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HOUSING FINANCE REFORM: ESSENTIAL ELEMENTS OF THE MULTIFAMILY HOUSING FINANCE SYSTEM

HEARING

BEFORE THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE

ONE HUNDRED THIRTEENTH CONGRESS

FIRST SESSION

ON

EXAMINING THE RECOMMENDATIONS FOR THE FUTURE OF THE MULTIFAMILY HOUSING FINANCE MARKET CURRENTLY SERVED BY FANNIE MAE AND FREDDIE MAC MULTIFAMILY SECURITIES

OCTOBER 9, 2013

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WEDNESDAY, OCTOBER 9, 2013

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
Washington, DC.

The Committee met at 10:02 a.m., in room SD–538, Dirksen Senate Office Building, Hon. Tim Johnson, Chairman of the Committee, presiding.

OPENING STATEMENT OF CHAIRMAN TIM JOHNSON

Chairman JOHNSON. I call this hearing to order.

Today's hearing is continuing work on housing finance reform. This hearing will focus on the future of the multifamily housing finance market currently served by Fannie Mae and Freddie Mac multifamily securities.

The topic of multifamily housing finance is often overlooked in broader housing finance reform discussions, so today's hearing will bring this important issue into focus for the Committee. Multifamily housing is a key source of housing to the one-third of Americans who are renters. Demographic trends indicate there will be growing demand for multifamily housing in the years to come. Without an adequate supply of such housing, the affordability challenges facing many American families will only increase.

Fannie Mae and Freddie Mac multifamily securities help ensure broad access to credit across the whole market, serving small communities as well as larger cities on the coasts. It also makes housing affordable to families with a range of incomes. Through the recent financial crisis, these securities performed very well, with collective default rates peaking at less than 1 percent. They also provided liquidity to the multifamily sector at the height of the financial crisis when other sources of financing withdrew.

In our discussion today, I hope to highlight the key elements of the enterprises' multifamily strengths and weaknesses before and during the crisis to help inform our discussions of the future. The hearing gives us a chance to examine recommendations from our witnesses and what essential elements of our Nation's multifamily housing finance system should be going forward, including the potential roles of private capital and the Government guarantee, as well as how a new system should be structured and regulated.

I also look forward to considering what reforms in this area will mean for rural and small communities like those in my State and how it may affect small lenders and small properties as well as the workforce and affordable housing supply. At a minimum, we must make sure that broad access to credit is preserved in a new housing finance system going forward.

With that, I turn to Senator Crapo for his opening statement.

STATEMENT OF SENATOR MIKE CRAPO

Senator CRAPO. Thank you, Mr. Chairman.

Today we continue our series of hearings on housing finance reform. More than 5 years after the collapse of the housing market and the beginning of the bailouts of Fannie Mae and Freddie Mac, reforming our housing system is urgently needed and is a top priority for this Committee.

As we have noted in previous hearings, we are now holding a number of hearings examining the specific aspects of our housing finance system. This morning we take an in-depth look into multifamily housing, which refers to loans secured by properties with five or more residential units.

Although the multifamily market is much smaller than the single-family market with around $850 billion in outstanding mortgage debt, it still serves as a vital source of housing for more than 15 million American households across the country.

The multifamily market differs significantly from the single-family market. While Fannie Mae and Freddie Mac suffered enormous losses on single-family mortgages during the recent crisis, multifamily loans at both enterprises experienced delinquency rates of less than 1 percent. There are some important lessons we can learn from the enterprises' multifamily activities as we continue to work for reform of the single-family market.

Fannie and Freddie both require private sector risk sharing and high-quality underwriting on all guaranteed multifamily loans. Fannie Mae employs strict underwriting guidelines and requires originators to retain risk through its delegated underwriting and servicing system or program. Freddie Mac underwrites all its own loans and shares risk with secondary market participants through structured transactions known as "K deals". These types of policies have helped ensure that Fannie Mae and Freddie Mac only guarantee mortgages of high credit quality in the multifamily space.

Still, by insuring mortgages against default, whether under the conservatorship or under a new system that involves a Government guarantee, the Government is inherently putting taxpayer money at risk.

The Government's market share of multifamily housing spiked dramatically during the financial crisis from around 30 percent of originations in 2006 to around 80 percent in 2009. This number has moderately decreased, but Fannie and Freddie along with the FHA still finance a significant portion of multifamily originations, and the GSEs' market shares remain at a higher level than has historically been the case.

Historically, private sources of capital, including banks, life insurance companies, the commercial mortgage-backed securities market, and real estate investment trusts, have played an important role in multifamily markets.

Given the exceptional performance of multifamily loans, it is worth investigating whether we can do more to encourage the private sector to finance more of these loans on its own, thus shrinking the Government's footprint in the market.

We all agree that the status quo in housing finance is not an option. I have seen a number of thoughtful proposals offering different views on how best to structure the future multifamily market, and I am interested to hear your views on these proposals, along with any recommendations regarding how to best reform the system in a way that ensures a liquid, well-functioning housing market.

How should the future multifamily housing system be structured? Who in the market should play the various roles needed for a healthy secondary market? MBA supports well-capitalized private insurers while other groups have advocated private issuer guarantors. How should any guarantee fee be priced to ensure that the Government is not underpricing risk and crowding out private capital?

I look forward to working with Chairman Johnson and the other Members of the Committee toward a bipartisan agreement that addresses these critical issues.

Thank you, Mr. Chairman.

Chairman JOHNSON. Thank you, Senator Crapo.

I understand that there is an event at 11:30 that many of our Members will be attending this morning, so we will need to adjourn this hearing at 11:15. Because of this, opening statements will be limited to myself and Ranking Member Crapo.

I would like to remind my colleagues that the record will be open for the next 7 days for additional statements and other materials.

I would now like to introduce our witnesses that are here today.

Our first witness is Mr. Thomas Bozzuto, who is chairman and CEO of the Bozzuto Group. Mr. Bozzuto is also representing the National Multi Housing Council and the National Apartment Association.

Mr. E.J. Burke is executive vice president and group head of the KeyBank Real Estate Capital. Mr. Burke is also here on behalf of the Mortgage Bankers Association.

Mr. Shekar Narasimhan is managing partner of Beekman Advisors.

And, finally, we have Ms. Terri Ludwig, president and CEO of Enterprise Community Partners, Incorporated.

Mr. Bozzuto, you may proceed.

STATEMENT OF THOMAS S. BOZZUTO, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, THE BOZZUTO GROUP, ON BEHALF OF THE NATIONAL MULTI HOUSING COUNCIL AND THE NATIONAL APARTMENT ASSOCIATION

Mr. BOZZUTO. Thank you, Senator Johnson, Ranking Member Crapo, and distinguished Members of the Committee. On behalf of NMHC and NAA, I thank you for this opportunity. My name is Thomas S. Bozzuto, and I am chairman and CEO of the Bozzuto Group, a 25-year-old privately held integrated real estate company. During my career, I have been responsible for the creation of approximately 50,000 homes, most of them apartments.

The apartment industry is a competitive and robust $1.1 trillion industry. We serve more than 35 million residents, and that number has been expanding and is expected to continue at the rate of a million a year.

In my written testimony, I highlight the important changes in supply and demand as well as the economic contributions apartments make to society to explain to Congress why it is so important to pursue mortgage finance reform separately for this housing segment.

While the housing crisis exposed serious flaws in our Nation's home mortgage finance system, the same cannot be said about the GSEs' multifamily programs. The industry did not overbuild, and the GSEs' multifamily programs performed well. Loan performance remains strong with delinquency and default rates at less than 1 percent.

In conservatorship, the GSE multifamily programs have netted more than $10 billion for the Federal Government. Most importantly, when all other sources of capital fled the market during the housing crisis, the GSEs increased their participation, providing much needed liquidity, and they did so throughout the country. In other words, they functioned as intended.

We share your collective desire to return to a marketplace dominated by private capital. The industry relies on a variety of sources besides Fannie and Freddie, including commercial banks, thrifts, life companies, FHA, CMBS, pension funds, and private mortgage companies. Together these sources have provided the apartment sector with up to $150 billion annually to develop, refinance, purchase, renovate, and preserve apartments.

However, each of these sources has its own focus, strengths, and limitations and has either been unwilling or unable to meet the full range of the multifamily industry's capital needs, even during healthy economic times. There is no evidence to suggest that that situation is any different today.

Yes, in the past few years, private capital has returned to the apartment sector, but it is typically concentrated in a handful of cities and on trophy assets. People who want to live in apartments in secondary and tertiary markets in rural areas are not benefiting from this resurgence.

Even in the major markets, firms providing workforce housing find themselves shut out. In 2013 alone, an estimated $100 billion in multifamily mortgages will need to be refinanced, and many of these are in areas that private capital will not go into. For these needs, the sector will need to rely on the GSEs.

But I am not here to suggest that GSEs continue. I would highlight instead for the Committee those elements of the existing system that worked well for apartment lending and, most importantly, did so at no cost to the taxpayer. It is our hope that these elements will be carried forward in any new program.

Overall, we support reform that will ensure broad liquidity at all times and in all markets. This can only be accomplished if the Federal Government maintains a role. That is the starting point. From there, we propose that any legislation include a separate title to address the reforms specific to multifamily housing, including the process for privatizing entities, transitioning to a new system, and defining eligible successors. Our written testimony provides specific details and recommendations.

Finally, we understand the desire to include an affordability mandate in any proposed legislation. It is important to note that multifamily housing is inherently affordable with 82 percent of existing apartments affordable to households earning 80 percent of area median income. We strongly encourage caution in defining a mandate to avoid unintended consequences. There are many options available, some better than others, and currently we are considering them. However, we fear that in the desire to achieve affordability, Congress will severely compromise the primary objective of ensuring adequate liquidity to all apartment markets at all times.

Most importantly, Mr. Chairman and Members of the Committee, as part of your deliberation, we urge you to recognize the unique needs and characteristics of the rental industry and to retain the successful components of the existing multifamily program in whatever succeeds them.

Thank you very much.

Chairman JOHNSON. Thank you.

Mr. Burke, you may proceed.

STATEMENT OF E.J. BURKE, EXECUTIVE VICE PRESIDENT AND GROUP HEAD, KEYBANK REAL ESTATE CAPITAL, KEY CORPORATE BANK, ON BEHALF OF THE MORTGAGE BANKERS ASSOCIATION

Mr. BURKE. Chairman Johnson, Ranking Member Crapo, and Members of the Committee, thank you for the opportunity to testify today. My name is E.J. Burke, and I am the 2014 chairman of the Mortgage Bankers Association as well as executive vice president and group head of KeyBank Real Estate Capital. I have over 34 years of experience in banking and commercial real estate finance. At KeyBank, I oversee multiple commercial real estate lending platforms in our commercial and multifamily finance business. KeyBank provides community banking services in 14 States and is a national commercial real estate lender and servicer.

The multifamily rental housing market is a critical component of our housing system—in size, reach, and the households that it serves. More than one in three American households rent their home, and more than 16 million of those households live in multifamily rental housing.

Renters include workers who want to live near their jobs, retirees on a fixed income, families with children, students, and households who value the convenience and mobility that renting offers. A large and diverse group of capital sources currently provide liquidity for multifamily housing, and that diversification continues to increase.

Private capital also bears significant risk in existing GSE multifamily finance platforms. The Government-backed sources have experienced, even through the recent financial crisis, very strong credit performance. Importantly, as the recent downturn demonstrated, the countercyclical role is one that only the Government can fill.

With Fannie Mae and Freddie Mac's conservatorship going on more than 5 years, policy makers must develop a long-term plan for the future role of the Government in the mortgage market. This plan must address the GSEs' unique role in multifamily rental housing. It is clear that the current state of the GSEs should not last indefinitely. However, policy makers should ensure the ongoing stewardship of valuable resources that support the multifamily market and utilize them to transition to a stronger housing finance system.

As the Committee considers the structure of a multifamily housing finance system, we believe that policy makers should focus on ensuring the availability of capital in all market cycles. MBA believes that public policy should strike a balance that continues to attract and deploy private capital in the multifamily market while establishing a focused Government guarantee that enables liquidity and stability in all markets and all economic cycles.

Bearing this in mind, MBA believes that a new system should incorporate several structural recommendations which I describe in more detail in my written testimony.

First, a wholly owned Government corporation should function as a catastrophic guarantor, administrator of a risk insurance fund, and regulator of secondary market entities. This guarantor would be funded by guarantee fees paid by issuers.

The new system should also allow multiple privately capitalized issuers of Government-guaranteed securities in the secondary multifamily mortgage market.

Next, the GSEs' existing multifamily assets and infrastructure should be preserved and carried over to a new system. Not only are these businesses valuable to U.S. taxpayers, transferring them to new entities would minimize market disruption and allow them to continue to serve the multifamily housing finance market.

Finally, we firmly believe that proposed approaches should also be reasonable, flexible, and balanced with regard to the need to attract private capital. For example, policy proposals contemplating affordability requirements should take into account that 93 percent of multifamily units have rents affordable to households earning area median incomes or less.

We are encouraged by recent legislative activity that has revived the policy debate on the future of Fannie Mae and Freddie Mac and commend the efforts of the Chairman and Ranking Member and those on this Committee who have introduced thoughtful proposals that would create a comprehensive framework for the future of housing finance.

Thank you for the opportunity to testify before you today. MBA remains committed to its key principle that a successful multifamily secondary market should rely primarily on private capital while ensuring stable and continued liquidity in all economic cycles through a Government role. We believe that this can be achieved in a manner that protects taxpayers, encourages competition, and builds upon the successes and strong foundation that exists today. We stand ready to work with the Committee as it continues to engage in this critically important effort.

I look forward to your questions.

Chairman JOHNSON. Thank you.

Mr. Narasimhan, you may proceed.

STATEMENT OF SHEKAR NARASIMHAN, MANAGING PARTNER, BEEKMAN ADVISORS, INC.

Mr. NARASIMHAN. Good morning. Chairman Johnson, Ranking Member Crapo, and Members of the Committee, thank you for inviting me to testify at this hearing on housing finance reform. My name is Shekar Narasimhan, and I am managing partner of Beekman Advisors. I have spent the past 35 years in housing and finance, including 4 years building single-family homes in eastern Kentucky. Later, when I was CEO of one of the first publicly traded commercial mortgage finance companies, we developed loan products to serve the low-income housing tax credit market. My experience in running and operating a real estate financial services business as a partner with the multifamily businesses at Fannie Mae, Freddie Mac, and FHA is what brings me here today. Through all of this, I developed a deep and abiding passion for affordable housing.

The multifamily businesses at the GSEs are not part of the problem in the housing finance system. In fact, they are part of the solution. Every major principle that has been articulated by stakeholders with regard to what a new housing finance system should look like is already in practice at these businesses today:

Alignment of interest between the borrower, the lender/investor, and the issuer;

Detailed underwriting of every loan;

Service of virtually every market segment with a menu of stable and responsible lending products. They have consistently served the middle market in multifamily, which is for lower-income households and working families, for the last 27 years;

Participation of both small and large private lenders. Lenders from Nebraska, lenders from California, large banks, publicly traded companies have been part of this system with skin in the game;

And a lengthy record of profitable operations, which is what gives us considerable hope that private capital can, in fact, be brought in to capitalize these entities;

And, finally, a footprint that responds appropriately to changing economic conditions. At a point when the capital markets were very frothy, the GSE multifamily businesses had approximately a 25-percent market share, and at the point when there was virtually nobody else in the capital markets during the crisis, they increased their market share to 70 percent. It is already down to 55 percent and will continue to shrink as the private capital market comes back in.

So I am here today to propose that the multifamily businesses at the GSEs should be used to really demonstrate the path to the housing finance system of the future. Let us spin them out as privately capitalized entities with Government guarantees that are limited to only the securities that they issue.

We all recognize that change is needed. Everyone would agree that 5 years of conservatorship, as Ranking Member Crapo said, is already too long. It has discouraged the best and brightest from working and remaining at the GSEs. It is, frankly, not allowing the secondary market to return to normal. But we have a large rental population that is growing: 41 million Americans live in rental housing today, and that number is actually growing. So we have rental demand. We need money to both refinance existing loans as well as to build new rental properties across the country.

The GSEs have played an enormously important role in this sector. We are arguing simply in order to keep rental burdens manageable, we need to keep the operations of these entities within the framework that they have operated, and one of the most important frameworks where perhaps we are going to be more prescriptive is to argue that since they have for the past 11 years of kept records demonstrated that they can serve families at 60 percent of area median income and do so profitably, they should be continued to be held to that standard in the future.

Responsible change does involve doing the least damage and encouraging the introduction of private capital. So the work that has been done recently at the multifamily units of Fannie Mae and Freddie Mac to determine how a spinout would occur is enormously valuable to this Committee and, frankly, gives you the blueprint for this to occur.

What we proposed, therefore, is an immediate spinout of the multifamily operations and that can fit into the architecture of any bipartisan proposal that you come up with. There is no reason to wait given rental demand, the need for rental units, and the profitable track records of these current businesses.

Thank you for the opportunity to make these remarks. I look forward to your questions and comments.

Chairman JOHNSON. Thank you.

Ms. Ludwig, you may proceed.

STATEMENT OF TERRI LUDWIG, PRESIDENT AND CHIEF EXECUTIVE OFFICER, ENTERPRISE COMMUNITY PARTNERS, INC.

Ms. LUDWIG. Chairman Johnson, Ranking Member Crapo, and Members of the Committee, thank you for the opportunity to testify this morning, and thank you for holding this hearing on a crucial but often overlooked segment of our housing market—the one-third of families that rent their homes. I am Terri Ludwig, the president and CEO of Enterprise Community Partners. We are a national nonprofit organization that creates opportunity for low-income families, starting with a stable home in a vibrant community.

One of our many business lines is multifamily lending with a focus on apartments that working families can afford. Today we have the opportunity to build a more perfect system of housing finance in this country, one that fixes the problems of the past system while building off the parts that worked.

As we work out the details, I urge Congress to keep two overarching goals in mind:

First, we must continue to have a liquid, stable, and affordable housing market that appropriately supports both homeowners and renters;

And second, whenever possible, Government support must be targeted to the families and communities that need it most.

Multifamily housing is a key consideration in both goals. Today roughly 100 million Americans are renters, a number that is expected to rise significantly in the coming years, and about 40 percent live in apartment buildings of five or more units.

On average, renters are younger, earn less income, live in smaller households, and are more likely to be people of color compared to homeowners.

Each of these populations rely heavily on multifamily housing. And even with the current levels of support to that market, renters face an unprecedented affordability crisis.

After adjusting for inflation, the typical renter's income has dropped over the past few years while their housing costs have steadily risen. At the same time, the number of apartments that are affordable to low-income families have declined while demand for these apartments has increased.

As a result, it is more and more difficult for working families to find a quality, affordable home. All told, nearly 11 million renter families are paying at least half of their income on housing, a severe cost burden that often leaves them one paycheck away from losing their home. That is more than a quarter of the Nation's renters, an all-time high.

This crisis would be much worse without Fannie Mae and Freddie Mac's presence in the multifamily market. More than two-thirds of the apartments financed by the GSEs last year were affordable to low-income families, and many were affordable to very low income families.

Meanwhile, other sources of capital, namely banks, thrifts, and life insurance companies, tend to stay away from this segment of the market, instead focusing on Class A properties in top-tier housing markets.

Fannie and Freddie bring other benefits to the market as well, including strong underwriting, broad liquidity, and a buffer from severe downturns. My written testimony goes into detail on each of these critical roles.

A key to their ability to perform these roles is access to a limited, explicit Government guarantee. And thanks to a series of recent reports from FHFA, we know what the rental market would look like without that guarantee.

The entire rental market would be subject to wild boom-and-bust cycles, causing interest rates to skyrockets New construction on multifamily properties would plummet. Average rents would increase. And since private capital would be less likely to invest in lower-end developments or second-tier markets, low-income families would be carrying the heaviest burden.

Thus, any reform must start with an explicit, limited, and paid-for guarantee on multifamily mortgages, and there are several other important steps that need to be taken to ensure a well-functioning rental market, many of which Shekar just laid out.

We think it is a good idea for Congress to spin off the GSE multifamily businesses starting immediately. When the public guarantor is fully operational, the insurance function should be transferred to the Government. And from that point on, new approved issuers should be allowed to purchase that same guarantee. We recommend starting with a co-op made up of small and community lenders.

These businesses are effective, efficient, and profitable, and they must be preserved to avoid unnecessary disruptions in the rental market. But we also need to ensure that the issuer of a Government-insured security has a defined public purpose.

First, the clear majority of apartments financed by Government-backed securities must be affordable to working families. Under our proposal, each issuer must prove at least 60 percent of the apartments they finance each year are affordable to low-income families.

Second, issuers should be encouraged to lead the market in affordable housing investments as Fannie and Freddie have for decades.

Third, we recommend levying a 5- to 10-basis-point fee on all insured securities to fund programs that will go to the very low income families.

Fourth, we recommend requiring all issuers to establish annual plans for serving historically underserved segments of the market.

Again, thank you for tackling this important issue today. The decisions made in the coming months will determine whether a stable home is within reach for millions of working families. We look forward to working with the Committee on these important issues.

Chairman JOHNSON. Thank you all very much for your testimony.

We will now begin asking questions of our witnesses. Will the clerk please put 5 minutes on the clock for each member.

Ms. Ludwig, in smaller communities in South Dakota, a limited supply of housing contributes to both affordability and economic development challenges as workers have trouble locating housing. These multifamily rental properties are also often smaller.

With these factors in mind, what steps should we take in legislation to address the issue of serving smaller and rural communities in a new system?

Ms. LUDWIG. Certainly. So today there are a number of programs that the GSEs already have in effect that help the ability to have underserved markets, particularly rural communities, to be able to have capital flow directly. For example, Fannie Mae today has a small loan lenders program which specifically targets loans that are less than $3 million in some markets and $5 million in others.

I would say that that has been a very substantial program, but compared to the need, we need to do significantly more.

So what we are proposing is to use the affordability fee to not only go to help extremely low income families, but also to look at underserved markets. For example, it has been proposed that there is established a market access fund that could be used to provide credit enhancements, reduce cost of underwriting, and look to set up other pilots that could address your question about how to further promote the small loan programs.

We think that some specific pilots around securitization are essential. And as I mentioned in my written testimony a moment ago, we think that Congress should stand up a new issuer to serve small and community banks, since that's where a lot of these loans are being made. These banks need to be well-positioned to keep making loans.

And, finally, I would say that it is not to be overlooked that Fannie and Freddie have been important investors in these markets over a long period of time. I know from Enterprise's experience, Fannie Mae has partnered with us to do over 700 affordable homes on Native lands, including those in South Dakota and Idaho. So we certainly would like to see that some of the opportunities for those GSEs to continue to invest in programs that support affordability remain in place.

Chairman JOHNSON. This question is for the full panel. Do each of you believe that the whole market will have access to affordable credit without the presence of a Government guarantee? Yes or no. Let us begin with Mr. Bozzuto.

Mr. BOZZUTO. No.

Mr. BURKE. No.

Mr. NARASIMHAN. No.

Ms. LUDWIG. No.

Chairman JOHNSON. Mr. Narasimhan, you have recommended an affordability threshold. Why is your proposed threshold important? And do you think the new issuers in your system will be capable of meeting your proposed target?

Mr. NARASIMHAN. The current multifamily businesses at the GSEs have been monitoring and tracking under a different regime, a goals regime, what they do in different segments of the market. So we have a methodology to track the income of tenants and the affordability of rents in units across both 100 percent of median income, 80 percent of median income, and in other ways. If this is done one time at the time of origination of a loan, it is not an intrusive requirement. It does not require interviewing tenants. It just involves using a rent roll and using AMI.

Over the past 11 years of keeping these records, they have traditionally, as part of their normal business, done more than 60 to 65 percent of their business on units that are affordable to those at 80 percent of median and below.

One of the precepts of our proposal is that private capital will come into these issuers and take the first loss prior to any Government guarantee and in addition to any other losses that are incurred by lenders or other participants in the system.

In order to bring in private capital, the first and most important requirement is that we have a stable regime so we have a track record here of performance with profitability at a standard that is already accepted in the market as being the middle of the multifamily market. So that is number one criteria.

Number two, to conclude, basically in order to be able to meet the standard, the GSEs are not stretching and taking more credit risk; they are doing what is within their capability to do. So we think a reasonable standard that is measured once a year should be applied as a public policy requirement.

Chairman JOHNSON. Senator Crapo, do you choose to pass?

Senator CRAPO. Yes, Mr. Chairman. Because of the time constraints, I will let my other colleagues go first, and so I will defer to Senator Corker.

Chairman JOHNSON. Senator Corker.

Senator CORKER. Thank you both. That is most generous, and thanks for having this hearing. And to all of you as witnesses, thanks for your outstanding testimony. It is kind of refreshing to have people whose titles are "Mr." and "Mrs." here, so thank you very much.

I do want to specifically ask a few questions—is it "Narasimhan"?

Mr. NARASIMHAN. "Narasimhan."

Senator CORKER. I am going to let you say it.

Mr. NARASIMHAN. I live in eastern Kentucky, and they just call me "Shekar."

[Laughter.]

Senator CORKER. Well, Mr. Shekar——

[Laughter.]

Senator CORKER. If you would, please walk us through the case series and how it works with multifamily. I know there are basically two types: there is a K-series and DUS. But if you would, walk through briefly, if you would, the basis structure of how the general financing arrangement works.

Mr. NARASIMHAN. Sure. The difference is that one is what is called an "issuer-based model," which is the DUS program, where on every single loan a lender that meets the capital standards required to be a lender and issuer under that program takes the first-loss risk if a loan goes bad. So they make a loan. They can sell it to Fannie Mae. Fannie Mae securitizes it. If that loan goes bad, they take one-third of the first of the losses on that loan.

Senator CORKER. Right.

Mr. NARASIMHAN. Which has typically amounted to over 10 percent of the outstanding principal balance. But in order to do that, they have to meet these standards, they have to meet the underwriting and so on. That is a loan-by-loan issuer-based system where I look at the financials of my counterparty.

The K-series is a securitization-based risk sharing where I buy $1 billion in loans, assume that every loan is $10 million. The average single-family loan, by the way, is $6 million, so let us say it is $10 million to simplify it. We have 100 loans in this pool made across the country. For the sake of comity, it is two loans per State. But we make 100 loans. We put them into a trust. We securitize them, and we sell typically the first 14 or 15 percent of the loss in the form of a two-tranche security, what is called an "unrated, bottom-of-the-barrel B piece."

Senator CORKER. And that is private sector risk, first——

Mr. NARASIMHAN. Somebody else is examining every loan, taking the risk, earning a yield on their risk, and then a mezzanine piece, which takes the second-loss risk, before anybody can hit the issuer.

Senator CORKER. And the overall risk to private investors is 15 percent, generally?

Mr. NARASIMHAN. Typically 14 to 15 percent.

Senator CORKER. So it looks like we are way low at our 10-percent level on single-family. I do want to point that out. So there are people willing to take 15-percent risk on these loans.

Mr. NARASIMHAN. Mr. Senator, in defense of those in the single-family business, this is a bulkier business. In securitization, when you have——

Senator CORKER. You can stop now.

[Laughter.]

Senator CORKER. And what is the role of the risk-sharing component in multifamily? In other words, in addition to putting up risk capital, what other attributes to the deal is having that risk capital there in advance of the public guarantee?

Mr. NARASIMHAN. I think the most important is that this is a very selected group of small and large lenders who lend mainly regionally and nationally. So you know and can look in the eye of your counterparty; you know who is doing this business. Multifamily is essentially business-to-business lending where the counterparty in the landlord and the borrower is a sophisticated party that is borrowing a significant amount of money. It is not—and we actually in every single loan on a quarterly basis collect financials, on an annual basis do inspections. So the lender has tremendous obligations to not only make a good loan, but to monitor it, manage it, ensure that the property is being maintained and kept up to standards, and then worry about when it comes due for a refinance that a balloon payment is coming due and it can be refinanced.

Senator CORKER. And that is one of the reasons that they perform better than the single-family. Is that correct? The underwriting is just different because you are looking at each transaction in a very focused way. And if I could, and very briefly because I want to ask one more questions, Mr. Bozzuto, has that played a role in ensuring that there was not the overbuilding that you referred to in your testimony?

Mr. BOZZUTO. Yes, Senator. There are a variety of factors that are related to that. The multifamily business as opposed to the single-family business tends to be a relationship business. It really is. It is not just a business-to-business business, but it is a people-to-people business. People who are in this business are in it a very long time.

Second, leverage is considerably lower. We have typically 30 percent, 25-percent equity in our projects, real equity, before the debt, and that has certainly contributed to the solvency.

