CALIFORNIA ASSOCIATION OF REALTORS®

September 12, 2013

U.S. Senate Committee on Banking, Housing, and Urban Affairs
534 Dirksen Senate Office Building
Washington, DC 20510

2013 OFFICERS

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Re: California Association of REALTORS® Comment Letter for Committee Hearing on Essential Elements of Housing Finance Reform

Chairman Tim Johnson and Ranking Member Mike Crapo;

On behalf of the 160,000 members of the California Association of REALTORS® (C.A.R.) I am submitting the following comments to the Senate Banking, Housing, and Urban Affairs Committees for the hearing on Essential Elements of Housing Finance Reform. I would like to first thank you for holding this hearing and recognizing the importance of this issue to the nation's housing market and economic recovery. REALTORS® play a unique role in the housing market as the only service provider to work with the homebuyer and home seller through the entire process. Additionally, REALTORS® also live in the communities where they work. Because of this, REALTORS® are in a position to see the impact mortgage financing has on the real estate transaction, the community and the housing market. It is imperative that Congress act judiciously in its attempt to reform the mortgage market so as not to hinder the current recovery and ensure the uninterrupted availability of affordable mortgage capital in all market conditions.

Essential Elements of a Housing Finance Market Reform

A mortgage finance reform bill must be applicable beyond today's current markets; it must anticipate various cycles and changes to the mortgage and housing market over the next fifty years. Unlike so many other areas of the economy, shelter is not an option for families but a necessity, and as such it is imperative that housing be protected as much as possible from capital market cycles. We respectfully submit this should be a guiding principle when writing mortgage finance legislation.

<u>A government guarantee is necessary for the mortgage market:</u>
Since the Great Depression the government has played a major role in guaranteeing liquidity in the housing market. This has ensured safe and affordable mortgage capital is available in all market conditions. Recent history has shown that market cycles have produced times when private capital has taken on a larger market share and times when private capital has fled the market. It is during the latter times that the government has played its most important role.

Over the last six-years the government has guaranteed about 90 percent of mortgage originations. <u>This wasn't because it priced private capital out of the market, it was because private capital chose not to invest in real estate.</u> In addition to the last six years, history has shown other times when private capital has pulled

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away from housing. They include the early 1990's, the early 1980's, and even for the decade following WWII. It isn't a bad thing, quite the contrary, that private capital should invest in markets they believe will provide the best return, but because shelter is a necessity the government must be there to step in during down markets.

America cannot afford to do away with a guaranteed intermediary

Lastly, there has been no evidence presented that the private market could or even wants to assume 100 percent of the credit risk and interest rate risk of the nation's housing finance market. Going as far back as the 1990's, private capital never took on more than 60 percent of the nation's mortgage market regardless of market cycles. The idea that private capital could now take over 100 percent of the mortgage market is simply unfounded given the current size and structure of the U.S. housing finance market. Even in today's recovering market, the private sector mortgage activity is inadequate. Abandoning established government mechanisms, especially without a very gradual transition, can't be done if the recovering market is to be maintained.

C.A.R. does not believe a government portfolio should be used as a source of profits. C.A.R. also opposes the purchase of risky private-label-securities for the portfolio. The purpose of the portfolio should be as an additional tool that will insulate the availability of mortgage capital from market cycles, and not "bail out" or subsidize the risky loans of private sector speculators.

High-cost areas should have higher loan limits:

As far back as 1980, Congress recognized the cost of housing in certain states to be higher than those of other states, and provided higher loan limits to ensure residents would have equal access to affordable mortgage capital. The policy of allowing a state's median home price to determine its qualification for higher loan limits allowed for a more equal number of homebuyers to have access to affordable financing that was protected from capital market cycles. It provided greater housing market stability and allowed for private capital to participate in as large or as small of a market share as they wanted. This thoughtful, fact-based adjustment should be maintained.

California is a high-cost state with a median home price of over $433,000 dollars. Currently, over 22 million Californians live in 15 counties with a median home price above the national loan limit of $417,000; seven of those counties have loan limits above the current $625,500 cap. These are not mansions being bought by millionaires, these are the median home prices and these are the prices average Californians must pay for homes. Their ability to purchase a home would be drastically restricted if they were forced into a "one size fits all" loan limit based on a single national median home price.

FHA legislation should be kept separately:
C.A.R. supports S. 1376, The FHA Solvency Act of 2013, passed out of this committee earlier this year. The committee was correct in separating the two issues of FHA reform and GSE reform. While both issues deal with mortgage finance, they are separate and very complex issues. Combining the two would muddy the waters of both and threaten the future of both reform efforts. C.A.R. believes the Senate should stay the course and maintain handling the two issues separately.

Mandatory risk sharing should not be codified:
C.A.R. is not opposed to risk sharing, to the contrary, we believe risk sharing can be an effective credit enhancer and a tool to protect tax-payers. C.A.R.'s concern with making the option a requirement is the belief that private capital will not be available for the risk-sharing mandate in all market conditions. To date we know of only one GSE risk sharing transaction. There are simply too many unknowns with risk sharing to make it mandatory, for example; will private capital be willing to take a first loss position on the entire MBS market in all market conditions? We know from history, 2007, 1991, 1980, and other down markets where private capital fled the market that the answer is "no." We also know that the absence of private capital can go on for years, not months. C.A.R. is concerned that codifying a mandate would destroy liquidity in mortgage markets, and leave loans on bank portfolios if they are unable to find adequate private capital to take the first loss position on a MBS.

C.A.R. suggests instead that proposed legislation "instruct" or "direct" risk sharing at an amount the private market will provide. And if private capital is unwilling to take the first-loss position or will not do so at a reasonable price then risk sharing should not be required.

The regulator should have necessary authority to react to all market conditions:
A new housing finance market will need a regulator with the authority and maneuverability to react to changing market conditions. C.A.R. is opposed to proposals that would either limit the ability of regulators to react quickly to a down market, or which would prevent countercyclical measures from being implemented over long periods of time. Any new regulatory agency will need the authority to handle not just the day-to-day operations, but the ability to set long term rules and guidelines without constant re-approval.

The government entity needs to be able to portfolio loans:
Any government entity, whether it be a replacement of Fannie Mae and Freddie Mac, or a reforming of the government sponsored enterprises (GSE) must include the ability to hold mortgages in a portfolio. This serves two vital purposes; 1) it allows the entity to pull non-performing loans from mortgage backed securities (MBS) if necessary; 2) it allows loan originators to sell their loans and recapitalize even if there is no secondary market demand for their MBS. As past market cycles amply demonstrate, there will be times when investors do not want to take on the

interest rate risk (this was the case in the 1980s). When this happens it is important that the lenders still be able to sell their mortgages so they can recapitalize their books for new originations. Only a governmental entity can counter the dangers of these cycles and provide security for homeowners.

Thank you for your consideration of our comments. C.A.R. believes there is nothing more important to the housing recovery than availability of mortgage financing. Congress should pass housing finance reform legislation that appropriately addresses the issues we have discussed above. If it does not there will be times when qualified homebuyers, through no fault of their own, will no longer be able to count on their lenders being able to provide a home loan.

Sincerely,

Don Faught
President, California Association of REALTROS®

Cc: Diane Feinstein, CA U.S. Senator
Barbara Boxer, CA U.S. Senator