Real Estate Finance in America
2015

Dodd-Frank Mortgage Rules:

The *Dodd-Frank Wall Street Reform and Consumer Protection Act* (Dodd-Frank) was the most far-reaching financial market reform ever implemented. Dodd-Frank has produced thousands of pages of new regulations impacting the real estate finance market. While many of the reforms were prudent, it is also clear that some of the rules implemented have produced significant, unintended consequences for borrowers and the real estate finance industry's efforts to serve them. Five years after enactment, targeted reforms to Dodd-Frank and its rules are needed to protect and expand the availability of capital for consumers and businesses, lower the cost of residential and commercial mortgage financing, and preserve access to mortgage credit for hard working Americans and for the businesses that drive the economy.

The Mortgage Bankers Association (MBA) recommends that federal policymakers support the following:

- Expand access to Qualified Mortgages (QMs) by ensuring all QMs are classified as "safe harbor" loans;
- Ensure that lower income borrowers can get access to QMs by raising the small balance loan threshold to $200,000 or less (up from $100,000 or less);
- Permit residential mortgage lenders to correct and compensate borrowers for inadvertent mistakes in Debt-to-Income (DTI) ratio calculations and other technical errors;
- Exclude residential settlement charges of affiliated business arrangements from the QM points and fees limits;
- Exclude from risk retention low–risk, single asset, single borrower commercial mortgage-backed securities (MBS);
- Modify the Qualified Commercial Real Estate Loan definition to include additional commercial real estate loans that reflect time-tested and industry standard underwriting practices;
- Allow greater flexibility for how risk retention purchasers can structure the first-loss commercial MBS position; and
- Exclude multifamily loans from the *Home Mortgage Disclosure Act* loan data reporting regime because these loans are transacted on a business to business basis.

CFPB Reforms:

A significant component of Dodd-Frank was its establishment of the Consumer Financial Protection Bureau (CFPB), an independent federal agency charged with protecting consumers from harm within the financial sector — including the real estate finance market. In its brief existence, the CFPB has already implemented a majority of the rulemakings mandated by Dodd-Frank and has assumed interpretive authority over most existing mortgage finance rules. Complicating the important transition to this new regulatory regime has been the CFPB's unwillingness to provide clear, written supervisory guidance and remediation plans to assist the industry in its compliance efforts. Instead, the CFPB has largely relied on enforcement actions, excessively broad civil investigation demands, and an overly adversarial investigative process to promote industry compliance.

The CFPB's "regulation by enforcement action" strategy opens up activities not previously believed to be prohibited to potential challenge by the CFPB, state regulators, attorneys general, and the plaintiffs' bar. This enforcement-first approach to promoting compliance has proven exceedingly costly and ultimately lessens the availability and affordability of mortgage credit for creditworthy borrowers.

In order to allow the real estate finance industry to serve the market with greater confidence, MBA recommends that federal policymakers require the CFPB to:

- Issue clear, written supervisory guidance and "FAQs" to better guide industry compliance;
- Establish a "remediation program" to allow institutions that do not have a history of violations to resolve supervisory concerns through non-public supervisory actions, including full remediation to affected consumers; and
- Strengthen due process protections for companies involved in CFPB inquiries, permitting the full participation of counsel without undue limits on such consultations.

Structural reforms to the CFPB's governance and oversight are also warranted to ensure the CFPB remains open, transparent and accountable:

- The CFPB's budget should be subject to the congressional appropriations process, instead of being funded directly by the Federal Reserve; and
- The CFPB should be governed by a five-member, bipartisan commission, instead of its current single-director format.

Future of the Secondary Mortgage Market:

Fannie Mae and Freddie Mac (the Government Sponsored Enterprises, or GSEs) play a central role in the real estate finance market, as they provide liquidity to industry institutions and purchase mortgages to package in MBS. These actions create stability and affordability for creditworthy borrowers, investors and institutions alike. Since the 2008 financial crisis, the GSEs have been held in conservatorship by the federal government and managed by the Federal Housing Finance Agency. While at the time necessary, GSE conservatorship is not a healthy "end-state" for the real estate finance market.