Senator CORKER. Thank you, and because of the generosity, I will stop just with making this statement, and you can nod your heads for brevity of time. But it is my understanding that most of you are pretty familiar with a bill that is before—Senate bill 1217 that a lot of people are involved in here. It is my understanding that relative to the multifamily piece, the only change that you would like to see happen is that the issuer be a private issuer, not a public issuer. And other than that, the bill works very well compared to the experiences that you have had in the past. Is that correct?

[Witnesses nod affirmatively.]

Senator CORKER. I will note that everybody is shaking their head up and down, and I will yield the floor. Thank you.

Chairman JOHNSON. Senator Reed.

Senator REED. Well, thank you very much, Mr. Chairman, and thank you for your testimony.

Mr. Bozzuto and I think the whole panel concurred that because of much more effective underwriting, the multifamily programs were credible, durable, and, in fact, contributed significantly and are still contributing. And that is going to continue regardless of whatever we do, we hope.

But there is one aspect, I think, in terms of attracting capital to the mortgage market there, and that is the role of Section 8 vouchers. Mr. Bozzuto, to what extent is a Section 8 voucher, particularly when you talk about the affordable market, critical to attracting private capital and also to ensuring that these projects not only can be built but they can continue to pay on the mortgages?

Mr. BOZZUTO. Senator, without subsidy, without Section 8 vouchers, without tax credits, it is virtually impossible in most parts of the country to build new construction that is affordable at the kinds of levels that you would be talking about.

Senator REED. So, you know, all of—and I think your testimony is extremely valuable—is premised upon not only sort of structural changes perhaps to the GSEs, et cetera, but also the continuation of these programs that support housing through tax credits and Section 8. Is that—I see nodding of heads.

Mr. BOZZUTO. Absolutely, sir.

Senator REED. And the other way to say that is if you look at the luxury market for residential, there is no problem there, there has never been a problem. Is that pretty fair?

Mr. BOZZUTO. No, I would not agree with that, sir. We build, my company, in my career—probably 7,500, 8,000 of the units I built have been affordable. It is impossible to build affordable housing without some form of subsidy. Market rate housing, luxury housing, which can be defined differently no matter where you are, can be built when capital is available, but private capital comes and goes. And part of the reason we maintain that liquidity is the public purpose is because if you look back at 2009, when there was a need for jobs, there was a need for rental housing, the only capital that was available for the apartment industry was coming from the public sector. So I would not say that at all times the luxury or the market rate business survives on its own.

And, second, even today, when there is private capital, if I went into a smaller community—and it does not have to be in Nebraska or West Virginia.

Senator REED. Westerly, Rhode Island.

Mr. BOZZUTO. Or Westerly, Rhode Island.

Senator REED. As you point out in your testimony.

Mr. BOZZUTO. Yes, sir. We were thinking about Point Judith.

Senator REED. You are getting close.

[Laughter.]

Mr. BOZZUTO. But even here, if I were to go to Hagerstown, Maryland, which is, you know, in theory a suburb of Washington, I could not today get a private insurance company to provide financing for a new project in all likelihood.

Senator REED. And the final point in your testimony in this area is that we are underbuilding given the projected demand, significantly; that even with this program that is working effectively, we need to do much, much more because just the projected demand for rental housing is so much greater.

[Witnesses nod affirmatively.]

Senator REED. Everyone is nodding their heads. I will take that agreement.

A final question, given all your expertise here, and given the fact that we are looking next week to this cataclysmic possibility of default, what would that do to your financing operations, Mr. Bozzuto, for example?

Mr. BOZZUTO. Even now our ability to plan new projects, our ability to get debt for new projects is essentially on hold because of great insecurity about what is being done by Congress.

Senator REED. Mr. Burke, does your business rely on overnight financing in terms of—I am sure the bank does, but are you beginning to see sort of the retraction-retention because of this debate?

Mr. BURKE. Yes. My business line—there is a different part of the bank that funds the bank and has more interaction with the markets. But I can tell you that there is a great—that uncertainty creates this——

Senator REED. So the secondary effect would be the part of the bank that funds you basically will stop doing anything because they are either uncertain or cannot get liquidity themselves. Is that——

Mr. BURKE. It would be the latter.

Senator REED. Yes, the liquidity would dry up, so you are seeing a potential huge contraction, which is two and three steps away from simply interest rates going up.

Mr. BURKE. Correct.

Senator REED. Well, thank you all for your excellent testimony and for your great work. Thank you.

Chairman JOHNSON. Senator Johanns.

Senator JOHANNS. Thank you, Mr. Chairman. Let me also say to the panel, your testimony has been extremely informative, and I must admit it is a bit head scratching, and let me offer a thought, and then I would like your reaction to it.

I do not think anyone on the panel is looking to this area of the real estate economy or industry and trying to make the claim that you were the problem. I think the testimony is accurate. This part of the real estate industry functioned as we hoped it would function, and that is on the good-news side of things.

On the other hand, it does not appear to me that historically or even now it has functioned very well outside of sizable metropolitan areas, and I think, Mr. Bozzuto, your testimony kind of nails it. If you think you are having that kind of challenge in Hagerstown, what would you say about Sidney, Nebraska, where these people are doing absolutely everything right, it is the home base of Cabela's, but they have some of the best economic development initiatives in the State of Nebraska—I mean, as their former Governor, I used to go out there and just marvel at what they were doing. You know what the first item on the list was every meeting I have ever had with them? Housing.

Now, this is an area where incomes are strong, job creation is strong, opportunities are strong, and they are constantly battling to get housing.

So to me, whether you are talking about Sidney, where everything is going right, or a very impoverished area of a community where things are not going so right, the job is not getting done.

So my question is: How do we get that job done? How do we do something that helps those extremes—an area that is blighted and needs help and an area where everything is happening but it is not in a major metropolitan area? Mr. Bozzuto, I will give you that puzzle, because I think that is a pretty important issue to folks like me from more rural States.

Mr. BOZZUTO. Senator, I absolutely agree with you. And I am not sure I can give you a prescription except that it would appear to me that unless we can figure some form of continued Government role with relatively clear legislation that describes—that provides a mandate, that talks about communities like that, and talks about affordable housing, but that allows the flexibility for the regulator that we would recommend be installed to manage that so that at different points in time, adjustments can be made, I am not sure that I know the answer. I would tell you that if—as difficult as it has been, without the GSEs it would have been truly impossible.

Insurance companies work on an allocation basis. They get a certain amount of money, and they get it in the beginning of the year, and it is much easier for them to spend their money in places like Washington, DC, or New York City, or L.A., or San Francisco than it is in places like Nebraska.

Senator JOHANNS. Mr. Burke.

Mr. BURKE. Senator, what I might suggest is that the way I see that problem is that the money manager in New York will not do the work to understand Sidney, Nebraska. So what you have to have is a mechanism where you can attract the capital from a money manager who is not going to take the time to understand the local economy. And what we are suggesting here is that through a mechanism similar to what the GSEs do today, you create a regime where people who understand real estate, people who understand the communities, for instance, community banks, have an opportunity to originate loans which then can be securitized with a Government guarantee. That would then funnel capital into those communities that need it.

For instance, a community bank knows—community banks have done a great job because they know their clients. But they have a liability structure that is short. So what you need to do is get long-term capital to be invested in these communities, and that is part of the reason I think we all today are saying that the program the GSEs have, something similar to that, could address that problem.

Senator JOHANNS. Mr. Chairman, I am out of time, but if I could ask the panel to put some brain power behind this, because what I worry is that we pass a piece of legislation, we kind of declare victory—and I hope the legislation passes; I am one of the cosponsors—but at the end of the day we look back in 2 years and 4 years and 5 years and say, my goodness, there is a huge gap out there. But there has always been a huge gap out there, and it would be good to have some strategies to figure out how we can improve that situation, whether it is an inner-city area or it is a rural area in one of our States.

Thank you, Mr. Chairman.

Chairman JOHNSON. Senator Menendez.

Senator MENENDEZ. Thank you, Mr. Chairman. Thank you all for your testimony.

Mr. Chairman, I appreciate you holding this hearing. In a context like New Jersey, multifamily housing is a big reality for people to have a place to call home. And it replicates the third of all American households that live in multifamily housing, 17 million households in the country. In my State there is a fair amount of that. In my own life, I know that that has been a reality.

I also know that 27 percent of them pay over half—half—of their income toward rental payments. And so that is an enormous challenge in the lives of individuals because when you are paying that much in rental payment, you know, there is very little else to do other things—educate your children and realize your hopes and dreams and aspirations, which is why I have been a big advocate for quite some time of having Fannie and Freddie expand their multifamily operations. And, in fact, they performed well during the crisis. They have lower serious delinquency rates than single-family lines and other sources of multifamily credit, such as private label commercial-backed securities and bank and thrift loans.

As a matter of fact, the FHFA's Inspector General has Fannie's and Freddie's multifamily programs as their only profitable major business segments from 2008 to the third quarter of 2011. That is pretty significant.

So my question to the panel is: What do you believe were the major drivers for that strong performance? And what lessons can we take away that can be more broadly applied?

Mr. NARASIMHAN. Senator, if I may, I think the first and most important is risk sharing. I think there has always been a very strong component in the multifamily programs of everyone is in this, and, of course, market conditions can change and loans can go back, but everybody loses something in the bargain. And you try not to have that loss at the community, but with the developer or the borrower, the lender or the issuer, and, in effect, the guarantor.

I do believe that that fundamental principle is probably—that led to good underwriting, that led to an avoidance of a race to the bottom. When the rest of the market started doing crazy stuff, they did not go there, because they had lenders and participants and borrowers saying we do not need to go there, we can do our business, reduce our market share, and stay fine. So I fundamentally believe that is the number one reason.

Senator MENENDEZ. Anyone else?

[No response.]

Senator MENENDEZ. Let me ask you this, then: You know, if—we want availability, but we also want affordability, and I understand the concerns that have been raised about what that mechanism looks like and how that might undermine the other elements of the market. But how does one—I think both you and Ms. Ludwig mentioned in your testimony some suggested mechanisms to improve affordability and access rather than simply subsidizing developments that would ultimately have no trouble getting finance in purely private sources. Can you talk a little bit about what those can be?

Ms. LUDWIG. Sure. So, first of all, as part of the recommendation, we propose an annual fee from 5 to 10 basis points on securities that are issued that would go toward promoting affordability. In past legislation Congress established the National Housing Trust Fund and the Capital Magnet Fund, both of which should be funded regularly in the future system. We also propose putting some of that money into a Market Access Fund, which will look to serve underserved markets and ensure that capital is available. We have the ability to do research and development to really push our thinking on how to promote affordability through credit enhancements, new product creation.

So, really, there are three primary uses of that fee: one is to provide through the National Housing Trust Fund essentially a block grant to lower income populations; the second is to the Capital Magnet Fund, to be able to use that to leverage private investment; and then the third is for this R&D type of facility.

And, finally, I think it is really important also that we take a very proactive approach to underserved markets and we are not thinking just retroactively about what we have done in reporting but, rather, we're recommending an annual planning process where each of the issuers sit down with their regulator and actually form a very targeted plan to address some of those underserved markets. So those would be essential.

Mr. NARASIMHAN. Senator, 2 seconds. I think we have talked about the creation of a market access fund which can enable private institutions to take more risk and push the envelop a little bit on the risk curve to be able to serve these kinds of markets. And I think we want to flesh that out further and then discuss it with you. But I think that is the way to get to this with the private sector taking the first-loss risk, with them doing the innovation.

Senator MENENDEZ. Well, we would love to work with you and anyone else on this issue, because at the end of the day, if you have availability but not affordability, you do not have availability.

Thank you.

Chairman JOHNSON. Senator Moran.

Senator MORAN. Mr. Chairman, thank you. Thank you to you and Senator Crapo for hosting this hearing. This is the first time in a few days that I have actually felt like a legislator. Your testimony was very valuable, well spoken, and I appreciate it.

First of all, I would say, I think in answer to Chairman Johnson's questions, all of you made clear the necessity or the importance of GSE financing in housing, and that was done with your yes or no answer, and all of you indicated the importance of that GSE for housing broadly across the country.

I also want to follow up on what Senator Johanns said. Our States are similarly situated, but I want to make certain that in any GSE legislation we are not committing the mistakes that have been made in the past, which seems to me to be mandating, requiring loans to be made that are not otherwise financially sound, that the risks are not accommodated by the return. And so when we talk about housing in rural communities, there needs to be a different fashion than forcing the lenders to allocate resources where the loans have a higher potential of going bad, they do not reflect market risk.

Mr. Burke, you indicated about the unknown, that somebody who is making a decision does not know Sidney, Nebraska, or communities in Kansas. Mr. Bozzuto, you talked about Topeka, Kansas, as well as Rhode Island in your testimony. Tell me, is there something unique about multifamily housing in a rural setting that makes the market—that markets would need to price at a higher return, a greater risk is encountered? Or is it only what Mr. Burke said about lack of really understanding? And then I want to follow up with the idea about community banks. Is there something unique about multifamily housing in a rural setting that increases the risk and, therefore, requires a greater return?

Mr. BURKE. I think the first thing to think about is loan size. The loan sizes are smaller in smaller communities. So the economics of doing the underwriting, the processing, and the closing of small loans has always made it difficult——

Senator MORAN. So the fixed costs——

Mr. BURKE. Right.

Senator MORAN. ——of that project——

Mr. BURKE. That is right.

Senator MORAN. ——associated with the financing makes it less economically viable.

Mr. BURKE. That is right.

Senator MORAN. OK.

Mr. BURKE. And part of the—I would say, just to buttress some of the comments that Shekar has made, the underwriting of multifamily is a very detailed and very complicated thing. So the smaller the loan, the higher those up-front costs are, the more unaffordable it gets.

So if we have lenders who are in those communities that already know those communities and give them access to capital where an investor does not have to do that work, they do not have to do that underwriting, you have a more efficient system.

Senator MORAN. Would that suggest the opportunity for a developer packaging multifamily housing in a number of communities to make a larger project? Is that——

Mr. BURKE. Well, you still have to understand——

Senator MORAN. The community.

Mr. BURKE. ——each individual project in each individual community, so I do not know that the package would help. But I think that if we have a mechanism for community lenders to access a Government guarantee, then I think we could make a dent in the problem.

Senator MORAN. Mr. Burke, do you have any knowledge—is this a question that is fair to direct to you? Our community bankers would continually tell us that they are overregulated in ways that lack common sense, that do not reflect the risk that the regulators presumably are trying to overcome. Are there regulations that reduce the chances that a community banker is going to make this kind of loan, originate this loan?

Mr. BURKE. I do not know that there are specific regulations that would, but I think when you sit down across the table from your examiner and the examiner has read in the *Wall Street Journal* that XYZ market a thousand miles away is experiencing problems and, you know, prove to me that your market is not, that has a dampening effect on the next loan that you are going to think about.

Senator MORAN. So the broad regulatory environment as compared to a specific regulation——

Mr. BURKE. That is right.

Senator MORAN. ——has this dampening effect.

Mr. BURKE. That is right.

Senator MORAN. Are there States in which there is a role model for increasing the housing stock? Have any of you experienced a place where this works better in Kentucky than it does in Kansas?

Mr. NARASIMHAN. No, I do not think so. Terri?

Ms. LUDWIG. No, I would say not. But I would also add that I think your question goes right to the heart of the need to do more testing around securitizing the smaller product, the small multifamily products. That is so essential for the markets we are talking about, regardless of which community you are in, but if you are in a smaller rural community. So I would turn to that recommendation as well.

Senator MORAN. OK. Mr. Chairman, thank you.

Chairman JOHNSON. Senator Hagan.

Senator HAGAN. Thank you, Mr. Chairman and Ranking Member Crapo. This is an excellent hearing, and I echo my colleagues in thanking you for your testimony today.

It seems like a lot of us are talking about the geographic diversity and the need for affordable and available housing in our rural communities. And North Carolina is certainly front and center in that situation, too.

I can think back to hurricane seasons and people saying, well, you know, from FEMA's perspective we will just people up in apartment buildings. There are none. So there is a huge need. And there is also a huge need in some of the resort communities for affordable housing for workers that are not in the luxury beachfront homes.

So it is really something that I think this Committee is understanding the need and the real desire that something needs to be done.

And besides the issue of geographic diversity, Mr. Burke, regarding the recently reproposed rule on credit risk retention for securitized loans, does your institution see any potential cost impact to borrowers and, by extension, to the tenant families as a result of the rule? And to what extent will this rule help or hurt liquidity for new projects and maturing debt?

Mr. BURKE. Are you referring to the CMBS risk retention?

Senator HAGAN. Yes.

Mr. BURKE. I think the rule that allows an issuer to transfer its risk retention obligation to a third-party BP Spire, the rules that require that buyer to retain the investment for a certain period of time will inevitably require a higher yield because it's a more illiquid investment by virtue of this restriction, and that ultimately would end up finding its way into the yield that you have to charge the borrower.

Now, having said that, I think the rule overall that allows a sophisticated third-party investor to acquire—or to take over that risk retention requirement is a good one. In CMBS, my own personal experience is that when you know that a third-party investor is going to sit across the table and tell you to remove certain loans because they just do not like them, it creates a lot of discipline.

So I think the rule overall is a good one, but it will inevitably result in a cost.

Senator HAGAN. Any other panelists?

Mr. NARASIMHAN. We probably slightly disagree on this. It would be a good thing. But I think that the CMBS business turned during the crisis or prior to the crisis into essentially a storage business, where loans were being warehoused with the sole intention of being securitized even before the ink was dry on the paper. And part of that behavior occurred because very few people had really any skin in the game other than the ultimate investor, who might or might not have understood what the collateral was. And certainly the rating agencies played a part in that.

So I think the notion that there should be skin in the game, how that is done to manage around risk-based capital and create a framework for competitive pricing is I think the issue. But we should not be debating whether there should be skin in the game at all.

Senator HAGAN. Let me ask about the private capital, too, and when we were talking—Mr. Bozzuto, I think you were talking about building a different part of Maryland. And yet the private capital, the insurance companies would not step forward. What will it take to get once again the community banks—and that might be from a regulatory situation, but insurance companies to start stepping back up to the plate and bringing private capital back into the market?

Mr. BOZZUTO. Senator, the insurance companies have come back into the market. In fact——

Senator HAGAN. In the rural areas, perhaps.

Mr. BOZZUTO. You have to imagine what happens at an insurance company in Hartford or a pension institution. A loan officer goes into a conference to make a presentation on a project: "I have a project I want to do in Raleigh." Well, you know, everybody knows where Raleigh is. Everybody has a preconception. It is easy to talk about the market. There are comparables.

"I want to do a project in Whiteville, North Carolina"? I mean, nobody knows what he is talking about. And that fellow or that woman is going to be very worried about their credibility. They are not going to do it. And that is why we need some sort of an inducement in the form of Government guarantee that will allow us to have access to capital for those kinds of markets.

Senator HAGAN. Thank you, Mr. Chairman.

Chairman JOHNSON. Senator Crapo, would you yield to Senator Warner?

Senator CRAPO. I definitely will, Mr. Chairman.

Senator WARNER. Thank you. That is extraordinarily generous, and I am going to owe you big time, not only letting me jump but letting it go not in order. And I asked Senator Johanns to stay for a minute because I just wanted to make three really quick points.

If we are going to make sure that Nebraska and Kansas and rural North Carolina and rural Virginia and Idaho and South Dakota stay in the mix, what we have got right now is—you know, the main thing we need to do is do not mess this up. And the activities right now of the FHFA by saying let us arbitrarily cut back 10 percent on multifamily—and you just got a nod on this one as well—would you not agree that if that 10-percent arbitrary cutback, the people who are going to get hit first are the affordable universe that Senator Menendez is interested in and the rural communities, because those would be the first lopped off the list. Is that a yes?

Mr. BOZZUTO. Yes.

Mr. NARASIMHAN. Yes.

Ms. LUDWIG. Yes.

Mr. BURKE. Well, Senator, in fact, Fannie Mae in the beginning of the year put out a rule that said, "We will not grant waivers. Do not bring us waivers on loans less than $10 million."

Senator WARNER. So if we do not do reform, the status quo is going to even further harm rural communities, point one.

Point two, you know, Ms. Ludwig had made a lot of comments about the need for this market access fund that S.1217 has. Mr. Bozzuto made the point, I thought a good one, that, you know, there are a lot of existing tools—Section 8, housing credits, and others—that make these deals doable at all, they have to remain in place. And one of the remarkable things about the Housing Trust Fund and all these other great ideas, we create them, but we have never funded them. Wouldn't the market access fund be the first time ever that there would be this stable existing fee that would be charged that would help provide some funding in this area?

Ms. LUDWIG. Absolutely.

Senator WARNER. Would that be a nod yes?

[Witnesses nod affirmatively.]

Senator WARNER. And that could help in rural communities as well as affordability communities.

And the third point—I know Senator Corker made this point already—what is the right capital number of risk sharing? And it seems like the multifamily business has kind of got it right. I do think we need more work, echoing what Senator Johanns said, on how we make sure the community banks—we can do more experimentation on securitization of those smaller communities' pools. But for those who feel that those of us who have said at the 10-percent level we have overstretched the amount of capital, I would again point out what Shekar's comments were. The market does a pretty good job of being able to tranche that, so if we put in too much protection, I actually trust your colleagues on the single-family side will figure out a way to tranche that, to price that risk accordingly.

But at the end of the day, I'd rather overshoot because never has there been taxpayer losses of any significance on multifamily. We'd like to have the same on single-family.

And my real great thanks to the Chair and the Ranking Member for letting me jump line.

Chairman JOHNSON. Senator Crapo.

Senator CRAPO. Thank you. Thank you very much, Mr. Chairman, and I appreciate our witnesses. Your testimony has been very good today.

I want to follow up on this same issue that we have been talking about in terms of access to the rural and smaller communities. And each of you have talked about it, but, Mr. Burke, I am going to direct my question to you.

You have all said basically that we need to have a mechanism to give the lenders in the smaller communities access to capital.

Specifically, what are we saying? Is it simply opening up to the community banks access to a guarantee, a Government guarantee? Or is there more of a mechanism that we need to be dealing with here? Mr. Burke, could you just walk us through how would we do this, getting access opened up to the community banks?

Mr. BURKE. If we were to create secondary mortgage market entities that had access to the guarantee and built some incentives for them to accumulate mortgages in these areas, I am highly confident they would develop partnerships with community banks to source these loans. Alternatively, if we could make it easier for a community bank to participate, I think it would help.

I mean, the problem, as I see it, is that, you know, we are talking—typically a multifamily mortgage is 10 years or more, and to put a 10-year fixed-rate asset on your books in a small bank is a difficult thing to do. So it is really a way to—it is a funding mechanism more than anything else.

I think banks would be—I think banks would welcome the opportunity to partner with a secondary mortgage market entity. I think, Terri, you suggested a co-op, which would be another mechanism. But I see it simply as a way to bring more permanent capital to those banks.

Senator CRAPO. Thank you very much.

And, Ms. Ludwig, would you——

Mr. BOZZUTO. I just wanted to add briefly to that. There is inherent inefficiency not only in the financing but in the construction and operation particularly of small properties. And as part of your discussion, you really need to, I think, recognize or consider some form of subsidy to make it worthwhile to do these smaller projects in rural areas.

Senator CRAPO. All right. Thank you. And just in the minute or so I have left, Ms. Ludwig, could you give a little more detail to the co-op suggestion you have made? How would that work?

Ms. LUDWIG. Sure. I actually might yield my time to Shekar, who has been probably more involved in the discussions, but at the highest level, I would say to set up an issuer that is a co-op of smaller and community banks essentially to be able to do these types of things.

Senator CRAPO. Shekar.

Mr. NARASIMHAN. The Federal home loan banks have already approached the idea of forming a cooperative of community banks and independent mortgage lenders, including CDFIs, that can participate in the secondary mortgage market, can put risk sharing in front of any Government guarantee, can have participants that can use their own documentation, their own credit standards, but have to meet certain norms of underwriting. I think the mechanism is exactly what E.J. Burke said: Figure out a way to give them access to long-term fixed-rate financing that is stable, allow them to continue to do the business they do and perform on their track record.

Senator CRAPO. All right. Thank you very much. And one last question, back to you, Mr. Burke. Some experts have indicated that, at minimum, there are certain markets in this country in which there is sufficient private capital to satisfy the needs of the market without taxpayer backing. Would you agree with that position, that there are some markets where there does not need to be the Government guarantee?

Mr. BURKE. Today there is. I think we have all said that certainly, you know, if you are doing a luxury apartment, luxury high-rise apartment in Los Angeles, today there would be no shortage of lenders that would raise their hand to make that loan. As Mr. Bozzuto has said, in 2009 no one raised their hand. So I think that is the challenge we have, is that markets change every day, and availability of capital changes every day. And whatever legislation, you know, comes through, we have to keep that in mind.

Senator CRAPO. All right. Thank you.

Senator MERKLEY [presiding]. Thank you very much. I appreciated all your testimony, and we are now in overtime, and in that sense, I will be very brief. But I want to address really kind of these different affordability strategies.

One suggestion is that there be basis points at the point of closing and basis points per year on various mortgage-backed securities to fund the Affordable Housing Trust Fund as one way of providing funds that might serve a variety of purposes to assist with affordable housing.

A second approach has been to say that there is a very good chance we are going to have two entities here, spinning off the Fannie and spinning off the Freddie version, and that each of them should have responsibility to serve a significant share of affordable housing, and the suggestion has been that 60 percent of the units should be serving families at 80 percent or less.

We have just heard mention of the co-op strategy, and then also there has been a suggestion that the enterprises that qualify under the multifamily section submit an annual plan on how they are serving rural areas and so on and so forth.

I do not think there has been much discussion to this point today about the concept of the basis points funding the trust fund and about the possibility of a requirement that 60 percent of the units financed by each of the entities serve under 80 percent. So, Mr. Shekar and Ms. Ludwig, would you like to comment on those approaches and the pros and cons?

Mr. NARASIMHAN. Sure. Let me take on the affordability criteria. My principal objective is to try to get them to do what they have been doing, that there has not—that has proven to be successful. They have done this before. They have done it over 10 years. They did it through the crisis. So, therefore, there is no logical reason that private capital can argue, when they have to invest billions of dollars in this business, that it cannot be done or that it requires moving out on the risk curve or otherwise.

So the principal argument is this is the middle of the market. We absolutely want private unguaranteed capital in the market as well, and we want to assure that they stay in the middle of the market and give them a simple level playing field standard that everybody knows up front and they can abide by, not goals that can change over time but this is the standard that they have to live with; when I invest my first dollar of private equity, I know the rules of the game.

Senator MERKLEY. So when folks say to you this has been done by the market without such a requirement, what is the counter position as to why it should now become a specified requirement?

Mr. NARASIMHAN. Well, perhaps you do things inadvertently, and now you can do them more deliberately. I do not think we fully recognized the consequences of implied guarantees until 2008. So I would argue we are doing something very cognitively here to say we will give a limited Government guarantee on securities for certain loans through certain guarantors and issuers that abide by certain rules. And we are setting the rules of conduct, if you will, for the secondary market going forward.

Senator MERKLEY. So in some ways you are saying that given that we are now making an explicit Government guarantee, there should be some standards for how that is utilized to the whole spectrum of housing.

Mr. NARASIMHAN. Yes, sir.

Senator MERKLEY. OK. Thank you.

Ms. Ludwig.

Ms. LUDWIG. Yes, I would agree with Shekar's point of view on that, so I would turn to the fee question, and what we have proposed is a 5- to 10-basis-point fee at the time of securitization on those tranches. And, you know, I guess I would add that this has been congressionally mandated to date for the Affordable Housing Trust Fund and the Capital Magnet Fund, but it has not been funded.

We need assurance of that critical funding for affordable housing. We have just spent a lot of time talking about that need and how essential that is to be able to get into underserved markets and also to serve folks that are lower than 80-percent AMI. Fifty percent and lower in particular for the Housing Trust Fund is one of the uses. The second use, again, is the Capital Magnet Fund, which allows us to leverage private dollars with this capital. And then the third use of those funds would be to create this capacity to address some of the underserved markets, think about product creation, guarantees, subsidies to help on the underwriting costs on some of these pilots. That is the type of innovation that I think we need in this space and that continuing obligation to serve the markets that currently are not getting served.

Senator MERKLEY. Senator Crapo, is there anything else you want to ask?

Senator CRAPO. No.

Senator MERKLEY. I have lots of things I would like to ask, but I am out of time. So in that regard, thank you to all of our witnesses for sharing their thoughts, not just today but in many conversations with different Senators on the panel as we work on these issues. And we look forward to your future input as we continue to work on this.

Thank you very much, and the hearing is adjourned.

[Whereupon, at 11:24 a.m., the hearing was adjourned.]

