Center for Responsible Lending

Comment on The Federal Housing Finance Agency's Enterprise Equitable Housing Finance Plans - Request For Input

October 25, 2021

The Center for Responsible Lending (CRL)[1] submits this comment on the Request For Input on the Equitable Housing Finance Plans for Fannie Mae and Freddie Mac, the Government Service Enterprises (GSEs). This important proposal and other Federal Housing Finance Agency (FHFA) fair lending and racial equity initiatives are critical to the GSEs supporting badly needed affordable housing and reducing the racial homeownership gap.

In this comment, we first summarize the current racial disparity in homeownership caused by longstanding and continuing discrimination. Next, we discuss the challenges and opportunities in redressing these disparities. While the racial homeownership gap and the causes of it have received more attention in recent years, there has been less discussion of the specific measures that can reduce this gap and their likely impact. Finally, we suggest steps to maximize the role of the GSEs in this endeavor.

The Magnitude and Scope of the Racial Homeownership Gap

The racial homeownership gap in the United States manifests longstanding policies and practices that have left families of color with a fraction of the personal and intergenerational wealth of others.[2] Our housing market and the racial homeownership gap are products of centuries of past and ongoing discrimination throughout the housing and lending process.[3]

This has resulted in huge racial disparities in homeownership, with the current gap at historic levels. At 74% for whites and 44% for Blacks, the over 30% gap in homeownership is wider today than it was in the 1960s.[4]

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[1] CRL is a nonprofit, non-partisan research and policy organization dedicated to protecting homeownership and family wealth by working to eliminate abusive financial practices. CRL is an affiliate of Self-Help, one of the nation's largest nonprofit community development financial institutions. For 40 years, Self-Help has created asset-building opportunities for low-income individuals, rural communities, women, and families of color. In total, Self-Help has provided over $9 billion in financing to 172,000 homebuyers, small businesses, and nonprofit organizations and serves more than 160,000 mostly low-income families through 72 credit union branches in North Carolina, California, Florida, Illinois, South Carolina, Virginia, Washington, and Wisconsin.

[2] This comment focuses on the GSEs' impact on homeownership. They also play an essential role in addressing the acute affordable and fair housing rental crisis as well. *See* Michael Calhoun and Lewis Ranieri, *Government-sponsored enterprises at the crossroads* (February 19, 2021), Brookings Institution, https://www.brookings.edu/wp-content/uploads/2021/02/20210219_CRM_CalhounRanieri_FINAL.pdf.

[3] Testimony of Ms. Nikitra Bailey, Executive Vice President, Center for Responsible Lending, Before the United States House of Representatives' Committee on Financial Services, *Justice for All: Achieving Racial Equity Through Fair Access to Housing and Financial Services* (March 10, 2021), https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-testimony-nikitra-bailey-hfsc-hearing-10mar2021.pdf.

[4] Laurie Goodman and Jung Zhu, *By 2040, the US Will Experience Modest Homeownership Declines. But for Black Households, the Impact Will Be Dramatic*, Urban Institute (January 21, 2021), https://www.urban.org/urban-wire/2040-us-will-experience-modest-homeownership-declines-black-households-impact-will-be-dramatic.

The disparity goes beyond the basic homeownership rate. Families of color enter homeownership significantly later, and own homes for less time, than white homeowners. Black homeownership typically begins eight to ten years later than white homeownership.[5] This has a profound impact on the amount of equity and wealth that families build through homeownership. For example, with 4% annual house value appreciation, a ten-year delay in starting homeownership results in 45% less equity growth for a family.

Another major factor that exacerbates the disparity in home equity growth is that families of color are more likely to have a distressed sale of their homes. A recent study found that Black and Hispanic homeowners are both more likely to experience a distressed sale and to live in neighborhoods where distressed sales erase more house value.[6]

Notably, these disparities are not projected to decline under current policies and the mere passage of time. Urban Institute modeled the likely future levels of homeownership in the US over the next 20 years. It projected that both Black homeownership would decline over time and the racial homeownership gap would increase.[7] These projections were made before the COVID crisis, which has disproportionately impacted families of color and put more who were able to become homeowners at risk of losing their homes.

Given the central role that homeownership plays in family wealth, these racial disparities are major drivers of the huge racial wealth disparity in the country. The median Black household has only one-eighth the wealth of the median white household, and "[h]omeownership plays a bigger role in creating wealth for Black families than it does for white families" as house equity forms nearly 60% of total net worth for Black homeowners compared with 43% for whites.[8] Without addressing these homeownership factors, we will not close the racial wealth divide.

