal Housing Finance Agency's (FHFA) Fannie Mae and Freddie Mac Single-Family Mortgage Pricing Framework Request for Input (RFI).[1]

Background

With respect to the single-family mortgage pricing framework for loans acquired by Fannie Mae and Freddie Mac (collectively the Enterprises), guarantee fees are used "to cover the administrative costs, expected credit losses, and the cost of capital associated with guaranteeing single-family mortgage loans."[2] Guarantee fees generate revenue for the Enterprises and are "the key revenue component in determining economic returns earned from their core credit guarantee business."[3]

Guarantee fees fall into two separate classes. Ongoing guarantee fees are based on the loan product and are collected each month while the loan is being repaid.[4] Upfront guarantee fees, which Fannie Mae calls loan level price adjustments (LLPAs) and Freddie Mac calls credit fees in price, are based on different factors like loan-to-value (LTV) ratio and credit score.[5] They are paid once upon the delivery of the loan to the Enterprises and are generally higher for those loans considered to be

[1] https://www.fhfa.gov/Media/PublicAffairs/PublicAffairsDocuments/Single-Family-Mortgage-Pricing-Framework-RFI.pdf.
[2] *Id.* at 6.
[3] *Id.* at 4.
[4] *Id.* at 5.
[5] *Ibid.*

riskier.[6] Both the ongoing and upfront guarantee fees are usually paid by borrowers as a part of the interest rate or points.[7]

Over the past few months, FHFA announced several changes to the Enterprises' upfront guarantee fees. Those changes included:

- Increasing upfront guarantee fees for high balance loans or for second home loans in January 2022, and exempting first-time homebuyers at or below 100 percent of area median income (AMI) in high-cost areas and affordable housing program borrowers from those fees;[8]
- Eliminating upfront guarantee fees in October 2022 for some first-time homebuyers (e.g., those at or below 100 percent of AMI or below 120 percent in high-cost areas), low-income borrowers, and borrowers in underserved communities;[9]
- Updating the upfront guarantee fee pricing grids in January 2023 to better align with the Enterprise Regulatory Capital Framework (ERCF);[10]
- Announcing a new upfront fee for certain borrowers with a debt-to-income (DTI) ratio above 40 percent.[11]

The January 2023 changes generated significant debate. Despite concerns that the revised pricing grids punished borrowers with good credit and provided discounts for borrowers with bad credit,[12] commenters noted that the revised pricing grids appeared to align with credit risk.[13] The DTI-based upfront fee was rescinded by FHFA, however, after stakeholder feedback regarding the operational

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6 *Ibid.*
7 *Ibid.*
8 *Id.* at 10.
9 *Ibid.*
10 *Id.* at 11.
11 *Ibid.*
12 *See generally* Jim Parrott, No, Fannie Mae and Freddie Mac Aren't Penalizing People with Good Credit to Help People with Bad Credit (Apr. 25, 2023), *available at* https://www.urban.org/urban-wire/no-fannie-mae-and-freddie-mac-arent-penalizing-people-good-credit-help-people-bad-credit.
13 *See* The Current Mortgage Market: Undermining Housing Affordability with Politics: Hearing Before the H. Fin. Servs. Comm., 118th Cong. (statement of Edward J. DeMarco) ("As for the recent changes, they appear to be reasonably aligned with credit risk after accounting for the new capital framework, the cost of private mortgage insurance, and recognition that the riskiest cells in the grid represent very few Enterprise purchases."), *available at* https://docs.house.gov/meetings/BA/BA04/20230517/115954/HHRG-118-BA04-Wstate-DeMarcoE-20230517.pdf & (statement of Janneke Ratcliffe) ("In summary, the pricing is a natural outcome of the FHFA's pricing approach, which is a direct function of capital (return on capital target), expected risk, expenses, and special fees. We argue that the May 1 grid changes are largely motivated by implementing the ERCF and factoring in PMI coverage and capital. Following that logic, distortions, if any, in the pricing structure reflect distortions, if any, in the capital requirements."), *available at* https://docs.house.gov/meetings/BA/BA04/20230517/115954/HHRG-118-BA04-Wstate-RatcliffeJ-20230517.pdf.