[Prepared statements, responses to written questions, and additional material supplied for the record follow:]

PREPARED STATEMENT OF THOMAS S. BOZZUTO

CHAIRMAN AND CHIEF EXECUTIVE OFFICER, THE BOZZUTO GROUP, ON BEHALF OF THE NATIONAL MULTI HOUSING COUNCIL AND THE NATIONAL APARTMENT ASSOCIATION

OCTOBER 9, 2013

Chairman Johnson, Ranking Member Crapo and distinguished Members of the Committee, the National Multi Housing Council (NMHC) and the National Apartment Association (NAA) would like to thank you for this opportunity to testify on housing finance reform and the multifamily perspective. We applaud your leadership in seeking to address the fatal flaws in our finance system that led to the fiscal crisis of 2008.

For more than 20 years, the National Multi Housing Council (NMHC) and the National Apartment Association (NAA) have partnered in a joint legislative program to provide a single voice for America's apartment industry. Our combined memberships are engaged in all aspects of the apartment industry, including ownership, development, management and finance. NMHC represents the principal officers of the apartment industry's largest and most prominent firms. NAA is a federation of more than 170 State and local affiliates comprised of 63,000 multifamily housing companies representing 6.8 million apartment homes throughout the United States and Canada.

My name is Thomas S. Bozzuto and I am the Chairman and CEO of The Bozzuto Group. The Bozzuto Group is a privately held, integrated real estate services organization. In our 25-year history, we have created quality homes and extraordinary communities—some 35,000 residences to date. Our more than 1,000 team members pride ourselves on providing outstanding service and consistent value for customers and partners.

I appreciate the opportunity to be here today to present the multifamily industry's perspective on the role of the Government-Sponsored Enterprises (GSEs), Fannie Mae and Freddie Mac, and specifically how the meaningful differences between the multifamily market and single-family market require very different solutions in the context of housing finance reform. I will also discuss why we believe there will be a continued need for Federal involvement in the multifamily sector even after Fannie Mae and Freddie Mac are phased out.

Before I do that, however, allow me to describe some key aspects of the apartment market and how changing demographics will demand a continued flow of capital into this sector if we are to meet the future housing needs.

The apartment sector is a competitive and robust industry that helps 35 million renters live in homes that are right for them. We help build vibrant communities by offering housing choice, supporting local small businesses, creating millions of jobs and contributing to the fabric of communities across the country. And we are increasingly important.

More than a third of America rents, and that number is growing. Between 2007 and 2012, the number of renter households grew by almost five million.[1] In this decade, renters could make up half of all new households—upwards of seven million new renter households.[2] An estimated 300,000 to 400,000 units a year must be built to meet expected demand; yet just 158,000 apartments were delivered in 2012—less than half of what is needed.

While some of this growth is clearly due to the challenging economic circumstances following the recession, the upward trend in renter households predates the fiscal crisis and is increasingly the result of Americans' changing housing preferences. In 1955, married couples with children made up 44 percent of all households. Today they constitute just 20 percent, and that number continues to fall. Among the fastest growing population segments in the next decade will be young adults in their 20s and empty nesters in their 50s—those most likely to seek options other than single-family houses.

In addition, almost 80 million Echo Boomers are beginning to enter the housing market, primarily as renters. Furthermore, many of their parents, the more than 77 million Baby Boomers, are beginning to downsize, and some will choose the convenience of renting.

All this increasing demand is good news because meeting it will create millions of jobs. Apartments are more than just shelter. They are also an economic power-

[1] 2012 American Community Survey 1-Year Estimates, U.S. Census Bureau, "Tenure". 2007 American Community Survey 1-Year Estimates, U.S. Census Bureau, "Tenure".

[2] Based on Harvard University Joint Center for Housing Studies' forecast of 13.8 million new households by 2030. The State of the Nation's Housing 2012, The Joint Center for Housing Studies of Harvard University, p. 16. *http://www.jchs.harvard.edu/sites/jchs.harvard.edu/files/son2012.pdf*

house. The $1.1 trillion industry oversees apartment stock valued at $2.2 trillion. In 2011, the apartment industry and its residents supported 25.4 million jobs. Moreover, in 2011, new apartment construction alone produced $14.8 billion in spending, supported 323,781 jobs and had a total economic contribution of $42.5 billion. The same year, the operation of the Nation's existing apartments accounted for $67.9 billion, 2.3 million jobs and a total economic contribution of $182.6 billion. Apartment resident spending in 2011 totaled $421.5 billion, supporting 22.8 million jobs and a total economic contribution of $885.2 billion. To put these numbers into perspective, apartments and the people who live in them contribute, on average, more than $3 billion a day to the economy.

Finally, apartments also produce societal benefits; not only are they environmentally sustainable, resource-and energy-efficient, but they also help create a mobile workforce that can relocate to pursue job opportunities.

I highlight these important changes in housing choice, supply and demand as well as the economic and social contributions apartments make to society to explain why it is so important for Congress to consider the unique needs of the apartment industry as it pursues mortgage finance reform options.

Many factors influence the apartment industry's health and ability to meet the Nation's growing demand for rental housing, but the availability of consistently reliable and competitively priced capital is the most essential.

The Great Recession exposed serious flaws in our Nation's residential home mortgage finance system. The apartment industry did not overbuild and for the most part did not overleverage during the housing boom, and the GSEs' multifamily programs did not contribute to the housing meltdown and are not broken. Unfortunately, the losses experienced in their single-family divisions have overshadowed the strong mortgage financing and credit performance of their multifamily programs.

More than just performing well, the GSEs' multifamily programs serve a critical public policy role by addressing a market failure in the housing finance system that results in an overabundance of capital for high-end properties in top-tier markets, but leaves secondary and tertiary markets like Westerly, RI, or Topeka, KS, underserved. The GSEs ensure that multifamily capital is available in all markets and at all times, so the apartment industry can address the broad range of America's housing needs from coast to coast and everywhere in between.

Let me be clear, I am not here to defend the GSEs or to suggest that they be continued in their current form. Instead, I would like to highlight for the Committee those elements of the existing system that worked well for multifamily lending and, more importantly, at no cost to the taxpayer. It is our hope that these successful elements can be incorporated into whatever Congress designs to replace Fannie Mae and Freddie Mac.

Multifamily Performance: A Success Story

It is hard to imagine a success story coming out of the worst housing crash in recent history, but the performance of the GSEs' multifamily businesses stands out. Overall loan performance remains strong with delinquency and default rates at less than 1 percent, a tenth of the size of the delinquency/default rates plaguing single-family. The GSEs' multifamily programs have also outperformed Commercial Mortgage-Backed Securities (CMBS), commercial banks and even FHA. In addition, since the Federal Government placed the GSEs in conservatorship, the multifamily programs have generated over $10 billion in net profits for the Federal Government.

Not only are the GSEs' multifamily programs operating in a fiscally sound manner, but they are also doing so while offering a full range of mortgage products to meet the unique needs of the multifamily borrower and serve the broad array of property types. This includes conventional market rental housing, workforce rental housing, and targeted affordable housing (e.g., project-based Section 8, State and local government subsidized and Low-Income Housing Tax Credit (LIHTC) properties).

The GSEs' multifamily programs adhere to a business model that includes prudent underwriting standards; sound credit policy; effective third-party assessment procedures; risk-sharing and retention strategies; effective loan portfolio management; and standardized mortgage documentation and execution. In short, the GSEs' multifamily models hit the mark. They have attracted enormous amounts of private capital; helped finance millions of units of market-rate workforce housing without direct Federal appropriations; sustained liquidity in all economic climates; and ensured safety and soundness of their loans and securities. As a result of the liquidity provided by the GSEs, the United States has the best and most stable rental housing sector in the world.

A One-Size-Fits-All Solution Will Not Work

It is tempting to believe that a single solution will solve all that ails our housing finance system. Unfortunately, that simply is not the case. Multifamily finance and single-family finance operate differently. The capital sources for multifamily are not as wide or as deep as those financing single-family, and the loans themselves are not as easily commoditized. Moreover, the financing process; mortgage instruments; legal framework; loan terms and requirements; origination; secondary market investors; underlying assets; business expertise; and systems are all separate and unique from single-family home mortgage activities. It is, therefore, critical for Congress to pursue a separate solution for multifamily. Failure to do so puts the millions of Americans who rely on the apartment industry for their housing and the $862 billion multifamily debt market at risk.

Although I talked about rising demand and the need for new construction to meet it, preserving liquidity for multifamily is about more than just building new apartments. Unlike residential mortgages, which are typically for 30-year terms, most multifamily mortgages are for a period of 7 to 10 years. This ongoing need to refinance apartment mortgages makes it imperative for the industry to have access to reliable and affordable capital at all times, in all markets and in all market conditions. In 2013 alone, an estimated $100 billion in multifamily mortgages will need to be refinanced, many of which finance apartments that are not located in areas that attract private capital.

Private Capital Is Necessary, but Not Sufficient

We share your collective desire to return to a marketplace dominated by private capital. Even with the critical backstop provided by the GSEs, private capital has always been an integral part of the multifamily housing finance system. However, historically, private capital has been either unwilling or unable to meet the full range of the multifamily industry's capital needs, even during healthy economic times. There is no evidence to suggest that the situation is any different today.

Historically, the apartment industry has relied on a variety of capital sources to meet its liquidity needs. They include:

- Fannie Mae and Freddie Mac
- Commercial Banks and Thrifts
- Life Insurance Companies
- Federal Housing Administration
- Commercial Mortgage-Backed Securities/Conduits
- Pension Funds
- Private Mortgage Companies

Together, these capital sources have provided the apartment sector with $100 billion to $150 billion annually, reaching as high as $225 billion last decade, to develop, refinance, purchase, renovate, and preserve apartment properties. Each of these capital sources has its own focus, strengths and limitations.

Commercial banks and thrifts generally serve as a source of credit for smaller, local borrowers. They typically provide floating rate, short-term debt, and often their willingness to extend this credit is based on the availability of permanent take-out financing offered by the GSEs. They have resumed lending to multifamily after the crisis, but they are unlikely to return to their precrisis levels because of higher risk-based capital requirements.

Life insurance companies tend to restrict their lending to a handful of primary markets and to luxury apartment properties. They do not generally finance affordable apartments, and their loan terms typically do not extend beyond 10 years. Importantly, they enter and exit the multifamily market based on their investment needs and economic conditions. On average, they have generally provided 10 percent or less of the annual capital needed by the multifamily industry, but that number has gone as low as 3 percent.

The private-label CMBS market did not become a material source of capital to the apartment industry until the mid-1990s, peaking at 16.5 percent of the market ($17.6 billion a year) in the housing bubble years of 2005–2007. The CMBS market completely shut down after the 2008 crisis and suffered high delinquency rates—reaching 17.4 percent in 2011. While CMBS is rebounding, regulatory changes imposed by financial regulatory reform legislation will mean that it will not return to its pre-bubble levels of lending.

Some have suggested that the Federal Housing Administration (FHA) could step in and fill the liquidity provided by Fannie Mae and Freddie Mac. This solution is unrealistic. FHA serves a very different market from Fannie Mae and Freddie Mac, focusing on construction lending and affordable rental properties not served by other sources of capital.

In all, however, FHA represents 9 percent of all outstanding multifamily mortgage debt, and even at that level has experienced serious capacity issues. When demand for FHA financing spiked during the credit crisis, FHA's backlog was so significant that borrowers reported loan applications languishing for 18 months or more.

Private capital has returned to the apartment sector, but already in this recovery we are seeing the historical pattern of uneven access to capital repeat itself. The new private capital coming into the apartment sector is concentrating in a handful of cities and on trophy assets. Apartment firms providing critical housing in secondary and tertiary markets and rural areas are not benefiting from the resurgence in private capital. Even in the larger markets, firms providing workforce housing find themselves equally shut out. The market failure the GSEs' multifamily programs addressed was ensuring capital reached markets deemed too risky or otherwise undesirable by institutional capital. It is imperative that a reformed system continue to fill this important public policy need.

Finally, it must be noted that a December 2012 Freddie Mac report commissioned by the Federal Housing Finance Agency (FHFA) estimated the potential consequences to the apartment sector of eliminating the Federal guarantee. According to that research, which was undertaken by Freddie Mac and independent third-party experts, interest rates would rise and debt financing capital would fall by 10 percent to 20 percent. That could result in a 27-percent drop in apartment supply, which could, in turn, cause rising rents nationwide and significant spikes in tertiary geographic markets. [3]

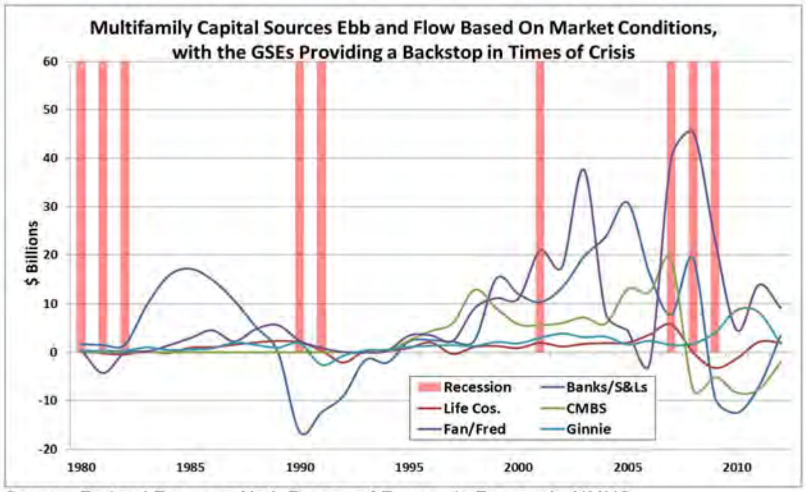
Federal Credit Guarantee: Meeting the Needs When Private Capital Disappears

Fannie Mae and Freddie Mac have served as the cornerstone of the multifamily housing finance system, successfully attracting private capital to the sector. Unlike any other single source of capital, they offer long-term debt for the entire range of apartment properties (market-rate work-force housing and subsidized properties, large properties, small properties, etc.), and they are active in all markets (primary, secondary and tertiary) during all economic conditions.

As the chart below shows, the Enterprises' share of the multifamily mortgage market has varied considerably over time, increasing at times of market dislocation when other sources of capital are scarce and scaling back during times when private credit is widely available.

When credit markets have been impaired for reasons that have nothing to do with multifamily property operating performance, the federally backed secondary market has ensured the continued flow of capital to apartments. For example, when private capital left the housing finance market in 2008, the apartment industry relied almost exclusively on Fannie Mae, Freddie Mac, and FHA/Ginnie Mae for capital.

[3] Freddie Mac, "Report to the Federal Housing Finance Agency: Housing Finance Reform in the Multifamily Mortgage Market", pp. 24–32. *http://www.fhfa.gov/webfiles/25161/FREReport__MF__MarketAnalysis.pdf*



Source: Federal Reserve, Natl. Bureau of Economic Research; NMHC

Between 2008 and 2010, the GSEs provided $94 billion in mortgage debt to the apartment industry. Without that critical backstop, thousands of otherwise performing multifamily mortgages would have gone into default because there were no private capital sources willing to refinancing maturing loans. This could have meant disruption to millions of renter households. The GSEs served a similar role during the 1997–1998 Russian financial crisis and in the post-9/11 recession of 2001.

Even now, with all players back in the market, Fannie Mae and Freddie Mac still provided 45 percent to 50 percent of multifamily mortgage debt in 2012. Again, this is not meant to suggest that Fannie Mae and Freddie Mac be allowed to continue. Rather it is to point out how large a chasm private capital would have to fill and to emphasize the public policy mission the existing system has served, ensuring liquidity and avoiding widespread adverse effects for the millions who rent.

Principles of Reform

There is widespread agreement that Fannie Mae and Freddie Mac must be dissolved. A reformed housing finance system should, however, retain the successful components of the existing multifamily programs in whatever succeeds them. Accordingly, multifamily housing reform must:

1. Provide Access to Federal Credit Support.

Given the market failure of the private sector to meet the apartment industry's broad capital needs, an explicit Federal guarantee for multifamily-backed mortgage securities should be available in all markets at all times. A private-only housing finance system would result in an abundance of capital for high-end properties in top-tier markets but leave secondary and tertiary markets like Sioux Falls, SD, or Boise, ID, underserved.

2. Provide Broad Liquidity Support at All Times, Not Just "Stop-Gap" or Emergency Financing.

Any Federal credit facility should be available to the entire apartment sector and not be restricted to specific housing types or renter populations. Moreover, it would be impossible to turn on and off a Government-backed facility without seriously jeopardizing capital flows.

3. Restrict Federal Credit Support to the Security Level.

The benefit of any Federal guarantee should only accrue to the investors of multifamily mortgage-backed securities; it should not apply to the underlying multifamily mortgages or the entities issuing the securities.

4. Support Private Capital and Protect Taxpayers Through Effective Guarantee Structure and Pricing.

Borrowers should pay for the guarantee in the form of an appropriately priced credit enhancement fee that insures taxpayers against future losses. Additionally, the fee should be priced to ensure that any advantage the GSEs historically have enjoyed over private mortgage capital is addressed and market participants not using Government guarantees are not crowded out.

5. Encourage Competition.

Other entities should be allowed to obtain a Federal charter to compete with the GSEs or their successors if they can meet mandated requirements, including robust levels of core capital and significant experiences in mortgage underwriting.

6. Empower a Strong Regulator.

A strong and independent regulator with expertise in multifamily lending is critical. To ensure sufficient financial resources and political independence, the regulator should be funded through industry assessments instead of congressional appropriations as is the case with the Federal Deposit Insurance Corporation, the Federal Reserve, and Office of the Comptroller of the Currency.

7. Impose Effective Capital Requirements.

Effective capital reserve requirements, both for mortgages held in portfolio and those securitized, are vital to further protect taxpayers from future losses.

8. Retain Limited Portfolio Lending (Without a Federal Guarantee) While Expanding Securitization.

Any restructured or successor entity should be able to retain limited multifamily mortgage portfolios, but no Government guarantee should apply to mortgages held in portfolio. Limited retained portfolios would be allowed for the following activities: (1) aggregating mortgages for pooled securities executions; (2) implementing pilot mortgage programs and product modification testing; (3) engaging in targeted higher-risk transactions (e.g., financing properties with rent-regulatory restrictions, student housing and senior and assisted-living developments); and (4) engaging in pilot and risk-sharing transactions for affordable and workforce housing production. To avoid a return to an overreliance on portfolio lending, portfolio loans would be subject to: (A) commercial bank mortgage risk-based capital standards; and (B) limits regarding absolute levels and percentage of guaranteed mortgage securities.

9. Reduce Existing Portfolios in a Responsible Manner.

As the GSEs are wound down, the current GSE multifamily portfolios should be largely transferred to the Federal Government to allow taxpayers to capture the portfolios' positive income stream and to eliminate any market advantage the GSE-successor entities would gain by retaining them on their balance sheets. However, any GSE-successor entities should be allowed to retain the minimum number of mortgages currently held in portfolio that are necessary to make them operationally viable. The GSE-successor entities should be charged with continuing to service the mortgages transferred to Government control and would be paid a fee for doing so.

10. Create Certainty and Retain Existing Resources/Capacity During the Transition.

To avoid market disruption, it is critical that policy makers clearly define the Government's role in a reformed system and the timeline for transition. Without that certainty, private capital providers (e.g., warehouse lenders and institutional investors) are likely to limit their exposure to the market, which could cause a serious capital shortfall to rental housing. In addition, during the transition years, it is vital to retain many of the resources and capacity of the existing GSEs. The two firms have extensive personnel and technological expertise, as well as established third-party relationships with lenders, mortgage servicers, appraisers, engineers and other service providers, which are critical to a well-functioning secondary market.

11. Focus on Liquidity, Not Mandates.

The public mission of a federally supported secondary market for multifamily should be clearly defined and focused primarily on using a Government backstop to provide liquidity and not for specific affordable housing mandates.

Essential Elements of a Reformed Multifamily Housing Finance System

Putting the principles outlined above into legislative action could be accomplished in a number of ways. We have provided additional details in Appendix I. NMHC/NAA believe that Congress would be well served by including the following provisions in any housing finance reform legislation:

1. Separate Title Addressing the Unique Needs of the Multifamily Sector

As noted earlier, a one-size-fits-all solution will not work in housing finance reform. We strongly recommend that any reform measure include a separate multifamily title. This separate title should address not only what will replace the GSEs' multifamily programs, but also how the transition to that new system will be handled.

2. Establish an Office of Multifamily Mortgage Oversight

An Office of Multifamily Mortgage Oversight should be established to oversee and regulate all aspects of Government-backed multifamily mortgage finance. In addition to serving as regulator, this Office should be charged with establishing and collecting fees paid by borrowers for Government-backed mortgages.

3. Transfer the Enterprises' Multifamily Activities to Successor Entities

Having documented the need for an ongoing Federal presence in multifamily finance, namely to serve properties and localities not well served by private capital, and having established the strong performance record of the existing GSEs' multifamily programs, reform legislation should include a mechanism for explicitly transferring Fannie Mae and Freddie Mac's multifamily lines of business to successor entities. This transfer should be separate and apart from the GSEs' single-family business given the significant differences between the two. We recommend that the regulator oversee the complete privatization of Fannie Mae and Freddie Mac's multifamily lines of business beginning no later than one year after a new regulator is put into place. In addition to overseeing the transition of Fannie Mae and Freddie Mac's multifamily programs from Government-sponsored enterprises to privately held entities, the regulator should evaluate whether there should be more than two private entities chartered to issue guaranteed mortgage-backed securities.

Focus on Liquidity Given the Innate Affordability of Multifamily

Policy makers are understandably still struggling to determine the degree to which an ongoing Federal role in the rental finance system should be connected with the pressing need to address the Nation's affordable housing shortage. We begin by noting that multifamily housing is inherently affordable housing; fully 82 percent of existing apartments are affordable to households earning 80 percent of area median income, a common standard for measuring affordability. Therefore, the mere extension of a Government role to ensure liquidity to the multifamily sector is, by definition, supporting affordable housing.

It is tempting to believe that more can be done to address affordability through housing finance reform, namely through imposing limitations on Federal guarantees or other mandated benchmarks. We caution policy makers not to overreach, however, as such well-intended moves, if overly prescriptive, could have adverse consequences.

To begin with, one way the GSEs have been able to produce such a stellar performance record in multifamily is by being able to build a balanced book of business where lower-risk, higher-end properties enabled them to take on riskier, deeply targeted affordable housing properties, such as Section 8 and Low-Income Housing Tax Credit properties. Just as critical, the GSEs' multifamily programs have been able, through their broad platforms, to provide capital for projects located in markets that do not meet the credit or return standards required by many private capital debt providers.

Not only does a broad multifamily lending platform help the GSEs and successor entities manage risk, but it also ensures that there is a sufficient supply of liquidity in severe market downturns. For instance, in the most recent financial crisis, even firms and properties that would normally be well served by private capital found themselves with no options.

After 2008, the insurance companies, banks and other private capital debt providers exited the market leaving even higher-rent or luxury properties scrambling for debt capital to refinance maturing mortgages. Publicly traded apartment REITs were unable to issue bonds to finance their assets and had to seek funding from Government programs. If the successor entities to Fannie Mae and Freddie Mac are more limited in what markets or properties they can serve, they will be unable to fill the critical public policy mission they have historically served. Failure to ensure sufficient liquidity for all types of apartments will have a spillover effect that could be disastrous for America's renters.

Nevertheless, we understand the need to tackle housing finance reform and affordability in the same debate. NMHC/NAA are reviewing the spectrum of options that could serve the Nation's affordability needs without putting the broader multifamily market at risk. They include portfolio goals, explicit on-budget funding, loan limits and affordability-based-guarantee-fee pricing. NMHC/NAA look forward to working with Congress on developing workable solutions to this vital policy issue.

Comment on Federal Housing Finance Agency Action To Curtail Fannie Mae and Freddie Mac's Multifamily Activities

Before closing, I would like to draw to the Committee's attention a letter that NMHC/NAA submitted to the Federal Housing Finance Agency (FHFA) regarding strategies it is considering as part of its 2014 Scorecard to reduce Fannie Mae and Freddie Mac's multifamily businesses. We appreciate that FHFA is seeking input before making this decision. However, placing caps on the GSEs' multifamily lending volume and reducing the diversity and availability of multifamily mortgage products as FHFA has proposed are not justified or necessary and will only lead to market uncertainty and instability. For this reason, we cannot support any further actions to restrict liquidity to the industry and residences we serve. Moreover, decisions made regarding the Enterprises' future activities are best left to Congress as opposed to their regulator. (Appendix II: NMHC/NAA Comment Letter: FHFA Letter To Limit Enterprises' Multifamily Activities.)

Finally, I would like to take a moment to address the opportunity you have to rebalance our national housing policy through housing finance. For decades, the Federal Government has pursued a "home ownership at any cost" housing policy, ignoring the growing disconnect between the country's housing needs and its housing policy. That had a devastating effect on our national economy, on local communities and for millions of households.

We now know that housing our diverse Nation means having a vibrant rental market along with a functioning ownership market. How we as a Nation tackle the housing finance reform effort that must be undertaken will, in large part, determine whether or not the country continues to have a strong rental sector. The stakes are too high to let the multifamily market become a collateral victim of the single-family housing crash.

I thank you for the opportunity to present the views of NMHC and NAA.

Appendix I

Suggested Legislative Recommendations for a Multifamily Title in Housing Reform Legislation

To implement the principles of reform NMHC/NAA recommend any legislation should include the elements outlined below. Because of the multifamily industry's unique needs and requirements, housing finance reform legislation should have a separate title governing the treatment of the sector. This will enable the government to wind down Fannie Mae and Freddie Mac's current multifamily activities and construct a new system enabling the apartment industry to access the capital necessary to meet the demand of America's renters.

Specific Recommendations

1. **Establish an Office of Multifamily Mortgage Oversight**

   Purpose

   - A new Office of Multifamily Mortgage Oversight would be charged with ensuring: (1) liquid capital is available in all markets at all times and for a wide range of multifamily property types; (2) transparency in the multifamily marketplace; and (3) access to federal mortgage credit to support a robust secondary multifamily mortgage and active multifamily mortgage backed securities.

   The Office of Multifamily Mortgage Oversight would have the following duties:

   - Market Regulator

     The Office of Multifamily Mortgage Oversight should be established as a separate unit within the entity ultimately charged with regulating the nation's government-backed housing finance programs. The Office of Multifamily Mortgage Oversight must have the capacity to evaluate the overall multifamily market, as well as expertise in multifamily mortgage underwriting, investment and securitization. This Director of the Office of Multifamily Mortgage Oversight should report to the chief executive and have dedicated research capacity and technical and capital markets expertise.

- Establish Standard Form Structures, Contracts, Reporting, Data Repository Maintenance
  There should be a uniform repository established for multifamily mortgage origination data for properties with five or more units. Information collected and made available with appropriate disclosure to investors should include property characteristics, borrower type, principal amount, interest rate, term, amortization, maturity date and effective prepayment date.

- Establish and Maintain Government Capital Through an Insurance or Reserve Fund Used Only to Pay Investors in Multifamily Securities
  A government guarantee of multifamily securities will exist exclusively to backstop, multifamily mortgage lending and securities activities.

- Establish and Collect Fees in Exchange for Providing Insurance on Principal and Interest of Qualified Securities.
  The guarantee fee and other fees to support targeted housing activities shall be collected as a portion of the monthly mortgage payment in the form of an appropriately priced credit enhancement fee that insures taxpayers against future losses.

- Authority to Protect Taxpayers in Unusual and Exigent Market
  The Office of Multifamily Mortgage Oversight may, upon determination that a material threat exists to the multifamily housing finance system, provide enhanced support to the market for a defined period.

2. Transfer Enterprises' Multifamily Activities to Successor Entities

Regardless of the transition of the single-family mortgage activities, a transition process tailored to the multifamily industry's needs is necessary because of the significant differences in capital sources and operations between single-family and multifamily mortgages. This different treatment is further justified by the long track record of strong credit performance in the Enterprises' multifamily programs. (See Overview of Multifamily Capital Sources in Appendix II).

The multifamily industry's ability to develop new properties, as well as to refinance the estimated $100 billion a year in mortgages that mature, relies heavily on reliable and stable access to credit and the existing origination and servicing expertise that is the result of the Enterprises' multifamily programs. Material disruptions in the debt capital markets will reverberate through local, regional and the national economies. To avoid triggering this consequence as Fannie Mae and Freddie Mac are wound down, the following actions are recommended to facilitate disposition of the Enterprises' multifamily portfolios and the transfer of their mortgage activities to successor entities.

A. As fully described below, the multifamily activities of Fannie Mae and Freddie Mac should be privately capitalized. Furthermore, additional entities should be approved to benefit from a partial government security guarantee.

B. Upon enactment of housing finance reform legislation, each Enterprise should be required to:

- Establish separate accounting for multifamily activities.
- Continue to reduce its multifamily portfolio and eliminate any portfolio activities other than those necessary to aggregate and facilitate securitization and address troubled mortgage assets.