[5] Jung Hyun Choi, Alanna McCargo, Laurie Goodman, *Three differences between black and white homeownership that add to the housing wealth gap*, Urban Institute (February 28, 2019), https://www.urban.org/urban-wire/three-differences-between-black-and-white-homeownership-add-housing-wealth-gap.
[6] Amir Kermani and Francis Wong, *Racial Disparities in Housing Returns* (September, 2021), National Bureau of Economic Research, https://www.nber.org/papers/w29306.
[7] Laurie Goodman and Jung Zhu, *By 2040, the US Will Experience Modest Homeownership Declines. But for Black Households, the Impact Will Be Dramatic*, Urban Institute (January 21, 2021), https://www.urban.org/urban-wire/2040-us-will-experience-modest-homeownership-declines-black-households-impact-will-be-dramatic.
[8] Alanna McCargo and Jung Hyun Choi, *Closing the Gaps: Building Black Wealth through Homeownership* (November 2020, updated December 2020), Urban Institute, at pp. 1-2, https://www.urban.org/sites/default/files/publication/103267/closing-the-gaps-building-black-wealth-through-homeownership_1.pdf.

Challenges to Building Homeownership Rates and Equity

The continuing impacts of these housing disparities, primarily the lack of family and intergenerational wealth, are not only manifestations of longstanding discrimination and the resulting racial homeownership gap but also deepen the chasm and create significant obstacles to closing it. They leave families with less wealth and fewer reserves to absorb financial shocks, while other discrimination renders these families more susceptible to such shocks. This results in less financial resiliency and therefore burdens families with lower credit scores. Almost twice as many Blacks (65.3%) as whites (33.6%) have no credit score or one below 620.[9]

Racial disparities in income and wealth also make it much harder for families of color to secure down payments to qualify for loans.[10] This reduces the number of families that can qualify for a mortgage, and for those who can, delays the time until that can be achieved.[11]

These factors also make it harder for lenders to serve families of color. Families with lower reserves or incomes are subject to more financial shocks, are more likely to need to stretch out their debt payments due and face greater risk of default. The impact of this on loan performance is significant. For GSE loans, the likelihood of default increases by more than a factor of ten between the lowest and highest credit categories.[12] Even for mortgages that do not default, delinquencies dramatically increase servicing costs for lenders and often make mortgages unprofitable even if they ultimately cure.[13]

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[9] Jung Hyun Choi, Alanna McCargo, Michael Neal, Laurie Goodman, Caitlin Young, *Explaining the Black-White Homeownership Gap: A Closer Look at Disparities across Local Markets*, Urban Institute (October 2019, updated November 2019), at p. 8 and figure 7, https://www.urban.org/sites/default/files/publication/101160/explaining_the_blackwhite_homeownership_gap_2.pdf.

[10] Christelle Bamona, *Hardship for Renters: Too Many Years to Save for Mortgage Down Payment and Closing Costs*, Center for Responsible Lending (April 2021), at p. 2 and fn. 6, https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-mortgage-downpayment-7apr2021.pdf; Bradley Hardy, Jonathan Morduch, William Darity, Jr., Darrick Hamilton, *Wealth Inequality, Income Volatility, and Race*, American Economic Association (December 2018), at pp. 2, 14, 16-17, https://www.aeaweb.org/conference/2019/preliminary/paper/KZG69HbE.

[11] U.S. Department of Housing and Urban Development, *Barriers to Minority Homeownership*, https://archives.hud.gov/reports/barriers.cfm; *Bank programs seek to widen the path to Black homeownership*, Washington Post (October 29, 2020), https://www.washingtonpost.com/realestate/bank-programs-aim-to-widen-the-path-to-minority-homeownership/2020/10/28/ff5edcfa-12f7-11eb-ad6f-36c93e6e94fb_story.html.

[12] VantageScore, *Credit Score Basics, Part 1: What's Behind Credit Scores?* (September, 2011), https://www.transunion.com/docs/rev/business/financialservices/VantageScore_CreditScoreBasics-Part1.pdf.

