HOUSING FINANCE REFORM

Who are the housing GSE's?

The housing Government Sponsored Enterprises (GSEs) -- Fannie Mae, Freddie Mac and the Federal Home Loan Banks (FHLBanks) -- have been, and remain, critical components of the U.S. housing finance system. They were created by Congress to support mortgage market liquidity and help address affordable housing needs.

The GSEs have operated with implicit government backing that allows them to raise funds at favorable rates, which ultimately benefits mortgage borrowers. The housing GSE system functioned well for decades, but the past few years have seen unprecedented turmoil. Freddie Mac and Fannie Mae were found to have serious accounting irregularities that required them to be placed under government conservatorship and receive direct federal support. The FHLBanks on the other hand have not experienced these difficulties and continue to operate normally.

The regulatory system for the GSEs underwent a complete overhaul during this period, with all GSEs now under the oversight of a single regulator, the Federal Housing Finance Agency (FHFA). As the conservator for Fannie Mae and Freddie Mac, FHFA is trying to balance the significant role that Fannie and Freddie have played during the housing downturn by supporting mortgage markets and mitigating mortgage foreclosures, while reducing taxpayer losses and minimizing future risk exposure.

Current Status and NAHB's Plan

NAHB is a strong proponent of housing finance reform and feels significant changes should occur in the conventional market, where Fannie Mae and Freddie Mac currently account for almost all activity. With the GSEs still operating under conservatorship, serious housing finance reform policy discussions are underway in congress, but there is not yet widespread agreement on the specific components of reform. Indeed, while the House of Representatives is considering legislation to completely remove the government role in the housing market, the Senate is currently engaged in bipartisan efforts to preserve the federal support necessary for the proper functioning of the U.S. housing market. While the approaches differ greatly, nearly everyone agrees that reform is critical to the economic recovery of this nation.

NAHB supports steps to increase the role of private capital in the U.S. housing finance system but does not believe the market can rely exclusively on private sources. History clearly shows the limitations of the private mortgage market. During bad times private mortgage credit evaporates leaving qualified buyers high and dry and the housing market in a free fall. Indeed, in the aftermath of the housing downturn, investors have been reluctant to invest in mortgage securities without government backing. Wall Street expects that this share would shrink dramatically without a government backstop. NAHB believes federal support is particularly important in continuing the availability of the affordable 30-year fixed-rate mortgage, which has been a staple of the U.S. housing finance system since the 1930's.

To help move this debate forward, NAHB has made recommendations to Congress outlining a plan by which Fannie Mae and Freddie Mac would be gradually phased into a private-sector-oriented system, where the federal government's role is clear, but its exposure is limited. Federal support should be limited to catastrophic situations where carefully calibrated levels of private capital and insurance reserves are depleted before any taxpayer funds are employed to shore up the mortgage market.

Congressional Action

A government role is essential for multifamily housing as well. More than one-third of Americans live in rental housing, and demand for rental housing is expected to increase.

Legislation pending before the House of Representatives (H.R. 2767, the *Protecting American Taxpayers and Homeowners*, or PATH Act), would take the nation in the wrong direction. The PATH Act seeks to remove any government role from the conventional mortgage finance market and to drastically reduce the Federal Housing Administration's role in the housing market. While the private sector must assume a greater role in the mortgage marketplace, unless we maintain a federal role to help absorb catastrophic risk, the U.S. mortgage and housing markets will suffer negative consequences.

The Cato Institute has suggested that the PATH Act would slash the market for 30-year mortgages from 70 percent to 40 percent. Mark Zandi's analysis finds that the share of 30-year home loans in the U.S. could plunge below 20 percent. Reducing the number of households that are eligible for mortgage credit would lead to an economic chain reaction that could throw the nation back into a recession. Fewer qualified buyers would lower housing demand, which would place more downward pressure on home prices. It only takes a 6 percent drop in home values to wipe out $1 trillion in household wealth.

Unlike the House, Republican and Democrat Senators are currently working together in a bipartisan manner to craft legislation that would maintain a limited federal backstop to the nation's housing finance system, very similar to the plan NAHB proposed. Legislation introduced by Senator Bob Corker (R-TN) and Senator Mark Warner (D-VA), S. 1217, the *Housing Finance Reform and Taxpayer Protection Act of 2013*, would maintain a proper level of government support, and is a good step forward in the debate. Moving forward, NAHB will work with Democrat and Republican leaders in the Senate Banking Committee as they craft bipartisan legislation similar to the Corker/Warner proposal for consideration by the full Senate.

Take Action

- House of Representatives - oppose the PATH Act (H.R. 2767) currently pending consideration by the House of Representatives.
- Senate - Support bi-partisan legislation that would maintain a limited federal backstop to the nation's housing finance system.

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