C. Upon enactment of housing finance reform legislation, each Enterprise should be required to set aside up to 75 percent of all net proceeds from multifamily mortgage activities into a separate account. These funds are to be used only to assist in the capitalization of the GSEs' multifamily units. Such proceeds should be exempt from the Treasury Stock Purchase Agreement and subsequent requirements for transfer of funds by the Enterprises.

D. Each Enterprise should be asked to prepare a capitalization plan, including an asset management plan for existing multifamily mortgage and guaranteed mortgages. This plan shall be submitted to the regulator upon its certification.

E. The regulator will approve or modify the capitalization plans and instruct the Enterprises to implement the capitalization and privatization of each multifamily unit within 12 months of certification. Any extension of the privatization activities will require approval of the regulator and may not exceed 36 months from the certification date.

F. Until such time as the multifamily activities are capitalized, the government must conduct activities to effectively oversee and support future multifamily secondary market financing. These activities include:

- Multifamily issuer, guarantor and associated entity oversight (servicer and special servicer);
- Guarantee fee administration and assessment;
- Credit policy and regulatory capital oversight;
- Product performance review and approval; and
- Loan performance, portfolio and security guarantee assessment and market analysis.

G. Upon successful capitalization, the new entity must repay, with interest at a rate determined by the Treasury Department, any dedicated revenues held by the government used to collateralize the privatization of the GSEs' multifamily mortgage activities. The repayment term may not exceed five years from initial capitalization.

H. Any revenues not used to capitalize the multifamily activities shall be returned to the Treasury.

I. All multifamily mortgage assets and guaranteed mortgages prior to privatization will transfer to the government.

J. The government will enter into an asset management agreement with the two approved successor entities to oversee the remaining multifamily portfolios and guaranteed mortgage assets at the time of regulator certification.

After successfully transitioning Fannie Mae and Freddie Mac from their status as government-sponsored enterprises to privately held entities, the government may act to expand the number of private entities to serve as approved issuers and or guarantors. Due to the need to retain a minimum share of the market, the government should approve entities on a limited basis until it determines the effectiveness and limitations of government credit and non-government credit to the multifamily market.

NMHC National Multi Housing Council®
Apartments: Smart Communities, Smarter Living

Appendix II

October 7, 2013

Federal Housing Finance Agency
Multifamily Housing Policy
400 7th Street, S.W., Room 9-261
Washington, DC 20024

Delivered electronically to multifamilypolicyissues@fhfa.gov

RE: Options for Reducing Fannie Mae and Freddie Mac's Multifamily Business, Released by the Federal Housing Finance Agency for Public Input

To Whom It May Concern:

On behalf of the multifamily industry, the National Multi Housing Council and National Apartment Association (NMHC/NAA) appreciate the opportunity to respond to the Federal Housing Finance Agency's (FHFA) August 9, 2013, request for input on strategies for further reducing Fannie Mae and Freddie Mac's presence in the multifamily housing finance market in 2014.

For more than 20 years, the National Multi Housing Council (NMHC) and the National Apartment Association (NAA) have partnered in a joint legislative program to provide a single voice for America's apartment industry. Our combined memberships are engaged in all aspects of the apartment industry, including ownership, development, management and finance. NMHC represents the principal officers of the apartment industry's largest and most prominent firms. NAA is a federation of more than 170 state and local affiliates comprised of 63,000 multifamily housing companies representing 6.8 million apartment homes throughout the United States and Canada.

While the apartment industry supports the return of a more robust private capital market, we believe that setting caps on the GSEs' multifamily lending volume and reducing the diversity and availability of multifamily mortgage products could interfere with stabilizing market forces currently at work. Fannie Mae and Freddie Mac served as an essential backstop during the economic downturn, maintaining liquidity in the market when private capital retreated.

As the economy has continued to recover, private capital has once again returned to the market, helping reduce the GSEs' share. In fact, the Mortgage Bankers Association estimates that Fannie Mae and Freddie Mac provided just 43 percent of the new multifamily mortgages originated in 2012, down from 85 percent in 2009. Their shares are estimated to fall as low as 30 percent or less in 2013. This drop reflects the fact that private capital sources have been, and will continue to be, the primary source of mortgage debt for the apartment industry. Notably, the marketplace has not needed artificial regulatory constraints to make room for that private capital. Market dynamics have accomplished it.

FHFA's latest announcement identifies a number of strategies with respect to the GSEs that the agency has under consideration, including restrictions on available loan terms, a reduction in loan products and limits on property financing and business activities. NMHC/NAA are concerned that the effects of implementing any of these strategies, individually or in combination, could disrupt the apartment industry in both the near and long terms. Mandated reductions in the GSEs' footprint create unnecessary uncertainty and could negatively affect a stable source of financing for a wide range of apartment properties in markets nationwide, threatening the industry's recovery at a time when rental demand continues to grow. Furthermore, these proposed strategies could reduce the GSEs' ability to respond to changing market conditions, leaving the apartment industry vulnerable in times when private capital sources are less active in the market. Finally, the strategies FHFA is evaluating could circumvent legislative proposals that Congress is currently considering as part of housing finance reform efforts.

Building, operating and maintaining our nation's rental housing is a capital-intensive activity. The apartment industry relies on private and public capital, as well as short- and long-term debt, to fund the development, operation and necessary maintenance of, and reinvestment in, real estate. This liquidity is critical to our industry's ability to provide safe, decent and affordable housing to 17 million households.

On a macro level, market experience leads us to conclude that artificially limiting the debt provided by Fannie Mae and Freddie Mac's multifamily programs will harm apartment availability by limiting options and creating voids in select markets. Although private capital is returning to the multifamily sector, it is not universally or equally available in all local markets. As a result, it is critical for there to be a national debt source that features a full range of mortgage options.

Furthermore, it is vital to note that Fannie Mae and Freddie Mac are not just capital sources. Because of the wide range of multifamily mortgage products they provide, they support and influence other debt providers by setting standards. Artificially constraining the Enterprises will result in a meaningful loss in competition and innovation that have benefitted borrowers and renters alike.

The apartment sector's investor base has expanded as well. Over the last 30 years, the industry has evolved from a mostly local individual owner/operator business to a sector with a growing number of regional and national firms. It now attracts high-net-worth private, corporate, pension and institutional investment fund capital, both within the United States and outside its borders. Thousands of properties and millions of units are operated under a wide variety of ownership structures, serving the ever-expanding needs of renter populations in our nation's towns, cities, suburban and rural areas.

It is also critical to understand that dislocations in the multifamily debt capital market ultimately impact America's renters by potentially restricting new supply at a time when demand for apartments is growing rapidly. With 77 million Baby Boomers who may consider downsizing and nearly 80 million Echo Boomers who are beginning to enter the housing market, NMHC projects that up to seven million new renter households will form this decade. Unfortunately, supply is already falling short of meeting this demand. An estimated 300,000 to 400,000 units a year must be built to meet expected demand; yet just 158,000 apartments were delivered in 2012 – less than half of what is needed.

In serving America's workforce, the apartment industry relies on a variety of capital sources and loan products to meet the nation's housing needs. Unlike the single-family housing finance system, each apartment loan must be customized and tailored. This is just one of the many reasons why the Enterprises serve a critical role in the multifamily sector. Regulators should also note that the availability of debt capital is not just essential for financing properties, but also for supporting the long-term operation of apartment communities.

Given that housing for America's families is at stake, NMHC/NAA request that FHFA, prior to advancing any proposals to limit the GSEs' multifamily activities, first assess the impact of such actions relative to the availability of sufficient multifamily capital in all markets nationwide. Until such analysis demonstrates that FHFA's proposed actions will not impact the availability of multifamily housing now and in the future, these actions should be tabled. Put simply, the risk is too great, especially at the present time when government policy has a significant influence on the financial and debt markets. Finally, it must be noted that Congress is currently examining housing finance reform legislation, and these efforts should be allowed to play out.

General Observations

First and foremost, we strongly urge FHFA to adopt the position of "do no harm." Placing additional restrictions on the Enterprises' multifamily lending activities will harm the debt markets serving the multifamily industry. We also believe the actions are simply unwarranted.

Before addressing the specific options FHFA outlined in its notice to reduce the Enterprises' multifamily mortgage footprint, we would first like to offer the following observations challenging the need for such action.

1. **Enterprise Debt Complements Other Capital**

   The evidence does not support the claim that the Enterprises' multifamily mortgage activities are crowding out the private market. Instead, their activities have historically ebbed and flowed based on market conditions. As the chart below indicates, except for the first part of the last decade, the multifamily mortgage capital backed by the Enterprises totaled less than the private capital serving the marketplace. When the markets expanded significantly in the early to middle part of the last decade, the Enterprises' share decreased significantly. The data also highlight that the Enterprises quickly responded to market conditions. When private capital became constrained, the Enterprises' share increased. This response is most evident during the recent recession. The Enterprises stepped in to serve a market for which private capital was significantly constrained. Once capital markets began to thaw, however, the Enterprises' share of multifamily mortgage capital began to decline.

Estimating the multifamily mortgage origination market is difficult, as complete data reflecting each source of capital does not exist. Furthermore, the available data is often an estimate that is the result of multiple assumptions. In 2012, the Mortgage Bankers Association (MBA) estimated the multifamily mortgage origination market, as measured by total debt closed, to be $143 billion.[1] MBA forecasts that the 2013 multifamily mortgage origination market will grow by 30 percent to $187 billion.[2] In 2012, the Enterprises' share of this market was 45 percent and should fall to 31 percent in 2013 given the cap on multifamily business put in place by FHFA earlier this year. Had the Enterprises' debt increased year-over-year by 10 percent, to $70 billion, in 2013, without an artificial cap, we estimate their market share would have declined by 8 percent to 37 percent of overall multifamily mortgage originations.

2. **FHFA Caps on Multifamily Activities Are Unwarranted and Threaten to Harm Taxpayers Instead of Protecting Them**

In a meeting with NMHC officers and staff on September 18, 2013, FHFA Acting Director Edward DeMarco said that plans to place limits on the Enterprises' multifamily mortgage activities are designed to protect Fannie Mae and Freddie Mac and insulate taxpayers against further losses. Although NMHC/NAA certainly support strong credit standards, FHFA's broad actions relative to the size of the Enterprises' multifamily businesses are unwarranted and unnecessary to further these objectives:

- The Enterprises' multifamily activities, not including lost benefits attributable to the Low-Income Housing Tax Credit, have been revenue positive and captured capital well in excess of needs to protect the taxpayer against losses. Fannie Mae reports that in 2012 its multifamily programs generated net income of $1.5 billion whereas Freddie Mac's segment earnings from multifamily programs registered $2.1 billion for that year.[3]

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[1] Mortgage Bankers Association, 2012 C/MF Annual Origination Volume Summation, February 2013.
[2] Mortgage Bankers Association, Q1 2013 Commercial/Multifamily Mortgage Bankers Originations, April 30, 2013.
[3] Form 10-K, Annual Report Pursuant to Section 13 of 15(d) of the Securities Exchange Act of 1934 for the Fiscal Year Ended December 31, 2012, Federal National Mortgage Association, pg. 94. Form 10-K, Annual Report Pursuant to Section 13 of 15(d) of the Securities Exchange Act of 1934 for the Fiscal Year Ended December 31, 2012, Federal Home Loan Mortgage Corporation, pg. 108.

- During the housing crisis, the Enterprises' multifamily risk-based capital and earnings actually subsidized losses in the single-family mortgage sector. NMHC/NAA strongly advocate the Enterprises' multifamily risk-based capital be separately maintained and reflected on balance sheets.

- Imposing further restrictions on the Enterprises' multifamily mortgage activities effectively denies the government the ability to recoup borrowed capital that would otherwise be generated from the strong performance of the multifamily business. As noted above, the Enterprises' multifamily mortgage activities are currently generating a substantial positive return to taxpayers.

- The Enterprises' multifamily portfolios are already shrinking as activities have moved from a balance-sheet-dominated execution to a securitization-based execution. This shifts risk to private capital and away from the Enterprises.

3. The Enterprises' Multifamily Performance Does Not Justify Scaling Back Their Activities

There are no credit risk reasons to justify federal intervention in the Enterprises' multifamily programs at this time. Compared to other sources of multifamily capital, the Enterprises have the strongest performance record. As a result of their already solid underwriting standards, multifamily mortgage credit remains the best in the industry and continues to improve. Based on these facts, placing limitations on the Enterprises' multifamily mortgage activities is unwarranted from a risk-based capital or credit risk perspective.

According to MBA data released for the second quarter of 2013, Fannie Mae's multifamily serious delinquency rate (60+ days) is 0.28 percent, and Freddie Mac's multifamily serious delinquency rate (60+ days) is 0.09 percent.[4] By comparison, commercial banks, community banks and thrift institutions have a serious delinquency/default rate (90+ days) of 2.16 percent, a substantially higher rate. Furthermore, these entities all benefit from deposit insurance that allows them to assume risk on investments including commercial and multifamily real estate lending. Commercial mortgage-backed securities (CMBS) have the highest serious multifamily mortgage delinquency rate among all sources (30+ days) at 7.81 percent. Finally, it must be noted that although life insurance companies reported a 0.08 percent delinquency rate, they limit their exposure to the highest-quality properties located in core urban markets. Accordingly, their risk profile cannot be accurately compared to other sources of debt capital. (See Appendix III for historical delinquency data)

4. Enterprises' Multifamily Programs Ensure All Markets Are Served At All Times

The apartment sector has historically relied on a wide range of capital sources in addition to the GSEs. They include commercial banks, life insurance companies, CMBS and the Federal Housing Administration's (FHA) multifamily programs. That said, each of these has its own focus, strengths and limitations. Moreover, even during healthy economic times, the private-market sources on a collective basis simply have been unwilling

[4] Mortgage Bankers Association, Commercial/Multifamily Delinquency Rates Decline in Q2, September 4, 2013.

or unable to meet all of the rental housing industry's capital needs. Please see Appendix I for a complete overview of multifamily mortgage financing sources.

Banks are limited by capital requirements and have rarely been a source of long-term financing. Life insurance companies have typically comprised less than 10 percent of the market, lend primarily to newer, high-end properties and enter and exit the multifamily market based on their investment needs and economic conditions. FHA has insufficient capacity. The private-label CMBS market will be an important capital source, but because of the stricter regulatory environment post-financial crisis, it is unlikely to return to the volume it reached pre-crisis.

The apartment industry is encouraged by the thawing in the private capital markets but is unconvinced by the claims of some private capital providers that they can fully replace the liquidity offered by the GSEs. Already in this recovery, we are seeing the historical pattern of uneven access to capital repeat itself. The new private capital coming into the apartment sector is concentrating in a handful of cities and on trophy assets.

Apartment firms providing critical housing in secondary and tertiary markets and rural areas are not benefiting from the resurgence in private capital. Even in the larger markets, firms providing workforce housing find themselves equally shut out. The Enterprises are a truly national source of multifamily mortgage debt. In that regard they maintain a flow of liquidity at the local, regional and national markets to complement private multifamily mortgage capital availability not control it.

Finally, the Enterprises, unlike many other commercial real estate debt sources, help finance subsidized rental housing, including Low-Income Housing Tax Credit and Section 8 Project-Based rental properties, as well as senior and assisted living housing.

Response to Specific FHFA Questions

Overall, NMHC/NAA are extremely concerned by FHFA's efforts to further reduce Fannie Mae and Freddie Mac's multifamily businesses. As indicated in the FHFA's August 9 Notice, the agency has already instituted a 10 percent volume reduction in 2013 through a combination of increased pricing, more limited product offerings and stronger underwriting standards. Taking additional actions as proposed could disrupt the market and impact the apartment industry's ability to meet America's housing needs. Absent evidence of increased credit risk, there is much to lose and nothing to gain.

We offer the following comments relative to the strategies FHFA has identified to further contract the Enterprises' multifamily businesses.

I. Loan Terms

FHFA has asked whether shorter-term mortgages, under 10 years, should be eliminated. It is vital that the Enterprises maintain their ability to offer financing with loan terms from five to 30 years. While it is true that the Enterprises have made fewer of these in 2012, it is flawed logic to assume that they are no longer necessary. Historically, the Enterprises offered short-term debt products as a hedge against higher long-term rates.

In higher interest rate environments, short-term mortgages benefit borrowers who need lower rates to produce the cash flow necessary for operations and debt service. Fannie Mae began to offer a seven-year term in the mid-to-late 1980s because of the interest rate environment at the time. Demand for short-term mortgages in the mid-to-late 1980s and early 1990s was driven by the fact that interest rates for mortgage loans with terms of 10 or more years exceeded 10 percent. When Freddie Mac re-entered the market in 1992, it offered a five-year term to assist borrowers to re-balance high-interest rate debt in their portfolios and to incentivize the refinancing of poor-performing loans.

In other words, the Enterprises' share of short-term mortgage debt is a function of the yield curve; recent reductions are due to limited demand during this time of historically low interest rates. Moreover, the banks have become very active through aggressive pricing and terms, but this is a result of competition among financial institutions not competition between financial institutions and the Enterprises or life insurance companies. The Enterprises' influence on short-term lending in this market environment is minimal.

We offer the following additional observations regarding the pernicious effects and unintended consequences that could result from artificially constraining available multifamily mortgage loan terms:

- **Secondary and Smaller Markets Disadvantaged**
  If FHFA chooses to eliminate the Enterprises' ability to offer five- and seven-year loans, it will disadvantage apartment owners in smaller and secondary markets where commercial banks are not as active. Even if they were willing, many local community and commercial banks simply lack the lending capacity to fully serve this market. FHFA must not overlook the fact that the Enterprises provide added liquidity in these communities, which benefits the residents of affordable rental housing.

- **Loans to Smaller Rental Properties Threatened**
  Owners of smaller properties, for a variety of reasons, often seek shorter-term loans. If FHFA chooses to eliminate five- and seven-year loans, it weakens the apartment industry's ability to serve the needs of smaller rental properties. Expanding liquidity to small multifamily properties is a long-established policy goal of the Enterprises.

- **Greater Regulatory Role for FHFA Necessary to Implement Proposal**
  Eliminating short-term financing options will force greater regulatory oversight because FHFA will need to monitor short-term debt markets and local bank lending activities, as well as forecast interest rates, to manage credit risk. This may not seem like a high-risk position for FHFA, but this requires active management of the Enterprises' loan activities and close observation of a market that has limits on transparency.

NMHC/NAA recommend that prior to taking any action to restrict loan terms, FHFA first undertake a comprehensive assessment of the likely impact of the proposal. It should produce a study of short-term bank, insurance company and Enterprise multifamily mortgage lending and then consider how eliminating certain Enterprise loans would impact the availability and liquidity of multifamily mortgage capital.

II. Variety of Loan Products

NMHC/NAA are extremely concerned about the prospect of limiting the variety of loan products that Fannie Mae and Freddie Mac currently offer to multifamily borrowers. The notion that limits should be placed on loan products implies FHFA does not understand the commercial and multifamily mortgage market and the Enterprises' role in the financing of multifamily properties. We offer the following in response to this strategy:

- **Market Liquidity**
  FHFA implies that the variety of products and financing options that the Enterprises currently offer represent a liability to the debt markets. In contrast, NMHC/NAA strongly believe that this range of products and financing options is critical to maintaining liquidity in all markets at all times. The Enterprises do not engage in credit lending such as single-family, residential mortgage lending. Rather, they lend to businesses that are collateralized by real estate and receive cash flow from rents. While loans may be customized to meet borrower needs, the underwriting, due diligence and legal structure are the same for every borrower. As stated earlier, the Enterprises fill gaps and voids; they offer competition and backstop markets and debt sources. Without their range of products, liquidity in the apartment sector would not be as strong, financing costs would be higher, real estate values would be lower and rents would be higher.

- **Standardization**
  Although the Enterprises may offer a wide variety of loan products, they have also been market leaders when it comes to managing those products and establishing standards to make multifamily mortgage markets extraordinarily efficient. The Enterprises have created uniform mortgage instruments in all 50 states and established a network of originators and servicers that have a strong alignment of interest and understanding of the marketplace. The Enterprises' lender agreements and requirements (i.e., Freddie Mac Multifamily Seller/Servicer Guide and Fannie Mae Multifamily Delegated Underwriting and Servicing Guide) have led the market and set standards for a variety of lenders. In fact, FHA relied on the Enterprises when it updated its loan closing legal documents in 2011.

  The Enterprises have also been a market leader when it comes to addressing investments necessary to preserve and improve properties and prevent further declines in rental income. They have created the standards used by most lenders regarding managing property and environmental risks such as including asbestos, lead-based paint, earthquakes and floods.

- **One-Size-Fits-All Approach Dangerous**
  Underwriting market risk factors requires a range of mortgage products, especially in concentrated markets (e.g., factory, military and workforce) and properties serving market niches (e.g., college and university rental housing and seniors and assisted living communities). Limiting mortgage products may benefit some lenders to the multifamily industry, but FHFA must consider the impact of such action on the rental-housing provider and, most importantly, the rental household.

  Critically, FHFA is likely to find itself in an adverse selection position should it choose to limit products and product flexibility. FHA has a single-size product. As such, FHA has limited ways to manage credit risk. It tends to cater to less-experienced and higher-leveraged owners. By limiting product offerings, FHFA could well be increasing risk in the Enterprises' guaranteed portfolios.

NMHC/NAA caution FHFA against limiting product offerings and instead encourage the agency to maintain its oversight of credit risk and capital requirements. The Enterprises have demonstrated exceptional credit discipline while meeting the needs of a nationwide multifamily market. They engage private capital through investors and guarantors, and they are effective and efficient in their loan application processing. Furthermore, they have been steady and steadfast in their support for apartment providers. Banks, thrifts, life companies, pension funds, Wall Street conduits and mortgage companies serve the interests of a $15 trillion commercial real estate market, of which the multifamily segment represents a small piece. To assume that these debt providers will replace products the Enterprises are prohibited from offering is imprudent and could have disastrous consequences to the marketplace and America's renters.

III. Limits on Property Financing

NMHC/NAA have concerns that FHFA's proposal to change what properties are eligible for Enterprise financing would have serious unintended consequences detailed below. Furthermore, given that Congress is currently debating housing finance reform and specifically examining this issue, future action should be left to elected policymakers. Accordingly, we urge a stay of any such action at this time.

Specifically, NMHC/NAA take exception with the following points outlined in FHFA's August 2013 Notice.

- ***"The properties with the highest market rents are affordable only to upper income households and these loans often have high balances on a per-unit basis."***

  This statement does not take into consideration many essential factors. Many properties that are considered "luxury" or "high-rent" built in the past 10 to 20 years are likely to include units for more moderate-income households and are part of the fabric of rental housing in a community. Additionally, FHFA fails to define "upper-income" household. Is that a household above the area median income? Is it a household in a rent-controlled and confined rental market?

- ***"In the past, statutory per unit limits constrained the Enterprises from providing high balance loans to multifamily properties."***

  This claim appears to be misleading. In the mid-1990s, Congress eliminated statutory per-unit limits. Lawmakers viewed per-unit limits as irrelevant due to the fact that there was limited new construction taking place and financing needs were much lower. As the economy grew and the demand for rental housing increased in the later part of the decade (1995-1999) and throughout the first part of the new century (2000-2010), land, entitlement, construction labor and material costs increased. High-end properties are not the only ones with significant per-unit loan costs. It is also very expensive to reinvest and reposition older rental properties, most of which serve the workforce housing market. The cost to construct affordable rental housing in core markets can be $300,000 to $450,000 per unit – the same cost for "luxury" rental properties.

- ***"More recently, participation in this segment of the multifamily market has contributed to a substantial increase in the average size of Fannie Mae and Freddie Mac multifamily loans."***

    This statement falsely presumes a linkage between loan size and credit risk. While NMHC/NAA certainly agree that loan exposure should be assessed and that larger loans can create greater liabilities in the aggregate, there is not a direct relationship between credit risk and loan size. In fact, in many cases, the opposite is at play. Larger loans are most likely to be made in top locations where rental demand is the strongest. Furthermore, developers receiving such loans are likely to be experienced operators who often carry less leverage, thereby placing more equity at risk than other borrowers. As such, the large loan does not present a high credit risk profile. For these reasons, large loans, in some cases, are a hedge against more risky, but smaller loans.

FHFA has the responsibility of balancing credit risk and affordable housing goals. In establishing the Enterprises' multifamily affordable housing goals for 2015 and beyond, FHFA must consider the multifamily guaranteed portfolio's health and quality. Placing limits on property financing is likely to weaken the credit quality of the guaranteed multifamily mortgage portfolio. The resulting increase in credit risk will reduce the Enterprises' ability to be active debt providers to targeted, higher-leverage affordable properties, paradoxically limiting FHFA's capacity to set goals to achieve greater affordable housing lending.

NMHC/NAA consider per-unit mortgage limits to be arbitrary and believe they will create more problems than they solve. Such limits constrain the availability of debt to finance rehabilitation and future investments in key components through replacement reserves. Notably, in 2009, when FHA sought to accommodate the apartment industry's refinancing needs, it implemented artificial adjustments to the per-unit mortgage calculation by eliminating the land value from the formula specifically to allow higher mortgage amounts to be financed. This formula remains in use today, and performance has not suffered. Furthermore, FHA uses adjustments for costs not attributable to the loan to finalize the per-unit mortgage calculation (NMHC/NAA offer the HUD 92264-A form as Appendix II to illustrate the calculation). If FHFA were to implement a per-unit mortgage limit with regard to Fannie Mae and Freddie Mac loans, it would face similar calculation issues and would likely have to develop a convoluted formula similar to the one FHA employs. Moreover, FHFA would have to undertake careful auditing to ensure proper implementation.

NMHC/NAA, in response to Questions 3 (a), (b) and (c), emphatically oppose setting per-unit mortgage loan limits or limits on transactions. We support the current process of evaluating the Enterprises' lending activities on a portfolio basis. Finally, we once again advise FHFA to allow Congress to set policy on this issue as part of its efforts to reform housing finance.

IV. Limits on Business Activities

FHFA's options regarding placing limits on the Enterprises' business activities are best analyzed through the prism of reducing credit risk. Rather than asking whether certain business activities should be restricted on the grounds that alternative sources of capital could take their place, a premise we challenge, FHFA's role as a regulator is to instead ask whether these business activities generate undue risk to the taxpayer. The answer is no.

The Enterprises have great capacity to add liquidity to the marketplace and assist private capital sources through structured transactions. They also have a significant impact on the preservation of existing rental housing through pool-based transactions that allow cross collateralized and substitution transactions at the portfolio level. It takes the experience and sophistication that has been developed over the past 23 years to provide this level of expertise to support the apartment sector.

NMHC/NAA strongly support the migration of the Enterprises' multifamily activities from their balance sheets to a securitized portfolio. The insertion of private capital through subordinated bonds is vital to protect taxpayers. That said, NMHC/NAA also favor enabling the Enterprises to retain a small portion of mortgage investments to facilitate mortgage aggregation for securitization and support unique transactions that may represent prudent mortgage purchases but have added credit risk.

Finally, while securitization makes sense as a general principal, multifamily mortgage securities, be they single-loan or pooled securities, single-class or multiple-class with subordinated investors, can make it more difficult to manage mortgage risk. Securitized loans cannot be amended or modified without express permission from the bond investors. Therefore, working out issues prior to mortgage default becomes impossible when a property financed by a securitized loan faces difficulties. For this reason, the Enterprises should have the ability to hold in their mortgage investment portfolio a small number of loans that may ultimately need to be modified over the course of the mortgage term.

Conclusion

We appreciate that FHFA has provided stakeholders with an opportunity to comment on the strategies the agency is considering. We look forward to working with FHFA to reduce the Enterprises' already low risk exposure and encourage the increased participation of private capital in multifamily housing finance. However, given the fact that private debt capital providers are already significantly increasing their role in multifamily finance, and the Enterprises' market share is already decreasing, it hardly seems appropriate to impose arbitrary and artificial limitations that could disrupt the positive market forces currently at work. The multifamily Enterprises operated exactly as designed. The GSEs backstopped the market when private capital was unavailable during the great recession, and their market share today is significantly lower during this time of abundant multifamily mortgage debt.

On behalf of the providers of rental housing, NMHC/NAA respectfully request that FHFA not impose further constraints on the Enterprises' mortgage activities. Our members who own and operate multifamily rental properties, with and without loans financed by Enterprise debt, are appropriately concerned by the options currently under consideration. They will have serious consequences for all borrowers, not just GSE borrowers. Clearly, the apartment industry stands behind any effort to ensure liquid debt markets, seeks additional private debt capital participation in the market and awaits the return of the CMBS market. However, placing additional caps on the GSEs' multifamily lending volume and reducing the diversity and availability of multifamily mortgage products, particularly while Congress is in the midst of deliberating on the future of the housing finance system, will only lead to market uncertainty and instability. For this reason, we cannot support any further actions to restrict liquidity to our industry and to the residents we serve.