[13] Laurie Goodman, *Servicing Is an Underappreciated Constraint on Credit Access* (December, 2014), Urban Institute, https://www.urban.org/sites/default/files/publication/33451/2000049-Servicing-Is-an-Underappreciated-Constraint-on-Credit-Access.pdf; Bonnie Sinnock, *Will servicers be able to better control costs in the next downturn?* (February 26, 2020), National Mortgage News, https://www.nationalmortgagenews.com/news/will-servicers-be-able-to-better-control-costs-in-the-next-downturn.

Finally, there is a scarcity of resources to address housing issues resulting from a lack of public acknowledgement of the scope of the racial homeownership gap and the broader affordable homeownership and rental crisis. There is a resulting hesitancy to invest sufficiently in affordable housing measures at a scale that will effectively address the crisis. This housing gap and shortage was at extreme levels before the COVID-19 crisis and even more families are at risk today. More than 20 million households in 2019 paid over 30% of their incomes for rent, with 62% of households earning under $25,000 expending over half their incomes on rent.[14] However, today's U.S. Department of Housing and Urban Development (HUD) budget, adjusted for inflation, is less than half what it was in the 1970s.

Currently, there is an effort in Congress as part of the reconciliation bill to secure down payment assistance for first-generation home buyers. Advocates sought $100 billion, and current estimates are that the final amount may be in the $10 billion to $30 billion range. At even the top of this range, $30 billion would create a total of 500,000 new Black and Latino homeowners, combined, over ten years. While this improves the lives of these families, it increases the homeownership rate for each of these groups a total of 1.5 percentage points over the entire ten-year period, resulting in a very small reduction in the 30% racial gap in homeownership. Even at $100 billion of down payment assistance, this would move homeownership rates only 5 percentage points over ten years and just return Black homeownership to the level before the 2008 financial crisis.

In summary, centuries of discrimination have produced stark racial disparities in wealth that presents a formidable challenge to overcome and requires a greater commitment, far larger resources, and a strategic approach.

Opportunities to Close the Homeownership Gap

First, there must be vigorous fair lending law enforcement throughout the market to eradicate ongoing discrimination. Studies and testing continue to show discrimination in many aspects of the home lending and purchase market. This is a shameful continuation of centuries of discrimination. Ongoing discrimination also reduces families' incomes and assets.[15] In addition,

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[14] Joint Center for Housing Studies of Harvard University, *The State of the Nation's Housing 2020*, https://www.jchs.harvard.edu/sites/default/files/reports/files/Harvard_JCHS_The_State_of_the_Nations_Housing_2020_Report_Revised_120720.pdf.

[15] Freddie Mac, *Racial and Ethnic Valuation Gaps in Home Purchase Appraisals* (September, 2021), http://www.freddiemac.com/fmac-resources/research/pdf/202109-Note-Appraisal-Gap.pdf.

the HUD Office of Fair Lending oversees GSEs' fair lending practices through enforcement of the *Fair Housing Act* and should vigorously do so.[16]

Providing mortgage credit on equal terms is a long overdue moral imperative, but its impact alone on closing the racial homeownership gap will be relatively small since it does not address the cumulative and continuing impacts of past discrimination that are major drivers of the gap. The Urban Institute analyzed the racial homeownership gap, controlling for factors that are closely tied to historic discrimination. The factors were credit score, income, and marital status.[17] Controlling for these factors combined explained nearly 90% of the national racial homeownership gap.

Stated differently, simply equalizing racial homeownership rates among different credit score categories will have limited impact due to the historic discrimination that created and perpetuates huge racial disparities in the placement of families in those categories. Due to discrimination, families of color are disproportionately in the credit and income categories with low homeownership rates.

To make meaningful progress, there must be new efforts and approaches together with dramatically increasing existing programs like down payment assistance.

Necessary Steps for Progress

<u>Inclusive lending</u>. The first priority is for the GSEs to lead the market in establishing fair and inclusive home lending. Historically, the GSEs have, as a result of their essential role in mortgage finance, set market standards and have significant influence in the market. Due to their government charters, statutory advantages, and size in the market, they offer lenders the most profitable option for selling many of their loans.[18] This GSE standard setting is seen in mortgage terms, structure of mortgage securities, standards for mortgage servicing, and even the forms that are used for mortgage notes and deeds of trust. Given the GSEs' dominance,