MBA believes that thoughtful, comprehensive GSE reform is necessary to protect the future interests of taxpayers and participants in the real estate finance market. Accordingly, MBA recommends that federal policymakers support the following core principles in any laws and regulations designed to reform the secondary mortgage market:

- An explicit federal guarantee for MBS to promote liquidity and stability, and to ensure that U.S. mortgage markets remain connected to global capital through all economic cycles;
- Protection for taxpayers through deep credit enhancement that puts significantly more private capital in a first-loss position, backed by a Federal Deposit Insurance Corporation-like federal insurance fund in the event of catastrophic losses;
- A single, highly liquid security delivered through a common securitization platform in the single-family market that provides an efficient means of hedging interest rate risk for long-term fixed mortgages;
- Preservation of key GSE infrastructure — technology, systems, data and people — by transferring them to any new entities created by GSE reform;
- Equitable, transparent and direct access to secondary market programs for lenders of all sizes and business models;
- Build upon the strengths of the GSEs' multifamily businesses that have incorporated substantial risk sharing with private capital and disciplined underwriting; and
- Support GSE multifamily and lender activities that provide liquidity and stability through a government guarantee at the security level, to provide liquidity in all market cycles in competition with a range of capital sources that finance multifamily rental housing.

Government Program Stability:

The Federal Housing Administration (FHA), Department of Veterans Affairs (VA), Department of Agriculture's (USDA) Rural Housing Service and the Government National Mortgage Association (Ginnie Mae) are all critical to supporting homeownership for many first-time homebuyers, low- to moderate-income families, military service members and veterans, and minorities; importantly, they also provide critical support for workforce and affordable rental housing. Moreover, the direct loans and loan guarantees of these government programs serve an important, counter-cyclical role in economic downturns for borrowers in the real estate finance system. Despite the gradual return of private capital, these public programs maintain a heightened role in today's real estate finance market. To ensure these programs properly protect the taxpayer, they need funding for the necessary technology, systems, and human capital to account for current volumes in a financially sound manner.

MBA recommends that federal policymakers support the following:

- Appropriate funding for FHA, VA, USDA's Rural Housing Service, and Ginnie Mae that allows each government program to responsibly account for their elevated volume levels;
- Funding provided through the congressional appropriations process, not through higher consumer premiums or fees that will ultimately be borne by consumers;
- Sensible supervision and enforcement policies that hold lenders accountable for quality originations, without exposing them to outsized penalties that discourage lenders from serving each program's mission;
- Pricing of FHA insurance that protects the Mutual Mortgage Insurance Fund against adverse selection and continues to build the Fund's critical capital reserves; and
- The provision of sufficient resources for FHA's workforce and affordable rental housing programs, and FHA multifamily policies and procedures that reflect the competitive landscape and economic trends.

Stable Tax Policy:

MBA supports efforts to provide enhanced and efficient capital availability to the residential and commercial/ multifamily real estate markets. Moreover, MBA supports stable, consistent and predictable tax policies that promote long-term economic growth and allow households and businesses to make long-term economic decisions, which is the foundation of strong real estate markets. Such tax policies will serve the broader goals of stimulating new jobs and economic expansion. MBA has concerns over changes to tax policies that would discourage prudent investment in real estate and supports preserving the current tax treatment of the following:

- The deductibility mortgage insurance premiums for first-time, low-and middle-income homebuyers;
- The deductibility of residential mortgage interest and state and local real estate property taxes paid by homeowners as part of their itemized deductions;
- The Low-Income Housing Tax Credit; and
- The Like-Kind Exchange.

Regulatory Capital Framework:

Regulatory capital policy is a significant lever employed by policymakers that impacts the availability and cost of real estate financing. The implementation of key elements of Basel III and related capital rules in 2015 has introduced a new regulatory regime for bank lending for commercial real estate construction loans and lines of credit. In addition, the Basel capital framework imposes punitively high capital requirements on residential mortgage servicing rights (MSRs) that raise servicing costs and discourage many institutions from servicing the mortgages they have originated. MBA supports a regulatory framework for banks, life insurance companies and other capital sources that provides liquidity to the real estate markets, promotes the efficient allocation of capital within institutions, and strengthens sound risk management practices that do not unnecessarily stifle real estate lending. Key changes needed to the regulatory capital treatment of real estate finance assets include:

- Reducing the harsh capital treatment of residential mortgage servicing assets by lowering the risk weight and raising the allowance on MSRs that can be counted as Tier 1 capital;
- Reforming the capital treatment for commercial real estate to ensure it does not deter construction lending; and
- Establishing liquidity rules that appropriately treat structured securities, including commercial and residential MBS.