Any questions on our comments can be directed to David Cardwell, NMHC Vice President of Capital Markets, at 202/974-2336 or dcardwell@nmhc.org.

Sincerely,

Douglas M. Bibby
President
National Multi Housing Council

Douglas S. Culkin, CAE
President
National Apartment Association

CAPITAL FLOWS TO THE MULTIFAMILY INDUSTRY

Historically, the apartment industry has relied on a variety of capital sources, each with its own focus, strengths and limitations, to meet its liquidity needs. They include:

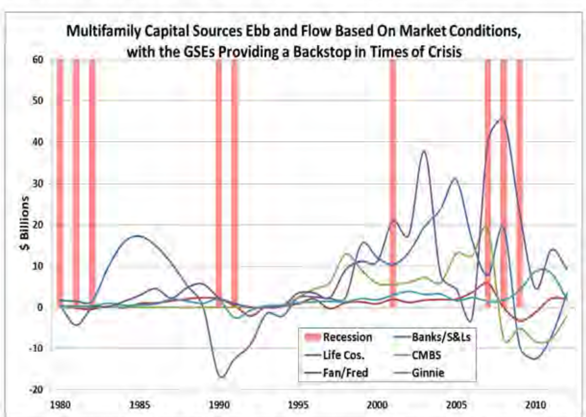
- Fannie Mae and Freddie Mac
- Commercial Banks
- Life Insurance Companies
- Federal Housing Administration
- Commercial Mortgage-Backed Securities (CMBS)/Conduits

Together, these capital sources have provided the apartment sector with $100 billion to $150 billion annually, reaching as high as $225 billion last decade, to develop, refinance, purchase, renovate and preserve apartment properties.

Fannie Mae/Freddie Mac: A Critical Liquidity Backstop in All Markets and All Economic Cycles

- The Government Sponsored Enterprises (GSEs) Fannie Mae and Freddie Mac have served as the cornerstone of the multifamily housing finance system in the modern era, successfully attracting private capital to the sector. Unlike any other single source of capital, they offer long-term debt for the entire range of apartment properties (market-rate workforce housing and subsidized properties, large properties, small properties, etc.), and they are active in all markets (primary, secondary and tertiary).

- As the chart below shows, the GSEs' multifamily programs has served as a backstop to the sector, increasing at times of market dislocation when other capital sources leave, and retreating as private capital returned to the market. This was seen most recently during the 2008 financial crisis, when all private capital left the market. As a result of that crisis-driven expansion, they currently hold 35 percent of the outstanding multifamily mortgage debt. Between 1990 and 2010, they accounted for 42 percent ($241.3 billion) of the net increase in mortgage debt.



Source: Federal Reserve, Natl. Bureau of Economic Research; NMHC

Commercial Banks: Short-term Financing for Smaller, Local Borrowers

- Commercial banks and thrifts generally serve as a source of credit for smaller, local borrowers. They typically provide floating rate, short-term debt, and often their willingness to extend this credit is based on the availability of permanent take-out financing offered by the GSEs.

- They currently hold 30 percent of outstanding multifamily mortgage debt. Between 1990 and 2010, they provided 23 percent ($131.0 billion) of the total net increase in mortgage debt. They have provided limited amounts of capital to the industry since the financial crisis and are unlikely to return to their pre-crisis levels because of higher risk-based capital requirements and new FASB accounting standards which impose meaningful limits on the ability of banks to provide capital to commercial real estate.

Life Insurance Companies: Target High-Quality Properties, Capital Allocations Change with the Market

- Life insurance companies tend to restrict their lending to a handful of primary markets and to high-quality, newer construction apartment properties. They do not generally finance affordable apartments, and their loan terms typically do not extend beyond 10 years. Importantly, they enter and exit the multifamily market based on their investment needs and economic conditions. On average, they have generally provided 10 percent or less of the annual capital needed by the multifamily industry, but that number has gone as low as 3 percent.

- They currently hold just 6 percent of outstanding multifamily mortgage debt. Between 1990 and 2010, they accounted for just 3 percent ($18.3 billion) of the net increase in multifamily mortgage debt.

FHA: Reliable Capital Source but Limited Mortgage Products and Capacity Issues

- FHA offers high-leverage, long-term mortgages with 35-year terms and 80 percent to 83 percent loan-to-value ratio. The capital they provide largely targets construction lending.

- After the 2008 financial collapse, they became a vital source of construction capital for apartments, and now FHA/Ginnie Mae currently hold 9 percent of outstanding multifamily mortgage debt. Between 1990 and 2010, they accounted for 7.0 percent ($40.1 billion) of the total net increase in mortgage debt.

- Capacity issues, long processing times and statutory loan limit requirements prevent FHA from serving a larger share of the multifamily market. They are also in the process of implementing more stringent underwriting and loan documents to reduce, not expand, the number of loans they will fund.

CMBS/Conduits: Volatile Capital Source

- The CMBS market did not become a material source of capital to the apartment industry until the mid-1990s, peaking at 16.5 percent of the market ($17.6 billion a year) in the housing bubble years of 2005-2007.

- The CMBS market completely shut down after the 2008 crisis. While it shows some signs of rebounding, regulatory changes imposed by financial regulatory reform legislation will mean that it will not return to its pre-bubble levels of lending.

- The CMBS market now holds 8 percent of the outstanding multifamily mortgage debt, although many of these loans have been referred to special servicers because of the aggressive underwriting and higher leverage employed during the housing boom. Their serious delinquency rate stood as high as 17.4 percent in 2011, but has since fallen to 7.81 percent. In contrast, the GSEs' delinquency rate is less than 1 percent.

Covered Bonds: Not Viable as a Significant Multifamily Capital Provider

- Covered bonds have been used in Europe to support the residential mortgage market; however, there is no viable covered bond market in the U.S. at this time. While they may be an additional source of capital for the apartment sector, they are not a viable replacement for existing capital sources. Not only have they not demonstrated extensive capacity to serve commercial/multifamily real estate markets, they present limitations to issuers since the issuer must hold risk-based capital against potential losses as the loans are held on the balance sheet.

Supplement to Project Analysis

U.S. Department of Housing and Urban Development
Office of Housing
Federal Housing Commissioner

OMB Approval No. 2502-0029
(exp. 10/31/2012)

Section or Title Number ______________

☐ Valuation Trial ☐ Conditional ☐ Firm **See last page for Public Reporting burden statement before completing this form**

Privacy Act Notice: The United States Department of Housing and Urban Development, Federal Housing Administration, is authorized to solicit the information requested in the form by virtue of Title 12, United States Code, Section 1701 et seq., and regulations promulgated thereunder at Title 12, Code of Federal Regulations. While no assurance of confidentiality is pledged to respondents, HUD generally discloses this data only in response to a Freedom of Information Act request.

Name of Mortgagor (Borrower)	Project Number
Name of Project	
Location of Project (street, city & state)	

Type of Borrower

☐ Private ☐ Profit ☐ Public ☐ Nonprofit ☐ State or Federal Instrumentality, etc.
☐ Management Coop. ☐ Sales Coop. ☐ Investor-Sponsor ☐ Builder-Seller ☐ Limited Distribution

Type of Project

☐ Rental Housing ☐ Mobile Home Court ☐ Board and Care ☐ New Construction ☐ Non-Elevator
☐ Cooperative ☐ Nursing Home ☐ Single Rm. Occupancy ☐ Rehabilitation ☐ Elevator
☐ Condominium ☐ Intermediate Care Facility ☐ Redevelopment ☐ Existing
☐ Capital Advance 202/811 ☐ Housing for the Elderly ☐ Supplement Loan ☐ ____________

I. Determination of Maximum Insurable Mortgage

Criteria		column 1	column 2	column 3
1. **Mortgage or Loan Amount Requested in Application**				$ ______
2. **Reserved**				$ ______
3. **Amount Based on Value or Replacement Cost**				
a. Value (Replacement Cost) in Fee Simple	$ ______ X ____ %		$ 0.00	
b. (1) Value of Leased Fee	$ ______			
(2) Grant/Loan funds attributable to R. C. items	$ ______			
(3) Excess Unusual Land Improvement	$ ______			
(4) Cost Containment Mortgage Deduction	$ ______			
(5) Total lines (1) to (4)	$ 0.00 X ____ %	$ 0.00		
c. Unpaid Balance of Special Assessment		$ ______		
d. Total line b plus line c			$ 0.00	
e. Line a minus line d				$ 0.00
4. **Amount Based on Limitations Per Family Unit**				
a. Number of **no** Bedroom Units	____ X $ ______	$ 0.00		
Number of **one** Bedroom Units	____ X $ ______	$ 0.00		
Number of **two** Bedroom Units	____ X $ ______	$ 0.00		
Number of **three** Bedroom Units	____ X $ ______	$ 0.00		
Number of **four** or more Bedroom Units	____ X $ ______	$ 0.00		
b. Cost Not Attributable to Dwelling Use	$ ____ X ______ %	$ 0.00		
c. Warranted Price of Land	$ ____ X ______ %	$ 0.00		
d. Total lines a through c			$ 0.00	
e. Total Number of Spaces	____ X $ ______		$ 0.00	
f. Sum: Value of Leased Fee and Unpaid Balance of Special Assessment(s)			______	$
g. Line d or line e, whichever is applicable, minus line f			______	$
5. **Amount Based on Debt Service Ratio**				
a. Mortgage Interest Rate		______ %		
b. Mortgage Insurance Premium Rate		______ %		
c. Initial Curtail Rate		______ %		
d. Sum of Above Rates			0.00 %	
e. Net Income	$ ____ X ______ %		$ 0.00	
f. Annual Ground Rent $ ______	+ Annual Spec. Assmt. $ ______		$ 0.00	
g. Line e minus line f			$ 0.00	
h. Line g divided by line d				$ ______
i. Annual Tax Abatement Savings $ ______	divided by ______ %			$ ______
j. Line h plus line i				$ 0.00

Previous editions are obsolete

Page 1 of 4

form **HUD-92264-A** (03/2010)
ref Handbooks 4480.1 & 4470.1

I. Determination of Maximum Insurable Mortgage (cont.)

Criteria	column 1	column 2	column 3
6. Amount Based on Estimated Cost of Rehabilitation Plus (i) "As Is" Value, **or** (ii) Acquisition Cost, **or** (iii) Existing Mortgage Indebtedness Against the Property Before Rehabilitation:			
a. Total Estimated Development Cost	$ ________		
b. Estimated Cost of Off-Site C onstruction	$ ________		
c. Sum of lines a & b		$ 0.00	
d. Grant/Loan funds attributable to R. C. items	$ ________		
e. Line c minus line d		$ ________	
f. "As Is" Value of Prop. Before Rehab. $ ________ X ________ %	$ ________		
g. Existing Mortgage Indebtedness (Property Owned) **or** Purchase Price of Property (to be Acquired)	$ ________		
h. Line e plus line f **or** line g, whichever is less		$ ________	
i. Line h X ______ %			$ ________
7. Amount Based on Borrower's Total Cost of Acquisition Section 223(f)			
a. Purchase Price of Project	$ ________		
b. Repairs and Improvements, if any	$ ________		
c. Other fees	$ ________		
d. Loan Closing Charges *	$ ________		
e. Sum of lines a through d		$ 0.00	
f. Enter the Sum of any Grant/Loan and Reserves for Replacement and Major Movable Equipment to be purchased as an asset of the project		$ ________	
g. Line e minus line f		$ ________	
h. Line g X ______ %			$ ________
8. Amount Based on Sum of Unit Mortgage Amounts			$ ________
9. Amount Based on Estimated Cost to Borrower			
a. Total Estimated Cost **(Exclusive of Site and Required Construction Off the Site)**	$ ________		
b. Purchase Price of Site	$ ________		
c. Total Cost of Clearing Site, if any	$ ________		
d. Expense of Relocating Occupants, if any	$ ________		
e. Cost of Off-Site Construction, if any	$ ________		
f. Sum of line a through line e		$ 0.00	
g. Line f X ______ %			$ ________
10. Amount Based on Existing Indebtedness, Repairs, and Loan Closing Charges Section 223(f)			
a. Total Existing Indebtedness	$ ________		
b. Required Repairs	$ ________		
c. Other Fees	$ ________		
d. Loan Closing Charges *	$ ________		
e. Sum of line a through line d		$ 0.00	
f. Enter the Sum of any Grant/Loan and Reserves for Replacement and Major Movable Equipment on Deposit		$ ________	
g. Line e minus line f		$ ________	
h. 80% of Value $ ________ X80%		$ ________	
i. Greater of line g or line h			$ ________

11. Amount Based on Deduction of Grant(s), Loan(s), Tax Credit(s) and Gift(s) for Mortgageable items:

a. 100% Project (Replacement) Cost *	$ ________	
b. (1) Grants/loans/gifts	$ ________	
(2) Tax Credits	$ ________	
(3) Value of Leased Fee	$ ________	
(4) Excess Unusual Land Improvement Cost	$ ________	
(5) Cost Containment Mtge Deduction	$ ________	
(6) Unpaid Balance of Special Assessment	$ ________	
(7) Sum of Lines (1) through (6)		$ 0.00
c. Line a. minus line b. (7)		$ ________

* Project Cost applies to Criteria 7 and 10 under Section 223 (f) and applications pursuant to 223(f). Project Replacement Cost applies to Section 221 (d) and other Sections of the Act mortgages limited by Replacement Cost.

* Attach format for computing loan closing charges.

Maximum Insurable Mortgage (Lowest of the Foregoing Criteria) $

Previous editions are obsolete

form **HUD-92264-A** (03/2010)
ref Handbooks 4480.1 & 4470.1

Fannie Mae Asset Quality 1971-2012

End of Period	Mortgage Asset Quality				
	Single-Family Serious Delinquency Rate[a] (%)	Multifamily Serious Delinquency Rate[b] (%)	Credit Losses as a Proportion of the Guarantee Book of Business[c, d] (%)	Real Estate Owned as a Proportion of the Guarantee Book of Business[d] (%)	Credit-Enhanced Outstanding as a Proportion of the Guarantee Book of Business[e] (%)
4Q12	3.29	0.24	0.48	0.35	18.8
3Q12	3.41	0.28	0.46	0.34	18.5
2Q12	3.53	0.29	0.50	0.34	18.3
1Q12	3.67	0.37	0.67	0.35	18.3
Annual Data					
2012	3.29	0.24	0.48	0.35	18.8
2011	3.91	0.59	0.61	0.37	18.4
2010	4.48	0.71	0.77	0.53	19.1
2009	5.38	0.63	0.45	0.30	21.2
2008	2.42	0.30	0.23	0.23	23.9
2007	0.98	0.08	0.05	0.13	23.7
2006	0.65	0.08	0.02	0.09	22.3
2005	0.79	0.32	0.01	0.08	21.8
2004	0.63	0.11	0.01	0.07	20.5
2003	0.60	0.29	0.01	0.06	22.6
2002	0.57	0.08	0.01	0.05	26.8
2001	0.55	0.27	0.01	0.04	34.2
2000	0.45	0.07	0.01	0.05	40.4
1999	0.47	0.11	0.01	0.06	20.9
1998	0.56	0.23	0.03	0.08	17.5
1997	0.62	0.37	0.04	0.10	12.8
1996	0.58	0.68	0.05	0.11	10.5
1995	0.56	0.81	0.05	0.08	10.6
1994	0.47	1.21	0.06	0.10	10.2
1993	0.48	2.34	0.04	0.10	10.6
1992	0.53	2.65	0.04	0.09	15.6
1991	0.64	3.62	0.04	0.07	22.0
1990	0.58	1.70	0.06	0.09	25.9
1989	0.69	3.20	0.07	0.14	Not Available Before 1990
1988	0.88	6.60	0.11	0.15	
1987	1.12	Not Available Before 1988	0.11	0.18	
1986	1.38		0.12	0.22	
1985	1.48		0.13	0.32	
1984	1.65		0.09	0.33	
1983	1.49		0.05	0.35	
1982	1.41		0.01	0.20	
1981	0.96		0.01	0.13	
1980	0.90		0.01	0.09	
1979	0.56		0.02	0.11	
1978	0.55		0.02	0.18	
1977	0.46		0.02	0.26	
1976	1.58		0.03	0.27	
1975	0.56		0.03	0.51	
1974	0.51		0.02	0.52	
1973	Not Available Before 1974		0.00	0.61	
1972			0.02	0.98	
1971			0.01	0.59	

Source: Fannie Mae

[a] Single-family loans are seriously delinquent when the loans are 90 days or more past due or in the foreclosure process. Rate is calculated using the number of conventional single-family loans owned and backing Fannie Mae mortgage-backed securities (MBS). Includes loans referred to foreclosure proceedings but not yet foreclosed. Before 1998, data included all seriously delinquent loans for which Fannie Mae had primary risk of loss. Beginning with 1998, data include all seriously delinquent conventional loans owned and backing Fannie Mae MBS with and without primary mortgage insurance or credit enhancement. Data before 1992 include loans and securities in relief or bankruptcy, even if the loans were less than 90 days delinquent, calculated based on number of loans.

[b] Before 1998, data include multifamily loans for which Fannie Mae had primary risk of loss. Beginning in 1998, data include all multifamily loans and securities 60 days or more past due. Beginning in 2002, rate is calculated using the unpaid principal balance of multifamily loans owned by Fannie Mae or underlying Fannie Mae guaranteed securities as the denominator. For the period 1998 to 2001, the denominator also includes other credit enhancements Fannie Mae provides on multifamily mortgage assets and multifamily non-Fannie Mae mortgage-related securities held for investment.

[c] Credit losses are charge-offs, net of recoveries and foreclosed property expense (income). Average balances used to calculate ratios subsequent to 1994. Quarterly data are annualized. Beginning in 2005, credit losses exclude the impact of fair-value losses of credit impaired loans acquired from MBS trusts. Beginning in 2008, credit losses also exclude the effect of HomeSaver Advance program fair-value losses.

[d] Guarantee book of business refers to the sum of the unpaid principal balance of mortgage loans held as investments, Fannie Mae MBS held as investments, Fannie Mae MBS held by third parties, and other credit enhancements Fannie Mae provides on mortgage assets. It excludes non-Fannie Mae mortgage-related securities held for investment that Fannie Mae does not guarantee. Before 2005, the ratio was based on the mortgage credit book of business, which consists of the guarantee book of business plus non-Fannie Mae mortgage-related securities held as investments not guaranteed by Fannie Mae.

[e] Beginning in 2000, the credit-enhanced category was expanded to include loans with primary mortgage insurance. Amounts for periods before 2000 reflect the proportion of assets held for investment with additional recourse from a third party to accept some or all of the expected losses on defaulted mortgages.

Freddie Mac Asset Quality 1974-2012

End of Period	Mortgage Asset Quality				
	Single-Family Delinquency Rate[a] (%)	Multifamily Delinquency Rate[b] (%)	Credit Losses/Average Total Mortgage Portfolio[c] (%)	REO/Total Mortgage Portfolio[d] (%)	Credit-Enhanced[e]/ Total Mortgage Portfolio[d] (%)
4Q12	3.25	0.19	0.54	0.24	13.0
3Q12	3.37	0.27	0.65	0.25	13.0
2Q12	3.45	0.27	0.63	0.26	13.0
1Q12	3.51	0.23	0.74	0.29	13.0
Annual Data					
2012	3.25	0.19	0.64	0.24	13.0
2011	3.58	0.22	0.68	0.30	14.0
2010	3.84	0.26	0.72	0.36	15.0
2009	3.98	0.20	0.41	0.23	16.0
2008	1.83	0.05	0.20	0.17	18.0
2007	0.65	0.02	0.03	0.08	17.0
2006	0.42	0.06	0.01	0.04	16.0
2005	0.53	0.00	0.01	0.04	17.0
2004	0.73	0.06	0.01	0.05	19.0
2003	0.86	0.05	0.01	0.06	21.0
2002	0.77	0.13	0.01	0.05	27.4
2001	0.62	0.15	0.01	0.04	34.7
2000	0.49	0.04	0.01	0.04	31.8
1999	0.39	0.14	0.02	0.05	29.9
1998	0.50	0.37	0.04	0.08	27.3
1997	0.55	0.96	0.08	0.11	15.9
1996	0.58	1.96	0.10	0.13	10.0
1995	0.60	2.88	0.11	0.14	9.7
1994	0.55	3.79	0.08	0.18	7.2
1993	0.61	5.92	0.11	0.16	5.3
1992	0.64	6.81	0.09	0.12	Not Available Before 1993
1991	0.61	5.42	0.08	0.14	
1990	0.45	2.63	0.08	0.12	
1989	0.38	2.53	0.08	0.09	
1988	0.36	2.24	0.07	0.09	
1987	0.36	1.49	0.07	0.08	
1986	0.42	1.07	Not Available Before 1987	0.07	
1985	0.42	0.63		0.10	
1984	0.46	0.42		0.15	
1983	0.47	0.58		0.15	
1982	0.54	1.04		0.12	
1981	0.61	Not Available Before 1982		0.07	
1980	0.44			0.04	
1979	0.31			0.02	
1978	0.21			0.02	
1977	Not Available Before 1978			0.03	
1976				0.04	
1975				0.03	
1974				0.02	

Source: Freddie Mac

[a] Based on the number of mortgages 90 days or more delinquent or in foreclosure. Excludes modified loans if the borrower is less than 90 days past due under the modified terms. Rates are based on loans in the single-family credit guarantee portfolio, which excludes that portion of Freddie Mac real estate mortgage investment conduits (REMICs) and other structured securities backed by Ginnie Mae mortgage-backed securities (MBS). Rates for years 2005 and 2007 also exclude other guarantee transactions. Single-family delinquency rates for 2008 through 2012 include other guarantee transactions.

[b] Before 2008, rates were based on the net carrying value of mortgages 60 days or more delinquent or in foreclosure and exclude other guarantee transactions. Beginning in 2008, rates were based on the unpaid principal balance of loans 60 days or more delinquent or in foreclosure and include

[c] Credit losses equal to real estate owned operations expense (income) plus net charge-offs and exclude other market-based valuation losses. Calculated as credit losses divided by the average balance of mortgage loans in the total mortgage portfolio, excluding non-Freddie Mac MBS and the portion of REMICs and other structured securities backed by Ginnie Mae MBS.

[d] Calculated based on the balance of mortgage loans in the total mortgage portfolio excluding non-Freddie Mac MBS and the portion of REMICS and other structured securities backed by Ginnie Mae certificates.

[e] Includes loans with a portion of the primary default risk retained by the lender or a third party who pledged collateral or agreed to accept losses on loans that default. In many cases, the lender's or third party's risk is limited to a specific level of losses at the time the credit enhancement becomes

PREPARED STATEMENT OF E.J. BURKE

EXECUTIVE VICE PRESIDENT AND GROUP HEAD, KEYBANK REAL ESTATE CAPITAL, KEY CORPORATE BANK, ON BEHALF OF THE MORTGAGE BANKERS ASSOCIATION

OCTOBER 9, 2013

Introduction

Chairman Johnson, Ranking Member Crapo, and Members of the Senate Banking Committee, thank you for the opportunity to testify on behalf of the Mortgage Bankers Association. My name is E.J. Burke, and I am Chairman-Elect of MBA, as well as Executive Vice President and Group Head of KeyBank Real Estate Capital. I oversee multiple commercial real estate lending platforms for KeyBank, NA in its commercial and multifamily real estate finance business, including construction and development lending, portfolio lending, community development lending, commercial mortgage-backed securitization, life company placement, FHA multifamily programs, and Fannie Mae and Freddie Mac multifamily lending. I have over 34 years of experience in banking and commercial real estate finance. KeyBank, NA is a $91 Billion regional bank that is headquartered in Cleveland, Ohio. KeyBank, NA provides community banking services in 14 U.S. States and corporate banking services nationwide. KeyBank Real Estate Capital is a national commercial real estate lender and commercial loan servicer.

Today's hearing serves as a catalyst to underscore the importance of multifamily rental housing. With Fannie Mae and Freddie Mac having been in conservatorship for more than 5 years, it is imperative that policy makers define a long-term plan for the future role of the Federal Government in the mortgage market. This plan must fundamentally include their unique role in multifamily rental housing. I commend the Chairman and Ranking Member for your leadership toward this end. We look forward to working with the Committee to help shape a vibrant rental housing market that builds upon the foundation that exists today.

As this Committee considers the essential elements of the multifamily housing finance system, we believe that policy makers should focus on ensuring that capital continues to be available in all market cycles. With this in mind, the policy discussion on the role of private capital and that of the Federal Government, in our view, is not mutually exclusive in character. We believe that public policy can strike a durable balance that continues to attract and deploy private capital in the multifamily market, while establishing a focused Government guarantee that enables liquidity and stability in all cycles—a role that only the Government can fulfill. This, in turn, will protect taxpayers and strengthen the financing system for rental housing.

These goals can be accomplished by building upon the strong foundation that currently exists in multifamily finance—where there is greater and increasing diversification in capital sources for multifamily housing, where private capital bears significant risk in existing multifamily finance platforms, and where Government-backed sources have experienced, even through the recent financial crisis, very strong credit performance. [1]

My testimony begins with an overview of the multifamily housing market and capital sources, including the GSEs, that support this market.

I then discuss overarching policy principles that we believe should guide the future of multifamily housing finance.

Based on these principles, I recommend a system that would strengthen multifamily housing finance, while providing commentary on current legislative approaches.

I conclude my testimony by emphasizing the importance of ensuring a stable transition and careful stewardship of taxpayer assets, in order to provide greater flexibility for Congress as it frames the regime that will govern the housing finance market.

Overview of the Multifamily Housing Market

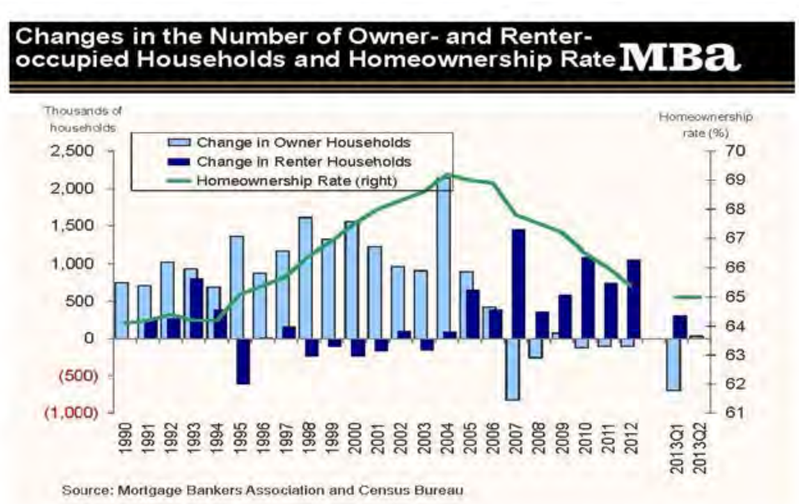
Importance of Multifamily Rental Housing

More than one in three American households rent their home, and more than 16 million of those households live in multifamily rental housing, a development with five or more units. The multifamily rental housing market is a critical component of our housing system—in size, reach and the households that it serves. Renters include workers who want to live near their jobs, young professionals, empty-nesters,

[1] For example, both GSE multifamily businesses have been profitable and have been prudent in their lending practices, as reflected in their current credit performance with less than a 20 basis point delinquency rate.

retirees on a fixed income, families with children, students, and households who value the convenience and mobility that renting offers. The vast majority of multifamily rental housing provides homes for households earning modest incomes, with 93 percent of multifamily rental apartments having rents affordable to households earning at or below the area median income. Overall, renters' median household income is about half of that of homeowners.[2]

The share of households renting their homes has risen to 35 percent from a low of 31 percent in 2004. And since the end of 2006, the number of renter households has increased by five million, while the number of owner-occupied households has declined by 1.5 million.



The number of renter households is expected to continue to increase substantially over the next decade. Harvard's Joint Center for Housing Studies "estimates that the number of renter households could increase by 360,000–470,000 annually between 2010 and 2020, in line with growth over the past decade."[3] This growth in renter households will require substantial investment in multifamily housing.

The nature of financing multifamily rental housing differs from that in single-family lending in important ways. Among them, multifamily lending involves loans that have larger balances with more complex and heterogeneous properties, compared to single-family loans. Multifamily loans require a detailed underwriting process due to the fact that the repayment of the loan is dependent on the ongoing financial performance of the property, which is in turn dependent on the property's income streams, expenses, market conditions and outlook, and numerous other factors. As a result, careful underwriting is required to confirm a property's creditworthiness and the borrower's ability to successfully operate the apartment property. The origination, underwriting, securitization and investor reporting, and servicing expertise necessary to successfully finance multifamily rental properties is considerable.