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[16] *See Memorandum of Understanding By and Between HUD and FHFA Regarding Fair Housing and Fair Lending Coordination* (August 12, 2021), https://www.hud.gov/sites/dfiles/PA/documents/FHFA-HUD-MOU_8122021.pdf.
[17] As discussed above, credit scores are profoundly influenced by historic family and intergenerational wealth. Income is likewise impacted by educational and other opportunities closely tied to wealth, as well as ongoing discrimination. Marital status is likewise impacted by these factors. A Federal Reserve study found that economic and demographic factors explained almost all of the racial differences in marital status of women. *See* Elizabeth Caucutt, Nezih Guner, and Christopher Rauh, *Incarceration, unemployment, and the black–white marriage gap in the US* (April 6, 2019), The Centre for Economic Policy Research, https://voxeu.org/print/64035.
[18] These advantages include the two congressional charters that are held by Fannie and Freddie, the previously implicit government backing of their liabilities, including their securities and debt (now explicit through the PSPA agreements), exemption from state taxation, and special security filing treatment.

these standards pervade the mortgage market and even apply to loans that are not sold to the GSEs.

But the GSEs currently do not require inclusive lending for the primary mortgage market loans that they purchase. Those selling loans through a government-supported window should be expected to serve their local markets via inclusive marketing and portfolios sold to the GSEs.

The GSEs should also ensure that broad use of machine learning, artificial intelligence, and big data are not used to perpetuate discrimination and thwart inclusive lending. For example, these measures can target potential borrowers working in the service industry and label them as more susceptible to risk from events like the current COVID-19 crisis. These protections should apply to the GSEs' own policies and the loans that they purchase.

Allocation of catastrophic risk. The GSEs should also lead the mortgage market in better managing and pricing catastrophic mortgage risk. Catastrophic risk is by far the biggest part of mortgage risk and of the cost passed on to consumers through the guarantee fees that the GSEs charge lenders, particularly for borrowers with lower credit scores. Catastrophic risk is so costly because the losses in these stress periods are so large compared to more ordinary times that it requires the GSEs to set aside considerable capital to protect for these events, and holding that capital is very expensive. These costs reflect systemic events, such as pandemics or broad market failures, rather than individual borrower behavior

The resulting higher mortgage costs passed on to consumers disqualifies potential homebuyers, makes their mortgages harder to sustain, and slows the growth of their home equity. CRL has previously submitted comments on FHFA capital rules and will comment on the pending capital rule proposal. We also discuss it here since the allocation of capital costs is one of the most impactful GSE racial equity issues.

FHFA and the GSEs should modify pricing to lower mortgage costs. Overall, the GSEs should pool more of the mortgage risk and keep their pricing as level as possible across credit categories without driving loans out of the GSE market through adverse selection. FHFA took some steps in recent capital rulemaking towards this and should do far more.[19] GSE pricing includes loan level price adjustments (LLPAs), an upfront fee charged by the GSEs on loans based on their credit categories. These LLPAs also should not be recharged on GSE mortgage

[19] *See* CRL et. al on proposed capital rule, *Comment to the Federal Housing Finance Agency on Enterprise Regulatory Capital Framework* (August 31, 2020), https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-comment-gse-capital-rule-31aug20.pdf.

refinances where the fee was already collected on the original loan by that GSE, as the GSEs are simply reissuing the loan at a lower interest rate and typically with a lower risk.

Capital costs for catastrophic risks are also a major driver of the cost of private mortgage insurance, which is often an even larger contributor to the cost of mortgages for low-wealth families than LLPAs, and is paid by homeowners who put down less than 20% of the purchase price on a GSE mortgage. FHFA's Private Mortgage Insurer Eligibility Requirements (PMIERs) rule setting out capital standards for mortgage insurers of GSE loans has a similar impact on mortgage pricing for homeowners as the GSE capital rule. The above standards regarding the amount of required capital and the even distribution of cost should also be applied to this insurance.

Differential pricing affects access to mortgage credit by increasing the price, sometimes significantly, for some borrowers relative to others, and there is evidence that price acts as a barrier to entering today's mortgage market. While Fannie Mae's guidelines allow it to purchase loans with credit scores down to 620 and LTV ratios of up to 97 percent, very few loans purchased by Fannie have these characteristics. Just 4 percent of Fannie Mae's 2020 single-family loan purchases had borrowers with credit scores below 680,[20] and just 1.1 percent had both a borrower with a credit score of under 660 and an LTV over 80 percent in 2016.[21]

One reason is that excessive risk-based pricing by both the GSEs and private mortgage insurers cumulatively add significant cost to loans for borrowers with lower credit scores and less wealth for down payments.[22] For instance, the combination of LLPAs and mortgage insurance premiums add over 270 basis points to the annual cost of a mortgage for a borrower with a credit score of 620 and an LTV of 97 percent.[23] Reducing differential pricing is likely to facilitate the GSEs' loan purchases in underserved markets.