challenges of implementing the fee.[14] In the press release rescinding the DTI-based upfront fee, FHFA advised that it would request input from the public about single-family guarantee fees.[15]

General Comments

CUNA applauds FHFA for engaging the public to obtain information that will inform its policy decisions about how it will oversee the single-family pricing framework of the Enterprises. As not-for-profit, financial cooperatives, credit unions have a specified mission "to meet the credit and savings needs of consumers, especially persons of modest means."[16] During 2022, credit unions originated $237 billion in first-lien mortgages, and they sold more than 16 percent of those mortgage loans into the secondary market.[17] America's credit unions depend on the liquidity, stability, and affordability that the Enterprises provide. The guarantee fees set by the Enterprises, therefore, affect credit unions and their ability to provide their members with affordable mortgage credit. Because of the wide-reaching effects that pricing decisions like setting guarantee fees can have on the safety and soundness of the Enterprises and equitable and sustainable access to mortgage credit, transparency and public engagement is vital to ensure that the Enterprises can continue to satisfy the purposes for which they were created.

Transparency Regarding the ERCF and Guarantee Fees

For the sake of transparency, CUNA urges FHFA to provide more data to the public about how the application of the ERCF will affect guarantee fees before making any policy decisions on the single-family pricing framework for the Enterprises. In the most recent annual report on the Enterprises' guarantee fees, FHFA noted that the Conservatorship Capital Framework (CCF) rather than the ERCF was used to analyze single-family capital requirements.[18]

Of the three different categories of costs that affect guarantee fees, the cost of capital is generally seen as the most consequential.[19] Moreover, the cost of capital depends on the return on capital that is targeted by the Enterprises and the amount of capital they need to hold, and FHFA expects the Enterprises to establish guarantee fees based on the amount of capital that would be needed to be well capitalized under the ERCF.[20] As the return on capital or the regulatory capital that needs

[14] Press Release, FHFA, FHFA Announces Rescission of Enterprise Upfront Fees Based on Debt-To-Income (DTI) Ratio (May 10, 2023), *available at* https://www.fhfa.gov/Media/PublicAffairs/Pages/FHFA-Announces-Rescission-of-Enterprise-Upfront-Fees-Based-on-Debt-To-Income-Ratio.aspx.
[15] *Ibid.*
[16] *Credit Union Membership Access Act*, Pub. L. No. 105-219, § 2(4), 112 Stat. 913, 914 (1998).
[17] National Credit Union Administration (NCUA) 2022 Credit Union Call Report Data; CUNA analysis.
[18] FHFA, Fannie Mae and Freddie Mac Single-Family Guarantee Fees in 2021 (Nov. 2022) at 8, *available at* https://www.fhfa.gov/AboutUs/Reports/ReportDocuments/GFee-Report-2021.pdf.
[19] *See* Donald H. Layton, Government Mortgage Interest Rates: A Serious Discussion about the Intertwined Topics of Risk Adjustment and Cross-subsidies, *available at* https://furmancenter.org/thestoop/entry/government-mortgage-interest-rates-a-serious-discussion-about-the-intertwined-topics-of-risk-adjustment-and-cross-subsidies (finding that the cost of capital made up two-thirds of the average guarantee fee in 2021).
[20] RFI, *supra* note 1, at 6.

to be held increases, guarantee fees need to increase as well to ensure that they are covering the costs they are designed to cover.