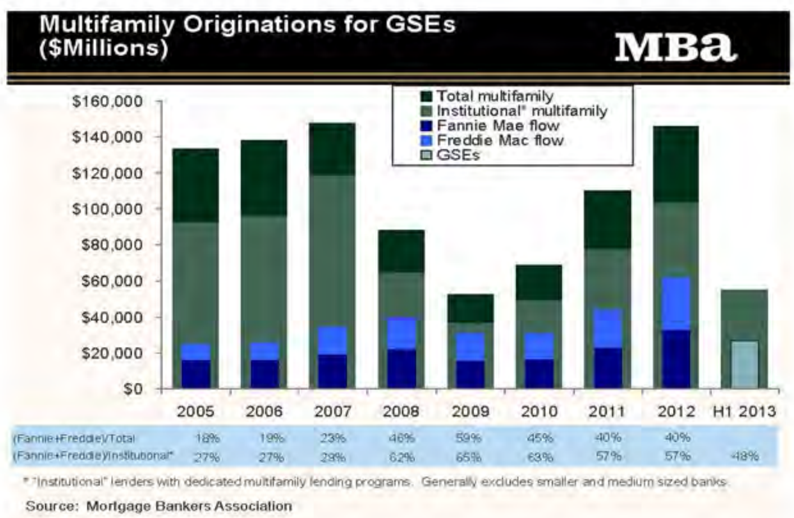
The finance market that supports multifamily rental housing is substantial and includes a range of market participants. The total amount of multifamily mortgage debt outstanding is approaching $900 billion.[4] Capital sources that finance the multifamily housing market include Fannie Mae and Freddie Mac, commercial banks, the Federal Housing Administration's (FHA) multifamily programs, life insurance companies, commercial mortgage-backed securities (CMBS) issuers, REITs, pension funds, State and local government agencies, and others. While all sources play an integral role in supporting the multifamily market, each has its own focus, strength, and limitations.

[2] Joint Center for Housing Studies, Harvard University, State of the Nation's Housing 2013.
[3] Joint Center for Housing Studies, Harvard University, State of the Nation's Housing 2011.
[4] MBA's Quarterly Analysis of Commercial and Multifamily Mortgage Debt Outstanding.

Importantly, when most private capital sources exited the multifamily finance market during the recent economic downturn, the GSEs and FHA continued to provide liquidity during this period of unprecedented market disruption.

The GSEs' Performance and Countercyclicality During Market Downturn

Let me turn to the role that Fannie Mae and Freddie Mac have recently played in the multifamily housing markets. The GSEs' role during the financial crisis demonstrates that they served a countercyclical role as providers of liquidity in the multifamily market when other sources pulled back. The GSEs' peak market share reached 59 percent of the total multifamily mortgage originations (and 85 percent of the institutional market)[5] in 2009. And since the crisis, their market share has trended downward—in 2012, 40 percent of the total multifamily market and 57 percent of the institutional market—even as overall multifamily origination volumes have increased.



As the market has stabilized, other lending sources have increased market share, with non-GSE capital sources competing vigorously with Fannie Mae and Freddie Mac to finance multifamily properties.

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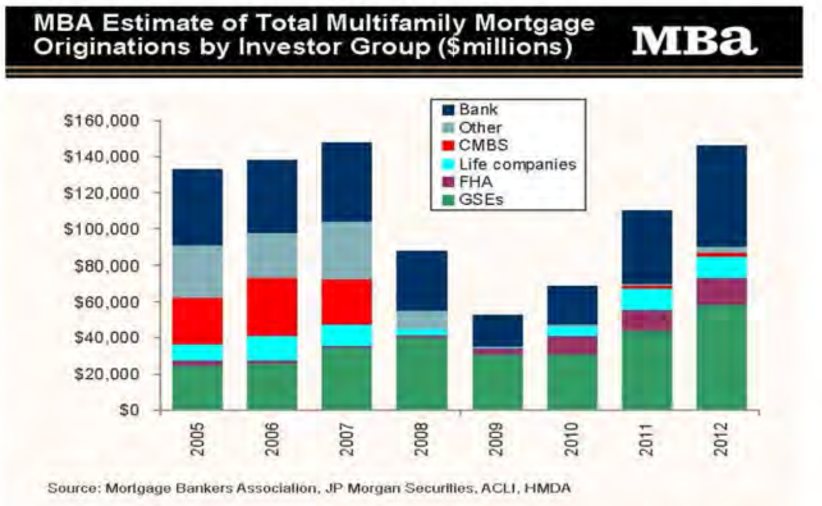
[5] MBA defines the institutional market as the part of the market served by lenders with a platform dedicated to lending to commercial and multifamily property owners.



In sum, the GSEs' multifamily businesses, their performance and role in the market are unique in many respects. As Acting FHFA Director Edward DeMarco observed in a speech earlier this year:

> Unlike the single-family credit guarantee business, the Enterprises have a smaller market share and there are other providers of credit in the multifamily market . . . Another difference from the single-family business is that each Enterprise's multifamily business has weathered the housing crisis and generated positive cash flow. In contrast to their common approach to their single-family businesses, Fannie Mae and Freddie Mac do not take the same approach to their multifamily businesses. Each approach also already embeds some type of risk sharing. For a significant portion of its business, Fannie Mae shares multifamily credit risk with loan originators through its delegated underwriting program. For a significant and increasing portion of its business, Freddie Mac shares multifamily credit risk with investors by issuing classes of securities backed by multifamily mortgages where the investor bears the credit risk. [6]

Policy Principles for Multifamily Housing Finance

Recognizing the unique attributes of the multifamily market, MBA recommends that policy makers support proposals that advance the following principles.

Our Nation's multifamily housing finance system should rely on private capital. Private capital should be the primary source of financing for multifamily rental housing. Private capital has historically been brought to bear through the range of lending institutions that have supported multifamily finance, such as portfolio lenders and CMBS issuers, the GSEs' multifamily programs that require loss sharing with originators and with investors, and the capitalization of the GSEs themselves. We believe that Government policies should maintain this reliance on private capital going forward.

Past experience shows that the Federal Government is the only entity that can ensure the availability of liquidity in all market cycles. The recent financial crisis and recession demonstrated that only the Federal Government can ensure liquidity through all market cycles, and, as demonstrated by the conservatorship of Fannie Mae and Freddie Mac, as well as programs like the Federal Reserve's asset purchases, the Federal Government will fill this role when necessary. Government policies should anticipate and prepare for this role.

The Government should ensure liquidity for multifamily mortgages through a carefully crafted guarantee on multifamily mortgage-backed securities. The Federal Government should provide a catastrophic backstop guarantee on mortgage-backed se-

[6] FHFA's Conservatorship Priorities for 2013, Remarks Prepared for Delivery by Edward J. DeMarco, Acting Director, FHFA (March 4, 2013).

curities. The catastrophic backstop role would be similar to that of the U.S. Government in a number of sectors and markets, including Federal deposit insurance in the banking system. This Government backstop should be available at the mortgage-backed securities level (rather than at the level of the issuer, as it is today with the GSEs) at all times to ensure liquidity in the multifamily finance market.

Taxpayers and the mortgage finance system itself should be protected through a strong regulatory framework and multiple layers of private capital. To protect taxpayers and the system itself, the Government guarantee-related market should be subject to strong and independent regulatory oversight and risk-based capital requirements. Taxpayers also should be protected through multiple layers of private capital, including the equity in the multifamily property itself and the entity-level capital of the security-issuing institution and any risk sharing it may undertake. As noted above, a Federal risk insurance fund should also be established, capitalized by risk-based premiums paid by participating firms. Only when all layers of capital are exhausted would a draw on the U.S. Treasury be authorized.

Policy makers should protect and preserve existing resources, as well as support greater transparency, during the transition to an overhauled housing finance system. Given the significant role of the GSEs in the multifamily market, their infrastructures, human capital, and resources should be carefully managed to avoid disruptions to the market, as well as to ensure an orderly transition to a new housing finance system. Prudent management of existing multifamily executions and mortgage portfolios is important due to its quality and positive cash flow generated—all of which are taxpayer assets.

Structural Recommendations for the Future of Multifamily Housing Finance

To implement these principles, MBA believes that a legislative solution should incorporate the following structural recommendations:

Establish a Government Guarantor. A wholly owned Government corporation should function as a catastrophic guarantor, administrator of a risk insurance fund, and regulator of secondary market entities. The Government guarantor, which would be backed by the full faith and credit of the U.S., would not be subject to the Federal appropriations process, but be funded by guarantee fees paid by issuers, as well as other statutorily defined assessments.

The Government corporation would, pursuant to statutory guidelines, approve private sector secondary market entities, as well as set standards by which secondary market entities would be eligible to issue Government-backed securities. The pricing of the guarantee should encourage competition, be commercially reasonable, and be subject to calibration based on predetermined criteria that considers market conditions.

Allow Multiple, Privately Capitalized Issuers of Government-Guaranteed Securities in the Secondary Multifamily Mortgage Market. Privately capitalized secondary market entities would be eligible to purchase mortgages, aggregate (if applicable), and issue Government-backed mortgage-backed securities that support the multifamily market. Regular and dependable security issuances would create the liquidity in the market to get attractive pricing and broad market participation by bond investors.

These issuers would be expressly permitted to purchase catastrophic reinsurance from the Government guarantor to wrap the MBS. The Government guarantee should be structured so that it can be expanded in times of market disruption. A mono-line structure, with segregated assets and separate capital standards, would facilitate capital adequacy determinations, regulatory oversight, and aggregation capabilities to support structured risk-sharing transactions. The Government guarantor/regulator would be able to authorize the establishment of multiple such entities.

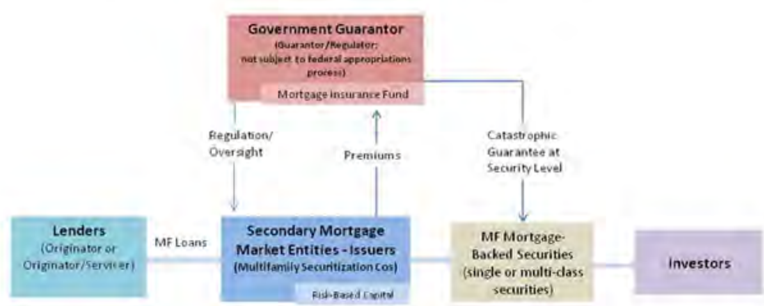
The secondary market entities should be required to be separately capitalized. Governance structures that enhance independence from potential affiliated business lines (if any) should be considered. We believe that these entities could be (but need not be) affiliated with single-family market entities. They would provide liquidity to the workforce rental housing market, including secondary and tertiary markets.

Preserve and Carry Over Execution Models. The GSEs' multifamily executions incorporate substantial private capital and risk sharing with other market participants, and have exhibited strong credit performance with current delinquency rates of less than 20 basis points. This and other flexibility in the structure of the Government wrap on MBS is important to allow for multiple risk-sharing executions to manage credit risk. These businesses are valuable to U.S. taxpayers and should be transferred to new entities that would serve the multifamily housing finance market. Notably, in the multifamily space, we do not believe there is a need for utilization of a common securitization platform, private mortgage insurance, or other single-family-specific concepts at this time.

Consider Affordable Character of Multifamily Rental Housing. By its very nature, multifamily rental housing tends to be affordable, with 93 percent of multifamily units having rents affordable to households earning area median incomes or less. Policy proposals contemplating affordability requirements, if any, on secondary market entities should take this into account. Any proposed approaches also should be reasonable and flexible, as well as balanced with regard to the need to attract private capital.

Summary Diagram. The following diagram summarizes our structural recommendations:

DIAGRAM OF RECOMMENDED MULTIFAMILY HOUSING FINANCE FUTURE STATE



Pending Legislative Proposals

MBA is encouraged by recent legislative activity that has revived the policy debate on the future of Fannie Mae and Freddie Mac. Senate and House members have introduced thoughtful proposals that would create a comprehensive framework for the future of housing finance. We commend these efforts. MBA views all such proposals through the lens of our guiding principles. In particular, the future system of multifamily finance should rely on private capital and protect taxpayers, while ensuring stable and continued liquidity in all economic cycles through a Government backstop.

In the Senate, Senators Corker and Warner have introduced bipartisan legislation that would transform the housing finance system. To the extent that the Committee considers portions of this bill in its efforts to craft comprehensive GSE reform legislation, we offer several recommendations.

With regard to its treatment of multifamily housing finance, MBA strongly supports the bill's approach that provides an explicit Government guarantee (through a Federal Mortgage Insurance Corporation (FMIC)) for multifamily loans. We also support the establishment of premiums paid into an FMIC-administered insurance fund, oversight by the FMIC as a strong regulator, and recognition of the value and retention of the GSEs' multifamily executions (i.e., Delegated Underwriting and Servicing and Capital Markets Execution/K-Deals).

However, we would urge that the statutory language explicitly distinguish between the roles of the FMIC and multifamily private sector participants: The FMIC should retain the role of regulator, Government guarantor and administrator of an insurance fund—but other roles should be transferred to private sector entities. Specifically, the bill should direct the FMIC to establish privately capitalized secondary mortgage market entities to serve as issuers in the multifamily housing finance market. The current multifamily platforms of the two GSEs could be moved over into such new entities. Moving these businesses to the private sector (through a sale or public offering)—with continued access to a Government guarantee—would likely return substantial capital to the U.S. Treasury.

These secondary market entities would purchase multifamily mortgages, aggregate loans, manage and distribute credit risk, credit enhance, and structure and issue Government-backed MBS that support the multifamily market. In other words, the secondary market entities would have access to purchase catastrophic reinsurance from the Government guarantor that wraps the MBS. We also believe that the FMIC should be authorized to approve several such companies in order to foster competition and innovation, setting forth criteria for the approval of these multifamily issuers. Governance guidelines and approval standards should be established as well.

Importance of FHA Multifamily and Health Care Programs

While not the focus of today's hearing, I would like to emphasize the essential role that FHA plays in supporting the multifamily housing market. The Federal Housing Administration is a critical source of the long-term, fixed-rate debt needed to build and refinance affordable rental units for working families, seniors, and underserved populations. FHA's multifamily and health care loan programs are each designed to address a different loan type or segment of the market.[7] FHA has played a strong, countercyclical role in this market as well. Its status as a Government agency subject to the Federal appropriations process, however, has presented inherent limitations in FHA's capacity, as we are witnessing today with commitment authority limitations and the recent Federal Government shutdown.

FHA provides an explicit Federal Government guarantee on multifamily and health care loans through a range of programs established by Congress. The guarantee is paid for through a mortgage insurance premium set by HUD and paid by the borrower. Not only have FHA multifamily and health care loans performed well with low default rates (as published by HUD in May 2013), but the programs generate significant revenue to the Federal Government in the form of a negative credit subsidy, generating positive cash flow to the U.S. Treasury. Diversification in business mix for FHA multifamily programs is essential and has contributed to their strong credit performance. Mortgage insurance premiums are deposited into FHA's GI/SRI fund, separate from the MMI fund that supports FHA's single-family programs. FHA serves a wide market that is sometimes bypassed by other capital sources. Many properties are in secondary or tertiary markets supported by niche borrowers and lenders, and this capital source supports a vital need in these areas.

Accordingly, MBA strongly recommends that Congress (1) reduce disruptions—at this time and on an ongoing basis—to the FHA multifamily and health care programs; (2) provide adequate FHA Commitment Authority for the full fiscal year to avoid costly and counterproductive stop and start problems; and (3) continue to encourage FHA to maintain a balance of affordable and market rate FHA multifamily financings.

Transition and Stewardship of GSE Multifamily Resources

As the Committee is well aware, the GSEs are subject to FHFA's conservatorship and the Treasury Department's controlling interest pursuant to the preferred stock purchase agreement originally entered into in September 2008.[8] With the GSEs controlled by the Federal Government, we urge policy makers to exercise stewardship with regard to the resources and assets of the GSEs' multifamily businesses—for purposes of ensuring a stable transition to the future system of multifamily housing finance.

While it is clear that the current state of the GSEs should not last indefinitely, policy makers should ensure the ongoing stewardship of valuable resources that support the multifamily market, utilizing them to transition to a stronger multifamily housing finance system. The resources of the GSEs, as taxpayer assets, should be preserved to support an orderly transition to a new mortgage finance system and ultimately to optimize potential returns to taxpayers.

The talent, expertise and intellectual capital of their staff are valuable to the Federal Government, and the future deployment of these resources should be a core consideration in the transition to the future state of housing finance. Similarly, the mulitfamily market executions of the GSEs (each utilizes a distinct structure as its primary execution and attract private capital that assumes a substantial credit risk position) and their existing multifamily books of business are clearly taxpayer as-

[7] Some of the major FHA multifamily programs are: (1) new construction/substantial rehabilitation (NCSR); (2) section 223(f) for the purchase or refinancing of existing multifamily properties; and (3) section 223(a)(7) for the refinancing of loans that already have an FHA-insured mortgaged. FHA and its lender partners also provide financing programs to support health care and assisted-living facilities.

[8] The Treasury Department's August 2012 announcement on the most recent amendment to the agreement, requiring an expedited reduction in the GSEs' retained portfolios and an all income sweep of the GSEs' profits (but for specified capital reserve amounts), further underscores the integral tie between these entities and the Federal Government.

sets, and should be viewed in a manner that supports the pathway toward the future state of multifamily finance.

We also caution that the multifamily finance market and the role GSEs play should not be viewed as a potential thought experiment to test out scenarios. Blunt or dramatic changes imposed in conservatorship, for example, would be highly disruptive, risk the loss of significant talent, and reduce the value of taxpayer assets. Regulatory or legislative actions that could substantially jeopardize the viability and value of key resources within the GSEs' multifamily businesses should be avoided. While policy makers should continue to explore steps to faciliate the transition forward, the do no harm principle should equally govern.

Conclusion

Thank you for the opportunity to testify before you today. MBA remains committed to its key principle that a successful multifamily secondary market should rely primarily on private capital, while ensuring stable and continued liquidity in all economic cycles. We believe that this can be achieved in manner that protects taxpayers and builds upon the successes and strong foundation that exists today. We would be pleased to assist the Committee as it continues to engage in this critically important effort.

PREPARED STATEMENT OF SHEKAR NARASIMHAN

MANAGING PARTNER, BEEKMAN ADVISORS, INC.

OCTOBER 9, 2013

Chairman Johnson, Ranking Member Crapo, Members of the Committee: Good morning. Thank you for inviting me to testify at this hearing on Housing Finance Reform. My name is Shekar Narasimhan, and I am Managing Partner of Beekman Advisors, which provides consulting services to various commercial real estate and financial services companies. I have spent the past 35 years in housing and finance, including 4 years building single-family homes in Eastern Kentucky. Later, when I was CEO of one of the first publicly traded commercial mortgage finance companies, we developed loan products to serve the low-income housing tax credit market. My experience in running and operating a real estate financial services business as a partner with Fannie Mae, Freddie Mac and FHA is what brings me here today. Through all this, I developed a deep and abiding passion for affordable housing.

The multifamily businesses at the GSEs are not part of the problem in the housing finance system. In fact, they are part of the solution. Every major principle articulated by stakeholders with regard to what a new housing finance system should look like is in practice at the multifamily businesses of the GSEs:

- Alignment of interest between the borrower, lender/investor, and issuer. Typically 20-percent borrower equity, lender, or investor taking risk if loan defaults and issuer putting its capital and reputation on the line;
- Detailed underwriting of every loan. Significant property, borrower and financial reviews with quarterly monitoring after loan closes and annual inspection to ensure maintenance;
- Service of virtually every market segment with a menu of stable and responsible lending products. Consistently serving the multifamily market for working class and lower-income households—strong rationale for policy makers to consider limited Government support for multifamily finance;
- Participation of both small and large private lenders in the system with skin in the game. Both issuer- and security-based risk-sharing models are already in place;
- A lengthy track record of profitable operations, even through conservatorship ($13.6 billion in profits over the last 3 years). Gives credence to the belief that private capital will be willing to capitalize these companies; and
- A footprint that responds appropriately to economic conditions. Market share ranging from 25 percent during a bull period for the capital markets to 70 percent at the height of the crisis.

I am here today to propose that the multifamily businesses at the GSEs should be used to demonstrate the path to the new housing finance system, by spinning them out as privately capitalized entities with Government guarantees limited to only the securities they issue.

We all recognize change is needed as everyone agrees that 5 years of conservatorship is already too long. It has discouraged the best and brightest from remaining at the GSEs and has stifled creativity. Moreover, it has left secondary markets uncertain. This is not good given that the significantly larger rental population (41 million at last count) desperately needs a steady supply of new rental housing units to keep housing burdens manageable. This is especially true for renters earning less than 80 percent of area median income. This is the market the current GSE multifamily businesses have served yesterday and today with over 60 percent of the units they finance affordable to those at 80 percent of area median income or below.

Responsible change, however, should involve doing the least damage. The work done recently at the multifamily units of Fannie Mae and Freddie Mac (at the behest of their regulator, FHFA) supports our conclusions on how to make this shift. Continue the focus of the new entities on the middle of the market and that they meet reasonable standards. Allow multiple entities to become issuers, but do not allow one to become dominant. Regulate the resulting issuers and guarantors to ensure a level playing field and have the ability and motivation to serve the broad markets now and in the future. In short, we believe our proposed pathway, if followed, will result in the least disruption to the markets and maximize the return to the Treasury.

What I propose therefore is an immediate spinout of the multifamily operations of Fannie Mae and Freddie Mac. It can fit into the architecture of any bipartisan proposal that embodies the principles of private risk capital in front of a limited Government guarantee and continued availability of multifamily financing at all times in all markets. Transition to this new multifamily state can occur within a 2–3 year period. First, create wholly owned multifamily subsidiaries of the current GSEs that can operate autonomously with a contract to manage the multifamily assets of their parent companies. Then, as soon as the Government guarantor is stood up, spin them out with a well-constructed regulatory framework that encourages private capital to invest in these entities for the long-term.

There is no reason to wait given rental demand and the profitable track record of these current businesses. This is laid out in the paper and subsequent proposal my two colleagues and I have written.

Thank you for the opportunity to make these remarks. I will enter our proposal and the supporting information into the record, and look forward to your questions and comments.

Multifamily Mortgage Finance Reform

Background and Recommendations for Reform

Senate Banking Committee

October 9, 2013

THIS DOCUMENT DRAWS FROM THE WHITE PAPER; "MULTIFAMILY FINANCE REFORM: MOVING TO A SOLUTION IN 2013". Dated June 24, 2013

White paper Co-Authors:

Raphael Bostic

- Dr. Raphael Bostic is the Judith and John Bedrosian Chair in Governance and the Public Enterprise at the Sol Price School of Public Policy at the University of Southern California. He has recently returned to USC after serving for 3 years in the Obama Administration as the Assistant Secretary for Policy Development and Research at the U.S. Department of Housing and Urban Development.

Shekar Narasimhan

- Shekar Narasimhan is the Managing Partner at Beekman Advisors. He also serves as Chairman of Papillon Capital, focused on sustainable infrastructure investing. Prior to Beekman Advisors, Shekar Narasimhan was Chairman & CEO of WMF Group, one of the largest multifamily GSE and FHA lenders which he sold in 2000 to Prudential Mortgage Capital Company.

Mark Willis

- Mark Willis is a Resident Research Fellow at the Furman Center for Real Estate & Urban Policy at the New York University. Before joining the Center, Mark was a Visiting Scholar at the Ford Foundation, working on research related to community development and the financial services sector. Prior to his time at Ford, Mark spent 19 years at JPMorgan Chase, overseeing its community development programs

Note: Organizational affiliations are for informational purposes only. Views are the authors alone.

Importance of multifamily

- Renters are an increasing share of the occupied housing stock.
    - Today 34% of households are renters, up from 31% in 2005.
    - As more people have moved from home ownership to rental, the overall rental vacancy rate has dropped for three years in a row to the lowest figure since 2001.
- Demand for multifamily is growing.
    - 40% of rental stock is in multifamily buildings (five or more units).
    - Multifamily renter occupied units increased by 5% from 15.2 million in 2005 to 16.0 million in 2011.
- Renters are facing a growing affordability crisis.
    - Renters earn, on average, about $30,000/year, approximately 55% of what homeowners earn.
    - 27% of renters pay more than half their income on housing, twice the share of homeowners similarly burdened.

Multifamily financing differs from single-family financing

- Multifamily properties are businesses.
- Typical size loan is $6 million versus single family at $100,000.
- Loans are individually underwritten by both lenders and investors.
- Underwriting involves analysis of rental income, expenses, property condition, etc.
- Typical "down payments" of 15-20 percent.
- Lenders perform annual inspections and quarterly financial reviews.

Role of Fannie and Freddie multifamily

- Liquidity: Fannie and Freddie alone backed nearly 60% of multifamily mortgages in 2012.
- Broad Access to Credit: These two GSEs serve broad geography and diverse lenders, including banks and insurance companies.
- Flexible Products: Fannie and Freddie offer more longer-term and fixed-rate loans than banks.

- Strong Underwriting: The multifamily delinquency rate during the crisis peaked for the two GSEs at 0.7%, compared to 12% for commercial mortgage-backed securities and 4.4% for banks.
- Countercyclical Support: The GSEs' share of the multifamily mortgage market grew from 25% prior to the financial crisis to 70% in 2009.
- Affordable: Over 60% of rental units financed by Fannie and Freddie are affordable to those earning less than 80% of median income.

Private Capital: Fannie Mae's DUS Model

- 24 multifamily lenders nationwide are approved under Fannie's delegated underwriting and servicing (DUS) program.
- Lenders underwrite the loans themselves and put them into mortgage-backed securities that are guaranteed by Fannie.
- Two structures of risk-sharing with the lender:
    - Lender absorbs 1/3 of losses; Fannie the other 2/3.
    - Lender absorbs first 5% of the losses and then absorbs 25% of any additional losses up to an amount equal to 20% of the loan balance.
- Loan servicer required to pay principal and interest on loans that are delinquent for up to 90 days.

Private Capital: Freddie Mac's K-Series

- 23 multifamily lenders nationwide are approved under Freddie's "Program Plus" program
- Freddie Mac underwrites each loan submitted by approved lenders working directly with the borrower
- Private investors typically take the first 15% of losses on a pool of loans
- Two subordinate tranches that absorb first losses are a "B" piece and mezzanine debt

Recommendations for multifamily reform

- Government Guarantor (GG) provides and charges for an explicit government guarantee of timely payment of principal and interest on qualifying multifamily mortgage-backed securities.
- Two newly incorporated issuers (initially Fannie's and Freddie's multifamily businesses) continue current DUS and K-Series models.

- Framework allows for additional approved issuers that can either adopt the current Fannie or Freddie models or the structure allowed for single-family mortgages.
- GG sets up a co-op specifically to ensure that small lenders have access to financing.

Stages of Transition

1. Fannie's and Freddie's multifamily operating units are spun off into self-contained subsidiaries of their respective corporations.
2. These subsidiaries operate autonomously (e.g., have their own lines of credit).
   A. The subsidiaries contract to manage the multifamily assets of Fannie and Freddie respectively and receive a fee for doing so.
   B. The subsidiaries pay Fannie and Freddie respectively for the right to issue securities based on their corporate guarantees of timely payment of principal and interest.
3. These entities are privatized as soon as feasible (no private owner can have more than a 19.9% ownership interest).
4. The entities buy the government guarantee from the GG once it is up and running.

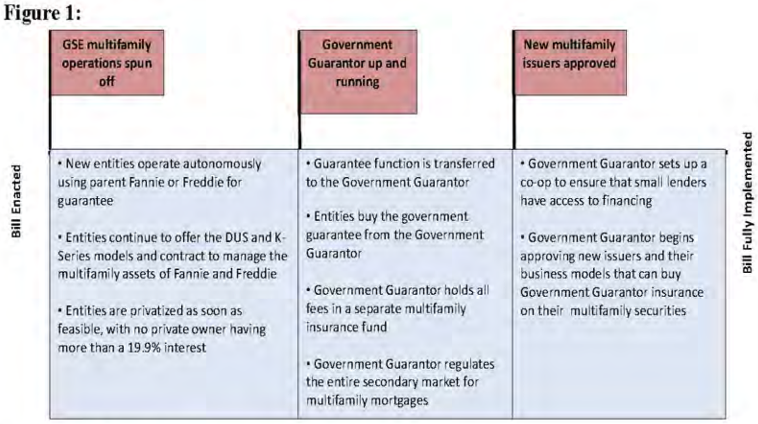
Market Focus

- For each approved issuer, at least 60% of the units financed each year by GG-backed multifamily securities must have rents affordable to tenants earning 80% of Area Median Income (AMI) assuming they spend no more than 30% of their income on housing (assessed at the time the loan is made).
- Any property financed by GG-backed multifamily security where the majority of the units have rents not affordable to renters earning less than 150% of AMI will trigger a 50 bps additional charge to be used for the National Housing Trust Fund, the Capital Magnet Fund and the Market Access Fund (Fund).
- An annual fee of 5-10 bps will be collected from all mortgage-backed securities that benefit from a government guarantee and used for the Fund.
- Approved issuers submit an annual plan for serving communities and market segments not well-served by private capital, including low-income communities, rural communities, subsidized affordable multifamily housing and small rental properties. They utilize the Market Access Fund to enable pilots and experimentation of products and processing changes to serve these markets.