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[20] Fannie Mae, United States Securities and Exchange Commission - Form 10-K (December 31, 2020), at p. 98, https://www.fanniemae.com/media/38271/display.
[21] Fannie Mae, 2016 Credit Supplement (February 17, 2017), at p. 7, https://www.fanniemae.com/media/26776/display.
[22] For a more detailed discussion of the levers that affect pricing and the distribution of pricing for credit risk, *see* Mike Calhoun and Sarah Wolff, *Who Will Receive Home Loans, and How Much Will They Pay?*, Urban Institute (2016), http://www.urban.org/policy-centers/housing-finance-policy-center/projects/housingfinancereformincubator/mike-calhoun-and-sarah-wolff-who-will-receive-home-loans-and-how-much-will-theypay.
[23] 350/4+186=273.5 basis points. Fannie's Mae's LLPA for this combination of credit score and LTV is a one-time fee of 350 basis points. *See* page 2, https://www.fanniemae.com/content/pricing/llpa-matrix.pdf. We assumed a LLPA multiple of 4 to convert this upfront fee to an ongoing cost comparable to the MI premium. The GSE ongoing cost equals 87.5 basis points (350/4). Borrower paid MI from Genworth for this combination of credit score and LTV is a continuing fee of 186 basis points. *See* https://new-

<u>Reduce avoidable losses in crises through GSE policies</u>. FHFA and the GSEs should institutionalize steps to reduce avoidable losses in crises. A good example was the interventions in the current crisis. The GSEs not only led the market in instituting long-term forbearance for borrowers affected by COVID-19 before Congress acted, but they also implemented the *Coronavirus Aid, Relief, and Economic Security Act* (CARES Act) forbearance provisions in a manner that greatly enhanced the beneficial impact of forbearance. Key was offering deferral of suspended payments until the mortgage pays off rather than requiring them to be repaid in a lump sum or shortly after the end of the forbearance period.

FHFA also directed the GSEs to cover servicers' advancement of these suspended payments to investors after four months of payments. This prevented a severe financial strain on non-bank servicers that could have disrupted the mortgage market. These steps helped individual homeowners facing stress from the COVID-19 crisis and stabilized the mortgage market and the economy. Going forward, FHFA and the GSEs should institutionalize such support. The resulting reduction in stress losses should lower the required capital levels for the GSEs and, in turn, mortgage costs for borrowers.

<u>Permanently remove caps on GSE single-family mortgage support</u>. CRL commends FHFA and the Department of the Treasury for suspending the recent PSPA amendments that cap the support the GSEs can provide for single family mortgage loans.[24] We urge the parties to permanently remove these caps. The single-family loan limit restricts the GSEs' purchase of so-called "high-risk" loans to 6 percent of their purchases and 3 percent of their refinance mortgages. These are defined as loans with at least two of the following characteristics: greater than 90 percent loan-to-value ratios (LTV), greater than 45 percent debt-to-income levels (DTI), and a borrower credit score below 680. While the GSEs are currently inside these caps, this January 2021 PSPA amendment went in the wrong direction. The GSEs should be doing more to address the affordable housing crisis and to make responsible mortgage credit available to underserved families of color.[25] FHFA and the GSEs should not impose additional roadblocks on responsible lending.

content.mortgageinsurance.genworth.com/documents/ratecards/national/monthly_premium_mi/00460.Natl.Monthly.Fixed.BPMI.0719.pdf. While the GSEs do offer affordable loan products with lower fees for borrowers below 80% AMI, these products constitute a very small percentage of purchases overall. *See* https://sf.freddiemac.com/working-with-us/originationunderwriting/mortgage-products/home-possible (Home Possible); https://singlefamily.fanniemae.com/originating-underwriting/mortgage-products/homeready-mortgage (Home Ready).

[24] Press Release, Treasury Department and Federal Housing Finance Agency Suspend Certain Requirements Under Preferred Stock Purchase Agreements with Fannie Mae and Freddie Mac (September 14, 2021), https://home.treasury.gov/news/press-releases/jy0350.