And this implicates the ERCF because the amount of capital the Enterprises need to hold under the ERCF is much greater than what was required under the CCF.[21] Furthermore, the amount of capital required under the ERCF has been calculated to be much greater than what is required by the Enterprises' stress tests.[22]

To have a meaningful and informed discussion about guarantee fees, the public needs to know how the ERCF will affect guarantee fees, considering that the 2022 report on guarantee fees that will be released later this year will be the first to look at guarantee fees through the lens of the ERCF. CUNA reiterates its previous comments from earlier ERCF proposals and urges that the FHFA undertake and release an analysis of the pricing impacts of the ERCF before moving forward with policy decisions on the Enterprises' single-family pricing framework. This added level of transparency can help stakeholders better understand the ERCF's effects on guarantee fees and pricing, including whether the ERCF and its effect upon guarantee fees affect the Enterprises' ability to effectively meet their affordable housing mission while providing liquidity and stability to the mortgage market.[23]

Transparency Regarding Targeted Returns

More transparency is also needed with respect to the targeted returns that FHFA has set for the Enterprises, and CUNA encourages FHFA to furnish more information about the Enterprises' single-family targeted returns. The targeted returns on capital are used to mitigate against the underpricing of risk.[24] The Enterprises, under their Charter Acts, have the ability to accept lower economic returns for mortgage loan activity directed at low- and moderate-income families as long as those lower returns are reasonable.[25] While FHFA has indicated that the Enterprises are earning "mid-single digit returns on single-family loan acquisitions in the aggregate, the RFI does not specify the return targets for different types of loans. Understanding what targets apply to different single-family mortgage loans across the spectrum of loans eligible for purchase by the Enterprises can provide stakeholders with more transparency into how the return on capital impacts guarantee fee decision-making.

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[21] *See* RFI, *supra* note 1, at 7 ("In general, the ERCF capital requirements are substantially higher than the requirements under which the Enterprises previously operated.").

[22] *See* Layton, *supra* note 19 ("But the most robust hard evidence that the ERCF is just too high – with $319 billion required across both companies, per the FHFA – is that this result is so wildly inconsistent with that of the government-mandated and -designed 'severe adverse' stress test results, which recently showed at most just a $4.5 billion loss.").

[23] *See* Letter from Celeste Mellet Brown, EVP & Chief Fin. Officer, Fannie Mae, to Alfred M. Pollard, General Counsel, FHFA (Aug. 28, 2020) at 4-5, *available at* https://www.fhfa.gov/SupervisionRegulation/RegulationFederalRegister/Pages/Commentonrule.aspx (explaining how "the burdens of higher, less risk-sensitive capital requirements, may fall on the borrowers least able to afford them.").

[24] RFI, *supra* note 1, at 11.

[25] 12 U.S.C. § 1716; 12 U.S.C. § 1451 note.

Components of Guarantee Fees and the ERCF

In considering whether upfront guarantee fees should be eliminated or whether future guarantee fee changes should only be made to the ongoing guarantee fees, more information about the effectiveness of the upfront guarantee fees and risk-based pricing at creating cross-subsidies would be informative.[26] This level of visibility can help stakeholders to understand how cross-subsidization through the use of guarantee fees is used by the Enterprises. But whether upfront guarantee fees are eliminated or frozen does not change the fact that total guarantee fees may need to increase due to the higher level of capital required by the ERCF.

Conclusion

Thank you for this opportunity to provide input on the Fannie Mae and Freddie Mac Single-Family Mortgage Pricing Framework Request for Input. If you have questions or if we can be of any assistance, please do not hesitate to contact me at (202) 603-1985 or dpark@cuna.coop.

Sincerely,

David Park
Senior Director of Advocacy & Counsel

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[26] *See generally* Donald H. Layton, Government Mortgage Interest Rates: A Serious Discussion about the Intertwined Topics of Risk Adjustment and Cross-subsidies, *available at* https://furmancenter.org/thestoop/entry/government-mortgage-interest-rates-a-serious-discussion-about-the-intertwined-topics-of-risk-adjustment-and-cross-subsidies (suggesting that FHA and VA loans could more effectively cross-subsidize certain loans by more robust adjusting of pricing based on risk).