Appendix

Stages of Transition

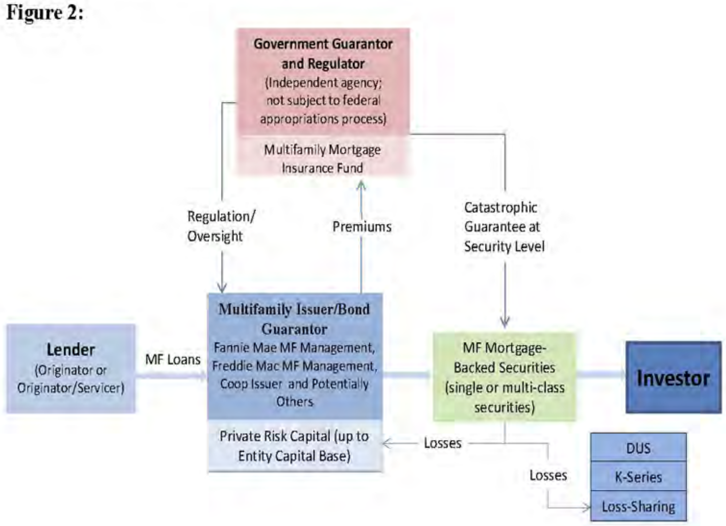
Figure 1:



Multifamily Finance Future State

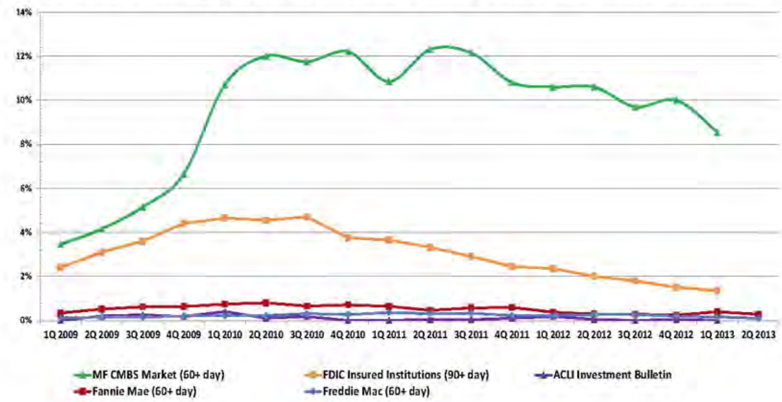
Catastrophic Guarantee from Government Guarantor kicks in only after Multifamily Issuer/Bond Guarantor Market Entity has used its capital base and all private parties have exhausted their risk-sharing obligations at the loan or security level

Figure 2:



Multifamily Market Delinquency Rates

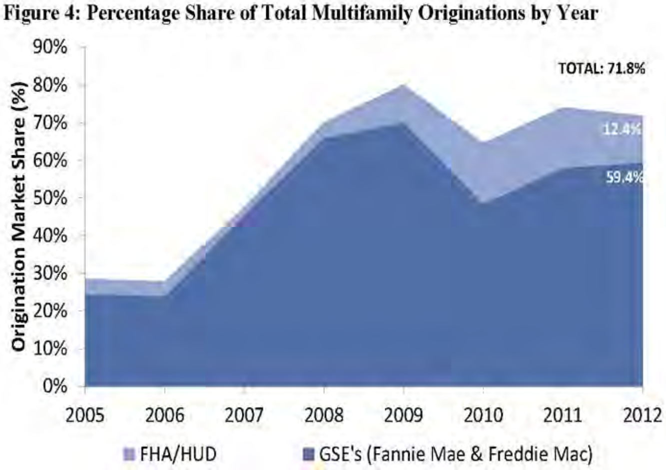
Figure 3: GSEs have superior performance over Banks, CMBS, comparable to Life Cos



Source: Freddie Mac, Fannie Mae, FDIC Quarterly Banking Profile, TREPP (CMBS multifamily 60+ delinquency rate, excluding REOs)

Historical Multifamily Market Share

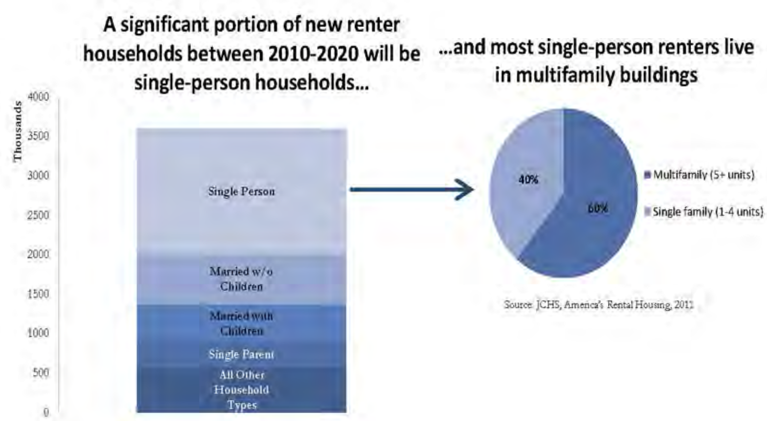
Figure 4: Percentage Share of Total Multifamily Originations by Year



Sources: Invesco presentation to Bipartisan Policy Center Housing Commission Forum; Fannie Mae, Freddie Mac and FHA public filings

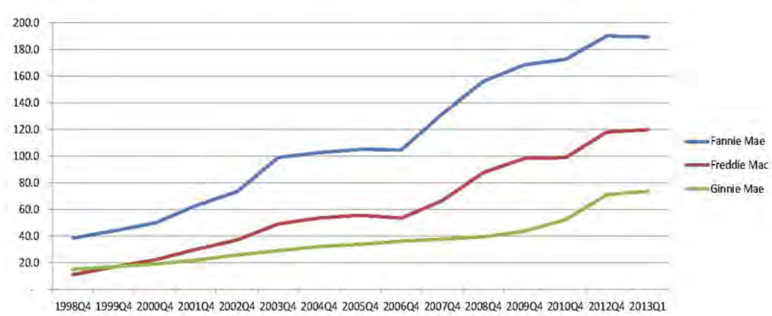
Growth in Rental Demand Continues into Future

Figure 5:



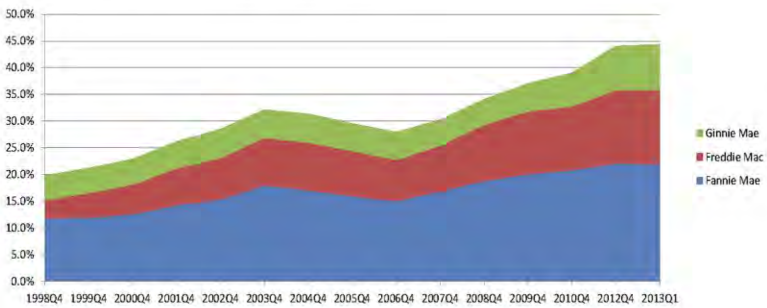
Multifamily Mortgage Debt Outstanding

Figure 6: GSE & Ginnie Mae Multifamily Mortgage Debt Outstanding ($ billions)



Source: Federal Reserve Flow of Funds

Figure 7: GSE & Ginnie Mae Multifamily Mortgage Debt Market Share (% of total): Near 45% and growing



Source: Federal Reserve Flow of Funds

Roles of Key Market Players

Figure 8:

Borrower	Lender	MBS Issuer/Bond Guarantor	Government Guarantor and Regulator	Investor
• Select lender • Select product • Acquire loan	• Underwrite loan • Originate loan • Service loans	• Acquire loans • Structure securities • Credit enhance securities, including buying Government Guarantor insurance • Issue & administer securities •Oversee risk-sharing partners (DUS Lenders, B-Piece buyers) • Disclosures	• Price the government guarantee • Collect G-fees and manage the multifamily insurance fund • Collect fees for the Affordable Housing Fund • Approval entities • Regulate the market for safety, soundness, access and affordability	• Purchase / sell securities with different risk characteristics • Access disclosures

PREPARED STATEMENT OF TERRI LUDWIG

PRESIDENT AND CHIEF EXECUTIVE OFFICER, ENTERPRISE COMMUNITY PARTNERS, INC.

OCTOBER 9, 2013

Chairman Johnson, Ranking Member Crapo, and Members of the Committee, thank you for the opportunity to testify this morning. I am Terri Ludwig, president and CEO of Enterprise Community Partners.

Enterprise works with partners nationwide to build opportunity. We create and advocate for affordable homes in thriving communities linked to jobs, good schools, health care, and transportation. We lend funds, finance development and manage and build affordable housing, while shaping new strategies, solutions, and policy. Over more than 30 years, Enterprise has created 300,000 affordable homes across all 50 States, invested $14 billion into communities and improved millions of lives.

One of Enterprise's many business lines is mortgage debt financing with a focus on affordable multifamily rental housing in low-income communities. Last year we originated $788 million in multifamily mortgages through our subsidiary, Bellwether Enterprise Real Estate Real Estate Capital, Inc., working with the Federal Housing Administration (FHA), Fannie Mae and Freddie Mac (the GSEs), private investors, and other partners. We are an FHA Multifamily Accelerated Processing (MAP) lender and Ginnie Mae issuer, a Fannie Mae Special Affordable Delegated Lender, a Freddie Mac Program Plus Seller Servicer and Targeted Affordable Housing lender and a U.S. Department of Agriculture Section 538 lender. We also make loans through the FHA Section 232 program and operate a registered community development financial institution, Enterprise Community Loan Fund, which invested $97 million into communities last year.

Before becoming president and CEO of Enterprise, I worked for more than 20 years in investment banking. My team and I used capital markets to efficiently invest in affordable housing and community development, often partnering with groups like Enterprise. This experience taught me that public–private partnerships are critical to bringing capital to working families in low-income neighborhoods. In countless communities across the country—rural, urban, and suburban—the combination of public and private financing is effectively producing quality affordable housing.

Still, there is an urgent and growing need for decent and affordable rental housing. Enterprise is working with Members of this Committee and others in Congress on several issues to ensure that the needs of low-income renters are met, including housing finance reform, preserving and expanding the Low Income Housing Tax Credit (Housing Credit), ensuring adequate appropriations for critical housing and community development programs, authorizing much needed reforms to rental assistance programs such as public housing and Housing Choice Vouchers, and finding new ways to preserve and improve the country's aging affordable housing stock. We look forward to continuing to work with you on these important issues as we work toward a day when every person in the U.S. has a quality and affordable home in a vibrant community.

We greatly appreciate the leadership of the Chairman, the Ranking Member and Members of this Committee as you work to determine the future of Fannie Mae, Freddie Mac, and the rest of the country's housing finance system. And we thank you for focusing today on an often-overlooked component of the reform effort: the multifamily mortgage market, which finances rental buildings with five or more units.

Above all else, we believe that any GSE reform plan must start with a simple goal: ensuring a liquid, stable and affordable housing market with appropriate support for both homeowners and renters, especially low income families.

In my testimony this morning, I will make the following points:

- *Multifamily housing is a key part of a well-functioning housing market.* Today more than one-third of the U.S. population rents, and that number is expected to grow in the coming years. And given who we expect these new renters to be—namely older or younger single-person households—multifamily will play an increasingly important role.
- *Fannie Mae and Freddie Mac play a critical role in multifamily housing finance today.* Among other things, Fannie and Freddie provide broad liquidity to the multifamily mortgage market, much-needed financing for affordable housing and a buffer from severe booms and busts in the rental market.
- *A limited, explicit Government guarantee is essential to a well-functioning rental market.* According to a series of recent studies from the Federal Housing Finance Agency (FHFA), without a Government guarantee on multifamily mort-

gages new construction of rental housing would plummet, average rents would rise significantly, and the entire rental market would be more vulnerable to boom-and-best cycles.[1] Low-income families would be disproportionately harmed, at a time when they already face an unprecedented affordable housing crisis.

- *Congress should pursue smart reforms to the multifamily market that preserve the business lines and other activities that work.* I will lay out a series of steps Congress should take to ensure a liquid, stable, and affordable rental market, starting by spinning off Fannie's and Freddie's multifamily businesses and providing access to a limited, paid-for Government guarantee.
- *Any future system of multifamily housing finance must have explicit provisions to support affordable housing, reach underserved segments of the market, and promote long-term sustainability.* I will lay out specific recommendations for each of these goals, which Congress should include in any housing finance reform legislation.

I'd like to start by providing a bit of context, including some background on the U.S. rental market and the Government's essential role in it.

Background on the U.S. Rental Market, Multifamily Housing, and the Growing Affordable Housing Crisis

More than 100 million people in the United States—about 35 percent of the population—rent their homes. In recent years more and more families have turned to the rental market, some because they are not ready for or not interested in home ownership, others because they have no other option. Over the past 8 years, the percentage of renters in the U.S. has increased by 4 percentage points.[2]

On average, renters are younger, earn less income, are more likely to be people of color and live in smaller households compared to homeowners. Their median age is 40, compared to 54 for homeowners. The typical renter household earns just over $31,000 per year, almost exactly half of the typical homeowner. Forty-seven percent are households of color, compared to 22 percent for homeowners. And 37 percent of renters are single-person households, compared to 23 percent for homeowners.[3]

Analysts predict a further shift toward rentals in the coming years. Part of this is due to the carry-over effects of the recent housing crisis, but the key driver is changing demographics. Harvard's Joint Center for Housing Studies projects an additional 3.6 million new households will become renters between 2010 and 2020, led mostly by an increase in younger, senior, and minority households.[4]

These populations increasingly rely on multifamily housing as a source of stable, affordable rental housing. Today 40 percent of rental units in the U.S. are in multifamily buildings, but roughly 60 percent of single-person renters—often a sign of a younger or senior household—live in multifamily buildings. In addition, analysts at Harvard have found that younger renters "tend to favor multifamily housing in center city locations" linked to transit, jobs, and other opportunities.[5]

Regardless of what type of housing America's renters live in, one thing is clear: they are facing an unprecedented affordable housing crisis. That's especially true for renters at the lower end of the income scale.

Housing costs for the typical renter rose by 6 percent between 2008 and 2011, while their income dropped more than 3 percent after adjusting for inflation, according to the Center for Housing Policy.[6] While the number of very low-income renters has increased by 17 percent since 2007, the total number of affordable rental units has actually declined.[7] As a result, of the 17.1 million very low-income renters in the U.S. today, 7.1 million spend more than half their income on rent, live in sub-

[1] Federal Housing Finance Agency. News Release: "FHFA Releases Fannie and Freddie Reports on Viability of Their Multifamily Business Without Government Guarantees". Attachment: "2012 Conservatorship Scorecard: The Enterprises' Reports on a Multifamily Future State Without a U.S. Government Guarantee". FHFA, 3 May 2013.

[2] Joint Center for Housing Studies of Harvard University. Chapter 5: "Rental Housing, The State of the Nation's Housing 2013". JCHS, June 2013.

[3] Ibid.

[4] Joint Center for Housing Studies of Harvard University. "America's Rental Housing: Meeting Challenges, Building on Opportunities". JCHS, April 2011.

[5] Ibid.

[6] Janet Viveiros and Maya Brennan. "Housing Landscape 2013: An Annual Look at the Housing Affordability Challenges of America's Working Households". National Housing Conference, Center for Housing Policy, May 2013.

[7] Joint Center for Housing Studies of Harvard University. "Fact Sheet, The State of the Nation's Housing 2013". JCHS, June 2013.

standard conditions, or both, according to the Department of Housing and Urban Development. [8]

All told, 27 percent of renters—about 11 million families—are paying at least half of their monthly income on housing, a severe cost burden that often leaves families one paycheck away from losing their home. That's an all-time high. [9]

Fannie Mae and Freddie Mac Play a Critical Role in Multifamily Housing Finance Today

Today there is roughly $875 billion in multifamily mortgage debt outstanding. [10] Capital flows to the multifamily mortgage market from five main sources and several smaller ones:

- *Fannie Mae and Freddie Mac,* which account for 36 percent of multifamily debt outstanding. The GSEs serve a wide geography and a range of income levels and housing types, during both good and bad economic times.
- *Banks and thrifts insured by the Federal Deposit Insurance Corporation (FDIC),* which account for 28 percent of multifamily debt outstanding. Banks and thrifts typically offer floating-rate, short-term debt, serving a broad range of lenders and communities. But their presence in the multifamily market has shrunk significantly since the start of the financial crisis.
- *The Federal Government,* which accounts for 10 percent of multifamily debt outstanding. This includes Ginnie Mae securities backed by mortgages insured by the Federal Housing Administration (FHA), the Department of Agriculture, and other Federal agencies. The FHA insures high-leverage loans with terms of up to 40 years and offers construction financing as part of the permanent loan.
- *Conduits for commercial mortgage-backed securities (CMBS),* which account for 9 percent of multifamily debt outstanding. These are securities issued by financial institutions made up of multifamily, office, retail, and other loans that are not backed by the Federal Government. The CMBS market was a leading source of capital during the recent housing bubble—peaking at 17 percent of the market in 2007—before it practically shut down during the crisis.
- *Life insurance companies,* which account for 6 percent of multifamily debt outstanding. Historically, life insurance companies have preferred to finance "Class A" multifamily assets, such as luxury apartment buildings in top-tier housing markets.
- *Other sources,* which account for the remaining 11 percent of multifamily debt outstanding. This includes State and local governments, private pension funds, Real Estate Investment Trusts, and nonbank corporate businesses.

From their volume alone, it's clear that Fannie and Freddie are a critical part of today's multifamily market. By purchasing and securitizing a range of multifamily mortgages across geographies and lender types, Fannie and Freddie ensure that developers and owners have the capital they need to build, maintain, and preserve rental housing. But increased liquidity is just one of many roles the GSEs play.

First, they promote stability and broad access to credit through flexible products. Fannie and Freddie tend to offer longer-terms and more fixed-rate loans than banks, thrifts, and life insurance companies, which helps owners plan for future costs. Shorter-term, adjustable-rate mortgages, on the other hand, require frequent refinancing and recapitalization, which could discourage owners from holding onto a property over a long period.

Second, the GSEs promote strong underwriting, which mitigates systemic risk in the rental market. Fannie and Freddie multifamily deals are carefully underwritten and include a significant amount of risk sharing with purely private investors, which further limits taxpayer exposure to risk. For example, Freddie Mac's K-Series deals typically require private investors to cover the first 15 percent of losses without a guarantee, while Fannie Mae's mortgage-backed securities require its licensed lenders to cover the first 5 percent plus a significant portion of further losses. [11]

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[8] U.S. Department of Housing and Urban Development, Office of Policy Development and Research. "Worst Case Housing Needs 2011: Report to Congress". HUD, PD&R, August 2013.

[9] Joint Center for Housing Studies of Harvard University. Chapter 6: "Housing Challenges, The State of the Nation's Housing 2013". JCHS, June 2013.

[10] Mortgage Bankers Association. "MBA Commercial Real Estate/Multifamily Finance: Mortgage Debt Outstanding: Q2 2013". MBA, September 2013.

[11] David Brickman. "K-Deals A Model for the Future of Mortgage Securitization. Freddie Mac, Executive Perspectives Blog: Insights on Housing Finance", September 2013. Available at *http://www.freddiemac.com/news/blog/david_brickman/20130906_mortgage_securitization.html.*

As a result, GSE multifamily loans have experienced much lower delinquency rates than similar loans from private investors. According to the Mortgage Bankers Association, today only about 0.2 percent of Fannie- or Freddie-backed multifamily loans are delinquent by 60 or more days, compared to 2.1 percent for loans held by banks and thrifts and 7.8 percent for loans in commercial mortgage-backed securities.[12]

Third, they provide crucial countercyclical support to the market. As recently as 2007, Fannie and Freddie combined for less than 30 percent of multifamily loan originations, while private investors absorbed the rest of the market in their eagerness for mortgage debt. By 2009—the year after the housing market collapsed, taking the entire financial system with it—Fannie's and Freddie's share nearly tripled to 85 percent as investors were leery of putting their money into housing without a Government guarantee.[13] Without that support, financing for multifamily housing would have all but dried up, halting all new construction and making it extremely difficult for building owners to refinance maturing loans.

Finally, the GSEs are critical sources of financing for affordable rental housing. This includes both the apartments financed through GSE multifamily securities and the investments held in each company's portfolio. Over the years, Fannie and Freddie have developed working relationships with small community banks, State housing finance agencies, and community development financial institutions across the country, allowing them to efficiently and profitably finance affordable housing in lower-income communities.

Last year, 67 percent of the rental units financed by Fannie or Freddie were affordable to families earning less than 80 percent of Area Median Income (AMI), commonly referred to as "low-income," while roughly 17 percent were affordable to families earning less than 50 percent of AMI, commonly referred to as "very low-income."[14] While rent data are not available on units financed by banks, we know that private investors tend to prefer higher-end properties in top-tier markets.

A key to Fannie's and Freddie's ability to play this important role in the market is their access to an explicit guarantee from the Federal Government.

A Limited, Explicit Government Guarantee Is a Key Part of a Well-Functioning Rental Market

After 5 years of conservatorship, we are pleased to see Congress making meaningful progress on housing finance reform. Regardless of what lawmakers decide to do with Fannie Mae and Freddie Mac, I urge you to preserve the aspects of the current system that have proven to work. This includes an explicit, limited guarantee on multifamily mortgages.

The Government guarantee on multifamily mortgages makes the U.S. rental market more liquid, more stable, and more affordable. These are four powerful reasons for maintaining it in any reform effort.

Eliminating the multifamily guarantee would have devastating consequences for the U.S. rental market, with low-income communities bearing the largest share of the burden. Earlier this year FHFA asked Fannie, Freddie and external consultants to assess what the market would look like without a Government guarantee on multifamily mortgages.[15] They found that:

1. Without a Government backstop, the rental market would be subject to wild boom-and-bust cycles, leading to significantly less development during market downturns. According to Freddie Mac's estimates, this lack of stability would cause multifamily interest rates to increase by 150 basis points and multifamily property values to decrease by as much as 16 percent; and[16]
2. Rental housing would be much more difficult to find and much more expensive. If the Government guarantee were to go away, new construction on multifamily housing would plummet by as much as 27 percent, while average rents would

[12] Mortgage Bankers Association. "MBA Commercial Real Estate/Multifamily Finance: Mortgage Delinquency Rates for Major Investor Groups: Q2 2013". MBA, August 2013.

[13] Federal Housing Finance Agency, Office of Inspector General. "FHFA's Oversight of the Asset Quality of Multifamily Housing Loans Financed by Fannie Mae and Freddie Mac". FHFA OIG, February 2013.

[14] Fannie Mae financed 559,000 multifamily units in 2012, 376,000 of which were affordable at 80 AMI or below and 109,000 of which were affordable at 50 AMI or below. Freddie Mac financed 435,000 multifamily units in 2012, 299,000 of which were affordable at 80 AMI or below and 60,000 of which were affordable at 50 AMI or below.

[15] Federal Housing Finance Agency. News Release: "FHFA Releases Fannie and Freddie Reports on Viability of Their Multifamily Business Without Government Guarantees". Attachment: "2012 Conservatorship Scorecard: The Enterprises' Reports on a Multifamily Future State Without a U.S. Government Guarantee". FHFA, 3 May 2013.

[16] Ibid.

rise by as much as 2 percent.[17] And since purely private investors would be less likely to finance lower-end developments in second- and third-tier markets, lower-income families would likely see even bigger increases in rent.

It's also important to note that Fannie's and Freddie's current multifamily businesses are quite profitable—as they have been throughout the housing crisis—and have steadily returned money back to the U.S. Treasury in recent quarters. According to 2012 financial reports, Fannie Mae's multifamily business reported a net income of $1.5 billion last year,[18] while Freddie Mac reported $2.1 billion.[19] Meanwhile, according to FHFA's own analysis, "there is little inherent value in (Fannie's and Freddie's) current multifamily businesses without the Government guarantee."[20]

Our Plan for Multifamily Housing Finance Reform

Last month, Enterprise coauthored a detailed plan for multifamily housing finance reform, along with members of the Mortgage Finance Working Group. The plan was initially drafted as a supplement to the bipartisan Housing Finance Reform and Taxpayer Protection Act of 2013 (S.1217), which preserves a limited and paid-for Government guarantee on qualifying multifamily securities. We propose:[21]

- Starting immediately, spin off Fannie's and Freddie's multifamily businesses into two self-contained subsidiaries of their respective corporations. The new entities would maintain the current multifamily products—namely the Fannie Mae DUS Program and the Freddie Mac CME Program K-Series—and contract with Fannie and Freddie to manage the existing multifamily assets.
- During a brief transition period, these entities would continue to purchase, securitize, and insure qualifying multifamily mortgage-backed securities, with support from the U.S. Treasury as needed.
- When the public guarantor (the FMIC under S.1217) is fully operational, the insurance function would be transferred to the Federal Government. From that point on, the new entities would have the option of purchasing FMIC insurance on the multifamily securities they issue, backed by the full faith and credit of the U.S. Government. The FMIC maintains all multifamily guarantee fees in a separate insurance fund.
- Over time, the new entities would be required to raise private capital with the option of buying out the Government's interest. Meanwhile, other Government-approved, privately funded companies would have the option of purchasing FMIC insurance on the multifamily securities they issue. As soon as possible, the FMIC would establish a third issuer (beyond the two new entities) to ensure that smaller banks have access to the secondary market for multifamily mortgages.

By spinning off the GSEs' multifamily businesses, Congress can ensure that the multifamily market continues to function smoothly through any transition period. By preserving Fannie's and Freddie's tried-and-true multifamily products, Congress can provide much-needed certainty to multifamily investors, ensuring that money keeps flowing into the rental market. And by setting a clear path forward for the companies' multifamily businesses—which remain profitable—Congress can help Fannie and Freddie keep top talent, retain institutional memory, and invest in the staff, systems and technology necessary to compete in a constantly evolving market.

In addition, by opening the Government guarantee to other Government-approved issuers down the line, Congress can promote competition in the market and protect taxpayers from "too-big-to-fail" bailouts. And by setting up a third approved issuer put in place to support smaller lenders, lawmakers can ensure that all communities have equitable access to the Government guarantee.

[17] Freddie Mac. "Report to the Federal Housing Finance Agency: Housing Finance Reform in the Multifamily Mortgage Market". Freddie Mac, December 2012.
[18] Fannie Mae. "Form 10-K: Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934". United States Securities and Exchange Commission, December 2012.
[19] Freddie Mac. "Form 10-K: Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934". United States Securities and Exchange Commission, December 2012.
[20] Federal Housing Finance Agency. News Release: "FHFA Releases Fannie and Freddie Reports on Viability of Their Multifamily Business Without Government Guarantees". Attachment: "2012 Conservatorship Scorecard: The Enterprises' Reports on a Multifamily Future State Without a U.S. Government Guarantee". FHFA, 3 May 2013.
[21] Mortgage Finance Working Group. "Multifamily Housing Finance Reform Proposal for Corker-Warner". Center for American Progress, August 2013. The Working Group's full proposal is available at: *http://www.americanprogress.org/wp-content/uploads/2013/08/MFWG-Corker-Warner-multifamily-recommendations-Aug1-FINAL.pdf.*

Other Important Components of Any Future System of Multifamily Housing Finance

There are other important issues that require attention in any multifamily reform legislation. These include:

Broad Affordability Mandate for Issuers of FMIC-Insured Multifamily Securities

A Government guarantee on multifamily securities is remarkably valuable. So it makes sense for policy makers to target the benefits of that support to the renters who need it most—namely low- and moderate-income families.

We propose a broad affordability mandate for all issuers of FMIC-insured multifamily securities. For each issuer, not less than 60 percent of the rental units financed through FMIC-insured securities in a given year must be affordable to low income families making 80 percent of AMI or less. This requirement would be assessed at the time of origination based on a 30-percent affordability standard and would be reported to the FMIC at the end of each fiscal year.

Support for Deeply Affordable Housing for Lower-Income Families

During the past two decades, Fannie and Freddie have shown that investors can finance affordable housing in a way that's both responsible and profitable. For very low-income renters below 50 percent of AMI, however, it's very difficult to make those deals pencil out without outside subsidy to help cover operating costs.

Therefore, instead of mandating that a certain percentage of Government-backed issuers serve very low-income families, we recommend levying an additional 5–10 basis point fee on all FMIC-insured multifamily securities to fund programs that provide housing to families earning 50 percent of AMI or less. Specifically, the proceeds from that fee would fund the National Housing Trust Fund, the Capital Magnet Fund and additional programs to support broad access to safe, affordable mortgage credit in low-income communities.