[25] *See*, e.g., discussion in Michael Calhoun and Lewis Ranieri, *Government-Sponsored Enterprises at the Crossroads*, The Brookings Institution (Feb. 2021), https://www.brookings.edu/wpcontent/uploads/2021/02/20210219_CRM_CalhounRanieri_FINAL.pdf.

Reduce default risk of individual mortgages in normal times. The current risk environment, as evidenced by a historic recession and the current pandemic over a dozen years, is different from previous decades and the responses differ too. Even ongoing risks are different in today's economy than fifty years ago when long-term employment stability and income growth were more prevalent. Today's gig economy and rapidly changing job market subject families to far more risk and volatility. Also, the growth of new households in the US is primarily from families of color who enter the market with less generational and personal wealth. Despite these transformational changes, our mortgages still largely reflect a previous Ozzie and Harriet world.

To address mortgage risks in the normal business cycle, the GSEs should lead development of mortgage products and practices to better accommodate income volatility and other common financial shocks.[26] Important steps taken after the Great Recession improved the loss mitigation practices of the GSEs and their servicers, providing more time for consumers to recover from mortgage delinquencies and more affordable modification options. Further measures and tools are needed to prevent mortgages from becoming delinquent and to cure them quickly without expensive distressed loan servicing. This would expand mortgage availability and sustainability for more families. As noted above, the current very high cost of servicing delinquent mortgages is a major obstacle to mortgages being offered in the first place to families considered at risk. The GSEs should specifically pursue and test products and programs to provide protection against financial shocks, such as income loss, major home repairs, and other types of events.

Mortgage servicing. Reform is also needed in handling distressed mortgages and the overall payment structure for mortgage servicing. This has also not sufficiently evolved to reflect the changed economic and risk environment of today and the future mortgage market. The level and distribution of the costs of distressed mortgage servicing unnecessarily creates barriers to more inclusive lending. FHFA and the GSEs should also help lead servicing reform efforts.

Streamline refinances. To help reduce the cost of buying or refinancing a home, and to stimulate the economy, FHFA and the GSEs should create a streamline refinance program for low-balance mortgages to ensure rate term refinances are more available, not more costly, for lower-income families who would save greatly on mortgage payments. Unfortunately, the refinance surge is not reaching lower-income and lower-wealth families adequately, and least of all borrowers refinancing smaller loan balances. Higher income and white Americans have disproportionately benefited from the current low interest rates. This is reflected in the average

[26] *See* JP Morgan Chase & Co., *Trading Equity for Liquidity: Bank Data on the Relationship Between Liquidity and Mortgage Default* (June 2019), https://www.jpmorganchase.com/institute/research/household-debt/report-trading-equity-for-liquidity.

credit scores of borrowers creeping yet higher in 2020.[27] Moreover, the GSEs should not charge any LLPAs on a streamline refinance, as LLPAs were already paid at purchase.

Greater resources and better targeting needed. Given the scale of efforts required to reduce the racial homeownership gap and provide affordable housing, the needs far exceed the available resources to meet them.[28] This requires additional investment and prioritizes resources being utilized and targeted to maximize their impact. Down payment assistance remains a major barrier to homeownership and additional measures should also be pursued.[29] And given the importance of getting families of color into homeownership earlier, structuring programs to maximize the number of borrowers reached in the next few years should be encouraged. The programs should also utilize methods such as first-generation home buyer eligibility and Special Purpose Credit Programs to implement programs.

Finally, the Federal Housing Administration (FHA) is an essential provider of home financing, particularly for first-time homebuyers and families of color. It benefits from government support and not having to pay returns to private investors to offer lower priced loans and down payments. FHA and FHFA should coordinate their programs to maximize the total affordable housing and racial equity impact of combined FHA and GSE lending.[30]

Housing supply. As the current restricted supply of housing shows, expanding housing supply is key to meeting affordable housing and racial equity goals. This should start with avoiding unnecessary losses of affordable homes through the sale of real estate owned (REO) properties to investors by recycling these homes back into single-family homeownership. The GSEs should examine all of their policies in disposition of REO to ensure that they support purchase by

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[27] Urban Institute, *Housing Finance At a Glance: A Monthly Chartbook* (February 2021), https://www.urban.org/sites/default/files/publication/103746/housing-finance-at-a-glance-a-monthly-chartbookfebruary-2021_0.pdf; Urban Institute, *Housing Finance At a Glance: A Monthly Chartbook* (December 2020), at p. 17, https://www.urban.org/sites/default/files/publication/103430/housing-finance-at-a-glance-a-monthly-chartbookdecember2020.pdf (FICO scores for banks and nonbanks in both GSE and Ginnie Mae segments increased over the course of 2019 and the first eleven months of 2020, due to increased refinance activity; this activity is skewed toward higher FICO scores); Urban Institute, *Housing Finance At a Glance: A Monthly Chartbook* (February 2020), at p. 17, https://www.urban.org/sites/default/files/publication/101766/february20chartbook202020.pdf.

[28] Joint Center for Housing Studies of Harvard University, *The State of the Nation's Housing 2020*, https://www.jchs.harvard.edu/sites/default/files/reports/files/Harvard_JCHS_The_State_of_the_Nations_Housing_2020_Report_Revised_120720.pdf.

[29] Michael Calhoun and Lewis Ranieri, *Government-sponsored enterprises at the crossroads* (February 19, 2021), Brookings Institution, https://www.brookings.edu/wp-content/uploads/2021/02/20210219_CRM_CalhounRanieri_FINAL.pdf.

[30] Borrowers of color have often been steered to FHA loans due to bias when they qualify for GSE loans at a lower cost. Also, especially in today's high demand/low supply housing market, FHA borrowers have been disadvantaged in having their offers considered and accepted. This illegal steering must be prevented through aggressive fair lending law enforcement.

owner-occupants and nonprofit organizations to the maximum extent possible. Recently revised provisions gave nonprofits greater access to sales of non-performing loans. But most of the homes included in bulk sales that become REO will continue to overwhelmingly go to investors who take the properties out of homeownership, notwithstanding FHFA's first-look to owner-occupant requirements for these loans that become REOs.

Second, the GSEs should continue to support financing for residential home development. The GSEs should provide equity investments to support the preservation of naturally occurring affordable housing projects. In addition, they should purchase construction-to-permanent financing mortgages before construction commences to facilitate new construction of both single- and multifamily housing.

Plans requirements must be specific. In the design and implementation of the GSE Equitable Housing Finance Plans, and the affordable housing plans, FHFA must ensure that the plans are sufficiently specific and accountable so that they are not diluted. Otherwise, financial considerations will push the GSEs to reach the targets at the lowest cost even when this reduces the program's impact. The mortgage market is very competitive for the GSEs and others and, as a result, participants are subject to adverse selection if their standards and pricing vary from competitors. This puts pressure on the GSEs to avoid such adverse selection if their affordable housing measures would make the other GSE more appealing to lenders, such as with less monitoring or inclusiveness requirements, and this creates a strong disincentive to implement these measures.

FHFA should impose a level playing field with specific requirements so that a GSE is not disadvantaged for implementing new initiatives that further racial equity. Therefore, the GSEs' plans need to specify not only what the goals are but measures for how they will be met. Certainly, flexibility to encourage innovation and accommodation to different circumstances is helpful, but a lack of standards actually limits flexibility as it leaves unchecked the pressure for the GSEs not to be disadvantaged compared to each other.

Conservatorship. Finally, the direction and incentives for the GSEs must be changed to encourage these goals. Even in conservatorship, the GSEs are for-profit companies with management that has a fiduciary duty to the shareholders to maximize share value. However, the GSEs' public mission is the reason for their establishment, special privileges, and ongoing support, including the massive government cash infusions in the Great Recession. The strong fiduciary pressure on the GSEs to generate income and retain capital to facilitate exiting conservatorship and demonstrate long term profitability for investors, must be offset by comparable and countervailing specific requirements to advance their public mission.

Fortunately, in conservatorship FHFA has the necessary authority and tools to direct the GSEs to greatly expand their affordable housing and racial equity efforts and impact as part of their requirements to fulfill their public mission. The *Housing and Economic Recovery Act* (HERA) provides the FHFA Director during conservatorship the authority of the shareholders, officers, and directors of the GSEs, and it authorizes the Director to take action that is in the best interest of the GSEs or the agency, which is entrusted with ensuring the GSEs fulfill their missions.[31]

Conclusion

Meaningful progress on racial homeownership is essential for equitable housing and is key to narrowing the racial wealth gap. This will only come with sustained action and resources that reverse and offset the damage of the past. Progress requires new and enhanced policies, expanded existing and new programs, and a substantial, sustained investment of additional resources.

[31] *See Housing and Economic Recovery Act of 2008*, section 1367(b)(2)(J)(ii).