These funds have the potential to meaningfully expand the supply of affordable rental housing in the U.S.—through States for the Housing Trust Fund and through community development financial institutions and nonprofit housing developers for the Capital Magnet Fund. The Capital Magnet Fund is particularly effective at encouraging private investment in affordable housing; in the initial round of funding in 2010, recipients were able to leverage 15:1 with private capital sources.[22] As originally envisioned, both funds should have received funding through assessments on the GSEs' ongoing business, but those obligations were suspended when Fannie and Freddie were put into conservatorship.

While we don't recommend placing a hard limit on the type of multifamily properties the FMIC can insure, there could be a benefit in discouraging higher-end properties from accessing the Government guarantee. For example, if the majority of units in a multifamily property financed by a FMIC-backed security are unaffordable to families earning less than 150 percent of AMI, the FMIC could collect an additional fee to fund affordable housing programs.

Plans To Reach Underserved Segments of the Multifamily Market

Private investors have historically done a poor job of serving the entire rental market on their own. Certain segments—namely low-income communities, rural and Native American communities, subsidized affordable multifamily housing and small multifamily housing—have been underserved by traditional capital markets, resulting in housing scarcity, disproportionately expensive rents, and unacceptably poor conditions.

Fannie and Freddie are critical sources of capital for these underserved segments. For example, prior to 2008 Fannie Mae was a primary investor in several affordable housing developments in tribal lands financed with the Housing Credit. In fact, Fannie was one of the only private investors in this market at the time. Over the past two decades Enterprise has partnered with Fannie to build or preserve nearly 700 affordable homes on Native Lands.

We recommend addressing this problem through an annual strategic planning process. Each year, each approved issuer of FMIC-insured multifamily securities should work with the FMIC to create a plan for serving underserved market segments. At the end of each year, each issuer would report on their performance toward that plan. If the issuer does not comply or routinely misses their targets under

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[22] U.S. Department of the Treasury, Community Development Financial Institutions Fund. "Treasury Officials, Congresswoman Lee Announce $80 Million in Awards for Affordable Housing: Inaugural Round of Capital Magnut Fund Awards Provides Critical Financing To Meet Affordable Housing Need". CDFI Funds, October 2010. Available at *http://www.cdfifund.gov/news__events/CDFI-2010-43-Treasury-Officials-Congresswoman-Lee-Announce-80-Million.asp.*

this plan, the FMIC can apply financial penalties or revoke their approved-issuer status.

In addition, we recommend mandating that the FMIC establish at least one pilot program to test the securitization of small multifamily loans, which typically finance rental properties with between 5 and 50 units. These buildings are a critical source of affordable housing in many communities, but they are often difficult to execute profitably through traditional capital channels.

Encouraging Investments in Low-Income Housing Tax Credits

For decades, Fannie Mae and Freddie Mac played a critical role in the Housing Credit market. Since its inception in the late 1980s, the Housing Credit has been America's main tool for building and preserving affordable homes, creating 2.6 million and counting. Each year the program finances roughly 90 percent of affordable homes created in the U.S., generating 140,000 jobs and $1.5 billion in State and local tax revenues in the process.[23]

Before the financial crisis, the GSEs provided roughly 40 percent of Housing Credit investments producing tens of thousands of affordable apartments each year, including in markets with little to no CRA-related investment. After the financial crisis began, Fannie and Freddie all but withdrew from the Housing Credit market. The market has since rebounded and is running smoothly today, but it lacks a stable entity to keep money flowing into Housing Credit deals during future economic downturns.

To further promote affordable housing, we believe that any future system of multifamily housing finance should include rules that encourage issuers of FMIC-backed securities to invest in Housing Credit deals. As one possible approach, the FMIC could count any affordable units financed through Housing Credit investments toward the issuer's annual affordability requirement described above.

Promoting Energy Efficiency and Long-Term Sustainability in Multifamily Housing

There are tremendous economic benefits to investments in energy-efficient systems for multifamily buildings. That's especially true for the existing affordable housing stock, where we're seeing rising utility costs straining many owners.

For example, Enterprise recently extended a line of credit to owners of a large multifamily development in Brookline, Massachusetts. The owners made an up-front investment of just under a million dollars to install energy-efficient boilers, water pumps, and controls. The retrofits brought a 25-percent reduction in energy usage in the first year, translating to $170,000 in savings. The owners project that future savings will stay around that level, meaning they'll recoup their investment in less than 6 years.

And that doesn't even account for the broad social and environmental benefits of greener housing. For example, green homes have proven to improve a resident's asthma,[24] cardiovascular health, mental health, and other major health issues.[25] Because low-income families have so much to gain from living in healthy, energy-efficient homes, we launched the Enterprise Green Communities initiative more than a decade ago, and today we're working to make green building the norm for our industry.

In recent years, Fannie Mae has been an important partner in that effort. Despite clear evidence of the long-term benefits of green investments, owners and developers often have difficulty securing financing to cover the up-front costs. Fannie is working to solve this problem through its Green Refinance Plus program, which helps owners of affordable multifamily housing access the capital they need to make economically justifiable energy and water retrofits. This also helps Fannie's bottom line: the lower operating costs in green multifamily properties tend to lower the risk of default.

The program is still in the pilot phase, but it has already helped several developers complete energy-efficiency retrofits that otherwise would not be possible. And perhaps most importantly, the program is taking steps toward creating a new industry standard by incorporating future energy savings into the underwriting and physical needs assessments for multifamily developments.

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[23] National Association of Home Builders.“ The Low Income Housing Tax Credit: The Most Successful Affordable Rental Housing Production Program in Our Nation's History”. NAHB.

[24] Tim Takaro, James Krieger, Lin Song, Denise Sharify, and Nancy Beaudet. “The Breathe-Easy Home: The Impact of Asthma-Friendly Home Construction on Clinical Outcomes and Trigger Exposure”. *American Journal of Public Health*, January 2011.

[25] Jill Breysse, David E. Jacobs, William Webber, Sherry Dixon, Carol Kawecki, Susan Aceti, and Jorge Lopez. “Health Outcomes and Green Renovation of Affordable Housing”. Public Health Reports, 2011.

We believe that Congress should pursue similar programs that promote healthy, energy-efficient rental housing with any future replacement for Fannie and Freddie to.

Conclusions and Next Steps

Thank you again for tackling this important issue. The decisions made in Congress today on GSE reform will have a profound impact on the U.S. housing market and the broader economy, so it's important that we get the details right.

A liquid, stable and affordable market for multifamily mortgages is absolutely critical to a well-functioning housing market—and that depends on a limited, explicit guarantee. It's also important that any reform effort preserves other components of the existing system that have proven to work, including Fannie's and Freddie's existing multifamily products and underwriting standards and a clear requirement that investors who benefit from a Government guarantee support affordable rental housing investments.

That said, housing finance reform on its own will not solve all of our Nation's housing problems. We are facing a critical affordable housing crisis in this country, with more than a quarter of renters living one paycheck away from losing their homes, while rental demand is expected to rise exponentially in the coming years. So GSE reform must be part of a series of policy changes and investments to address the needs of low-income families and communities, including preserving and expanding the Housing Credit, reforming rental assistance programs and investing in proven housing and community development programs with adequate appropriations that help communities build capacity to meet their specific housing needs.

I look forward to working with you Chairman Johnson, Ranking Member Crapo, and other Members of the Committee on these and other critical reforms. I appreciate the opportunity to testify today and look forward to your questions.

RESPONSES TO WRITTEN QUESTIONS OF CHAIRMAN JOHNSON FROM THOMAS S. BOZZUTO

Q.1. Can you share with us any recommendations you have regarding the multifamily housing provisions in S.1217?

A.1. As lawmakers look ahead to reforming the housing finance system, NMHC/NAA urge them to recognize the unique needs of the multifamily industry, an industry that provides housing to 35 million Americans. The single-family and multifamily sectors operate differently, have divergent performance records, and require distinct reform solutions. A one-size-fits-all solution will not work. The capital sources for multifamily are not as wide or as deep as those financing single-family, and the loans themselves are not as easily commoditized. In addition, the financing process; mortgage instruments; legal framework; loan terms and requirements; origination; secondary market investors; underlying assets; business expertise; and systems are all separate and unique from single-family home mortgage activities.

Suggested Legislative Recommendations for a Multifamily Title Modeled After the Corker-Warner Bill (S. 1271)

The Corker-Warner bill (S. 1271, *Housing Reform and Taxpayer Protection Act of 2013*), represents one way to go about reforming the existing housing finance system. As currently drafted, the legislation provides more detail on how single-family would operate than on how multifamily would be treated.

General Recommendation

It is important that the multifamily provisions be contained in a separate title, preferably replacing Title VI with language to enable the FMIC to wind down and transfer Fannie Mae and Freddie Mac's current multifamily activities as outlined below. Sections 602 (multiple lender issues) and 603 (GAO report of full privatization of the secondary mortgage market) should be placed in Section VII-General Provisions.

Specific Recommendations

1. **Establish an Office of Multifamily Mortgage Oversight**

   The Corker/Warner bill establishes the FMIC to regulate the housing finance system once the GSEs are wound down and FHFA activities are transferred to the FMIC. This multifamily title of the bill should create an Office of Multifamily Mortgage Oversight within the FMIC to oversee the multifamily housing finance system as defined below.

   Purpose

   - Ensure liquidity to all markets at all times and for a wide range of multifamily property types, transparency, and access to federal mortgage credit to support a robust secondary multifamily mortgage and active multifamily mortgage backed securities.

   Duties and Responsibilities

   - Market Regulator [Sec. 201, 231, 232]
     Statutorily require a separate unit under the jurisdiction of the FMIC that has the capacity to evaluate the overall multifamily market, as well as having expertise in multifamily mortgage underwriting, invesment and securitization. This unit should report to the chief executive and have dedicated research capacity and techincal and capital markets expertise.

- Establish Standard Form Structures, Contracts, Reporting, Data Repository Maintenance [Sec. 202, 223, 224]
  There should be a uniform repository established for multifamily mortgage origination data for properties with 5 or more units. Information collected and made available with appropriate disclosure to investors should include property characteristics, borrower type, principal amount, interest rate, term, amortization, maturity date, and effective prepayment date.

- Establish and Maintain a Separate Insurance Fund for Multifamily Securities [Sec. 203]
  The FMIC Multifamily Insurance Fund will be capitalized by, and exist to exclusively backstop, multifamily mortgage lending and securities activities.

- Establish and Collect Fees in Exchange for Providing Insurance on Principal and Interest of Qualified Securities. [Sec. 203, 204]
  The guarantee fee and other fees to support targeted housing activities shall be collected as a portion of the monthly mortgage payment in the form of an appropriately priced credit enhancement fee that actuarially insures taxpayers against future losses.

- Authority to Protect Taxpayers in Unusual and Exigent Market Conditions [Sec. 205]
  Similar to the authority in Section 205, the FMIC may, upon determination that a material threat exists to the multifamily housing finance system, provide enhanced support to the market for a defined period.

2. Transfer and Continuation of Enterprises' Multifamily Activities to FMIC Office of Multifamily and Successor Entities

The Corker-Warner bill winds down and eliminates Fannie Mae and Freddie Mac's single-family activities. A very different transition process is necessary for multifamily because of the significant differences in capital sources and operations between single-family and multifamily mortgages. This different treatment is further justified by the long track record of strong credit performance in the Enterprises' multifamily programs. (See Appendix I: Overview of Multifamily Capital Sources).

The multifamily industry's ability to develop new properties, as well as to refinance the estimated $100 billion a year in mortgages that come due, relies heavily on reliable and stable access to credit and the existing origination and servicing expertise that is the result of the Enterprises' existing multifamily programs. Material disruptions in the debt capital markets will reverberate through local, regional and the national economies. To avoid this unintended and adverse consequence of housing finance reform, the following actions are recommended to facilitate the wind down and disposition of the Enterprises' multifamily portfolios and the transfer of the mortgage activities to successor entities.

A. As fully described below, the multifamily activities of Fannie Mae and Freddie Mac should be privately capitalized. Furthermore, additional entities should be approved to benefit from a partial government security guarantee.

B. Upon enactment of the *Housing Finance Reform and Taxpayer Protection Act of 2013*, and prior to the certification of the FMIC, each Enterprise will:

   - Establish separate accounting for multifamily activities; and,

   - Continue to reduce their multifamily portfolio and eliminate any portfolio activities other than those necessary to aggregate and facilitate securitization and address troubled mortgage assets.

C. Upon enactment of the *Housing Finance Reform and Taxpayer Protection Act of 2013*, and prior to the certification of the FMIC, each Enterprise will set aside 75 percent of all net proceeds from multifamily mortgage activities into a separate account. These funds are to be used only to assist in the capitalization of the GSEs' multifamily units. Such proceeds are exempt from the Treasury Stock Purchase Agreement and subsequent requirements for transfer of funds by the Enterprises.

D. Each Enterprise will prepare a capitalization plan, including an asset management plan for the existing multifamily mortgage portfolio and guaranteed mortgages. This plan shall be submitted to the FMIC upon its certification.

E. The FMIC will approve or modify the capitalization plans and instruct the Enterprises to implement the capitalization and privatization of each multifamily unit within 12 months of certification. Any extension of the privatization activities will require approval of the FMIC and may not exceed 36 months from the FMIC certification date.

F. Upon successful capitalization, the new entity must repay, with interest at a rate determined by the FMIC, any dedicated revenues held by the government used to collateralize the privatization of the GSEs' multifamily mortgage activities. The repayment term may not exceed five (5) years from initial capitalization.

G. Any revenues not used to capitalize the multifamily activities shall be returned to the Treasury.

H. All multifamily mortgage assets and guaranteed mortgages prior to privatization will transfer to the FMIC.

I. The FMIC will enter into an asset management agreement with the two approved successor entities to oversee the remaining multifamily portfolios and guaranteed mortgage assets at the time of FMIC certification.

J. Until such time as the multifamily activities are capitalized, the FMIC must retain activities to effectively oversee and support future multifamily secondary market financing. These activities include:

- Multifamily issuer, guarantor and associated entity oversight (servicer and special servicer);
- Guarantee Fee administration and assessment;
- Credit policy and regulatory capital oversight;
- Product performance review and approval; and,
- Loan performance, portfolio and security guaranty assessment and market analysis.

Within 12 months of the privatization of the multifamily entities, the FMIC shall publish requirements for successor entities to serve as approved issuers and or guarantors. FMIC shall solicit up to three proposals for successor entities. Upon receipt and review and approval, chosen successor firms will be provided access to the FMIC insurance under the same terms as the prior Enterprises' multifamily mortgage entities.

Assuming the bill adopts the recommended transition approach to multifamily, Title V of S. 1271 needs clarification that any elements referencing wind down and transition outside of the Multifamily Title apply exclusively to the Enterprises' single-family activities. This clarification could be accomplished by adding a general statement as part of the title purpose/preamble that these apply exclusively to the single-family operations of the Enterprises.

3. Definitions

The Corker-Warner bill provides explicit definitions for a variety of components of the new housing finance it envisions. These following definitions must be added to the bill's existing single-family elements to enable the multifamily system to operate within the Federal Mortgage Insurance Corporation.

- ***Approved Multifamily Issuer*** – A FMIC-approved entity to issue eligible multifamily mortgage-backed securities, including those subject to a partial government guarantee. The entity must have contractual access to a dedicated multifamily mortgage origination network that operates nationwide and meets the terms and conditions approved by the FMIC. The entity must: have adequate capacity to implement loan underwriting and due diligence activities; sufficient resources to oversee effective credit policy, mortgage loan purchase and aggregation activities, investor relations, and capital markets; and securitization capacity to issue securities and access appropriate investor markets. [Sec. 2 (2), Sec. 213]

- ***Approved Multifamily Bond Guarantor*** – The term "approved multifamily bond guarantor" means any entity that provides credit enhancement that is approved by the FMIC to guarantee the timely payment of principal and interest on securities collateralized by eligible multifamily mortgages and insured by the FMIC. In cases in which the Issuer has the capital necessary to meet regulatory and corporate capital reserves, the Issuer may serve as guarantor. In such cases, the Issuer and guarantor must have a limited retained portfolio that does not exceed 25 percent of outstanding non-guaranteed securities and mortgages currently held in portfolio, including loans held for aggregation and specialty assets that are not easily securitized but meet a specific public purpose such as student housing and seniors housing. [Sec. 2 (1), Sec. 214]

- ***Approved Primary Servicer*** – An entity that has a contractual obligation to an issuer to collect principal and interest payments, reserves for replacements, escrows and other capital associated with a mortgage note. The entity must also have resources to assess and inspect properties and meet other FMIC-approved terms and conditions. [Sec 2 (4), Sec. 212]

- ***Approved Special Servicer*** – An FMIC-approved entity that has a contractual obligation to the Issuer to service mortgage loans that are delinquent, in default or foreclosure or which do not comply with the terms of the mortgage note. The special servicer may not be affiliated with the guarantor or Issuer.

- ***Covered Multifamily Security*** – A security covered by a guarantee provided by the FMIC and the guarantor by virtue of the fact that the security is exclusively backed by eligible multifamily mortgages as defined by regulation. [Sec. 2 (9)]

- ***Eligible Multifamily Mortgage*** – A mortgage that meets characteristics (i.e., risk profile) defined by regulation. [Sec. 2 (11)]

- ***Multifamily Real Estate*** – Rental property assets of five (5) or more units eligible to collateralize the previously mentioned qualified mortgages.

RESPONSES TO WRITTEN QUESTIONS OF SENATOR WARREN FROM THOMAS S. BOZZUTO

Q.1. According to a September 2012 GAO report, multifamily housing programs played a large role in helping Fannie Mae and Freddie Mac achieve their annual affordable housing goals. As the report states, "multifamily mortgages had a disproportionate importance for the housing goals because most multifamily housing serves targeted groups." Meanwhile, the delinquency rates on the GSEs' multifamily mortgages were extremely low. Even during the height of the housing crisis, less than 1 percent of the GSEs' multifamily mortgages were delinquent. Does this demonstrate that a Government-backed multifamily housing program can pursue affordable housing goals without creating excessive risk of delinquency or default?

A.1. Yes. It's true that multifamily housing is inherently affordable, which played a significant role in the low delinquency rates for the GSEs when it came to multifamily mortgages. In addition, approximately 90 percent of the apartment units the GSEs financed—more than 10 million units—were affordable to families at or below the median income for their community. This included an overwhelming number of market-rate apartments with no Federal rent subsidies that were produced with virtually no risk to Federal taxpayers.

Multifamily Housing Provides a Diversity of Credit Risk

One of the ways the GSEs were able to produce such a stellar performance record in multifamily is by building a balanced book of business where lower-risk, higher quality loans enabled them to take on riskier loans like deeply targeted affordable housing properties, such as Section 8 and Low-Income Housing Tax Credit properties. This diversification of credit risk across the guaranteed portfolio (both securitized and balance sheet) is necessary in order to provide competitive and affordable loans to a wide range of borrowers, properties, and locations.

Many targeted affordable loans have demonstrated strong performance, but due to their income restrictions and other factors, they present greater risk to the lender. Often less experienced and financially strong owners, weaker market locations, and typically higher operating costs are what create greater risk both during the loan term and at maturity. In addition, the value of targeted affordable properties does not typically appreciate like market-rate apartment properties, which adds to the loan maturity risk.

Higher quality loans with lower-risk profiles are not only luxury rental communities, they include a wide range of properties. They can be newer or older, with significant amenities, or their location can be such that amenities are not significant to the value. High quality loans often include properties with rents serving a range of income levels, from workforce households to meeting the housing needs of families with incomes above the area median income. Most properties built after 1980 typically have some set-aside of units that meet the needs of lower-income households.

Multifamily Programs Help To Provide Capital in Underserved Areas

Just as critical, the GSEs' multifamily programs have been able, through their broad platforms, to provide capital for projects located in secondary and tertiary markets that do not meet the credit or return standards required by many private capital debt providers. The GSEs have to vary their portfolio through being active in geographic diversification and do so in as many markets as possible—avoiding any geographic concentration. This has the added impact of providing capital to preserve and support rental housing in these markets. Much of this rental housing is targeted at moderate and lower-income households and is not as focused on meeting goals as it is on providing capital on good quality multifamily properties in sound rental housing markets.

In addition, the extent to which the goals have an impact on the performance of the GSEs needs to be put into the context of a mortgage lender that cannot diversify their debt investments beyond multifamily rental housing. This, along with the goals, creates the need to expand their debt offerings in order to cover a broader range of market locations and meet the needs of borrowers.

Q.2. Could you describe what the multifamily housing market would have looked like—before, during, and after the crisis—if the GSEs had not had affordable housing goals?

A.2. It is difficult to quantify the impact the affordable housing goals have had on the GSEs' multifamily lending activities. The GSEs' affordable housing financing is the result of many factors other than the influence of the Government-mandated goals. Since the early 1990s the primary focus of the GSEs' multifamily financing activities has been on meeting the sector's liquidity needs. It is this comprehensive approach that has had a significant impact on financing workforce and affordable rental housing.

Multifamily Housing Is Inherently Affordable

Without question, an overwhelming number of apartment properties are affordable to households below the area median income. The majority of rental housing units are also affordable at rents between 60 to 100 percent of area median income and the demand for rental housing is only expected to grow in the coming decade and beyond.

The current multifamily lending structure has allowed the GSEs to diversify the risk in their lending activities, giving them greater reach to address affordable housing needs. Without this diversification, the expense associated with higher risk affordable housing would have been higher mortgage costs.

In addition, even when the regulator specifically asked that there be a greater focus on credit, over meeting goals, the GSEs multifamily programs continued to implement sound credit policy and serve the rental housing needs of America's families. All this reflects the strength of the multifamily market and helps emphasize that it is inherently affordable.

It is important to note that certain activities may have been impacted more than others if the affordable housing goals were not in place. For example, a large number of older properties would likely not have received important investments, fewer private activity bonds would have been issued to support low-income rental housing, and owners in secondary markets would not have had access to competitive mortgage capital. Although it would be difficult to quantify, the goals may also have provided additional assistance to both the LIHTC and the Section 8 Project-based housing program.

One thing is clear, multifamily housing's core business practices support lending on workforce housing, and housing in all markets, during all economic conditions. The broad multifamily lending platform has helped the GSEs manage risk and ensured that there was a sufficient supply of liquidity—before, during and after the most recent crisis. It is this comprehensive approach, more than the affordable housing goals that support the production and the preservation of multifamily affordable rental housing.

RESPONSES TO WRITTEN QUESTIONS OF SENATOR COBURN FROM THOMAS S. BOZZUTO

Q.1. In addition to the financing activities of the GSEs, the Federal Government has a number of direct spending programs and tax expenditures to support multifamily housing. An essential component of housing finance reform must be an examination of existing Federal subsidies for multifamily housing. Please identify all of the Federal programs and tax expenditures that support multifamily housing and the total Federal cost of these programs.

A.1. The Federal Government supports rental housing using direct loans, loan guarantees, and grants through a variety of programs designed to support broad and discrete housing needs including senior assisted living, military housing, farm labor housing, low income, and housing for person with disabilities. The primary programs NMHC/NAA members engage with are listed below.

Department	Program	FY2012 Enacted Appropriation (millions)
Department of Housing and Urban Development		
	Federal Housing Administration: Section 221(d)(3) and (4)	[$20]
	Federal Housing Administration: Section 232/223(f)	[$20]
	Section 8: Project-Based Voucher Program	$9,340
	Section 8: Tenant-Based Voucher Program	$18,914
Department of Agriculture, Rural Housing Service		
	Section 538 Loan Guarantee Program	$130
	Section 515 Direct Loan Program	$64.5

Department of Housing and Urban Development

Federal Housing Administration: Section 221(d)(3) and (4): The Section 221(d)(4) program insures mortgage loans to facilitate the new construction or substantial rehabilitation of multifamily rental or cooperative housing for moderate-income families, elderly, and the handicapped. The program insures loans made to nonprofit and cooperatives (Section 221(d)(3) profit-motivated borrowers by private lenders (Section 221(d)(4)).

Federal Housing Administration: Section 232/223(f): The Section 223(f) program insures loans for the purchase or refinancing of existing multifamily rental properties financed with conventional or FHA loans.

Section 8: Project-Based Voucher Program: The PBV Program operates as a contract between a local housing authority and a private property owner, wherein a tenant will pay 30 percent of their monthly income and HUD will pay the remaining cost for that unit. The subsidy remains on the unit for a contractual term, and is not portable with the tenant.

Section 8: Tenant-Based Voucher Program: The Tenant-Based Voucher Program provides a rent subsidy to a family to use for any qualifying rental unit, wherein the family will pay 30 percent of their monthly income toward their rent and HUD will pay the remaining cost for that unit. The subsidy is portable with the tenant, who can move from one property to another and apply their subsidy as appropriate.

Department of Agriculture, Rural Housing Service

Section 538 Loan Guarantee Program: The 538 Program encourages private sector financing for rural rental housing for low- and moderate-income families. Approved activities for financing include construction of new rental housing, acquisition, and rehabilitation of existing rural rental properties, Eligible borrowers for this program include Individuals, general and limited partnerships, corporations, LLC's, trusts, nonprofits, tribes, and public bodies.

Section 515 Direct Loan Program: The 515 Program makes direct, competitive mortgage loans to provide affordable multifamily rental housing for very low-, low-, and moderate-income families, elderly persons, and persons with disabilities. Individuals, partnerships, limited partnerships, for-profit corporations, nonprofit organizations, limited equity cooperatives, Native American tribes, and public agencies are eligible to apply.

[For more information on these programs, please contact the Department of Housing and Urban Development and the Department of Agriculture, Rural Housing Service.]

With respect to tax expenditures that impact multifamily housing, these must be divided into two categories: (1) tax expenditures that are directly targeted to multifamily housing; and (2) tax expenditures that can benefit owners, operators and developers of multifamily housing but are not uniquely designed to benefit the apartment sector (e.g., like-kind exchanges, the deduction for taxes on real property, and the exclusion of capital gains at death). For simplicity's sake, the remainder of our response is focused on the former category.

To identify the tax expenditures specifically targeted to multifamily housing and their cost, we have looked to Estimates of Federal Tax Expenditures for Fiscal Years 2012–2017, which was prepared by the staff of the Joint Committee on Taxation and released February 1, 2013 (JCS-1-13). The value of tax expenditures cited covers the 2013 to 2017 period. Our analysis of this document indicates that the following tax expenditures are directly targeted to multifamily housing:

- Credit for low-income housing ($36.5 billion);
- Exclusion of interest on State and local government qualified private activity bonds for rental housing ($5.2 billion); and,
- Depreciation of rental housing in excess of alternative depreciation system ($21.0 billion).

Q.2. Would you agree many of these Federal programs, such as Low-Income Housing Tax Credits and tax-exempt bonds, have the same purpose and generally overlap one another?

A.2. We would disagree with the premise that many of these Federal programs are duplicative and make the argument that each serves to benefit a segment of renter populations. Accordingly, the various housing programs are actually quite complementary of one another. An analysis of each type of incentive is illustrative.

The tax provision allowing for 27.5-year depreciation of rental property, for example, is designed to enable investors in rental housing to recover the cost of buildings serving the broadest spectrum of renters. Lengthier depreciation schedules would make multifamily housing developments less attractive relative to other types of investments. The provision helps to ensure that the Nation can continue to provide safe and decent housing to 18 million households. It is noteworthy that whereas just 158,000 apartments were delivered in 2012, an estimated 300,000 to 400,000 units must be built each to year to meet expected demand.

Low-Income Housing Tax Credit

Turning to programs targeted to meet the needs of income-restricted residents, the Low-Income Housing Tax Credit (LIHTC) is a public–private partnership program designed to serve families with incomes of 60 percent of area median income or less. As a key driver of the production of affordable units, the vast majority of which would otherwise not be constructed, the LIHTC program has done so admirably, financing more than 2.6 million units since its inception in 1986.

According to a New York University Furman Center for Real Estate and Urban Policy study, *What Can We Learn About the Low-Income Housing Tax Credit Program by Looking at the Tenants?* (October 2012), which analyzes the program's performance in 16 States, 43 percent of LIHTC units serve households with incomes of between 0 percent and 30 percent of area median income.

Section 8 Housing Voucher Program

The Section 8 Housing Voucher Program has long served as America's primary rental subsidy program. Funded by HUD and administered by local public housing authorities, the program provides subsidized rents for qualifying low-income families in private rental housing, including apartments. The Section 8 program is required to distribute 75 percent of vouchers to those with incomes of 30 percent or less of area median income.

This public–private partnership has the potential to be one of the most effective means of addressing our Nation's affordable housing needs and supporting mixed-income communities. However, the program's potential success is limited by too many inefficient and duplicative requirements, which discourage private providers from accepting vouchers. These include a required three-way lease between the provider, resident, and the public housing authority; repetitive unit inspections; resident eligibility certification and other regulatory paperwork. Collectively, these make it more expensive for a private owner to rent to a Section 8 voucher holder.

The program has also been plagued with a flawed and volatile funding system that has undermined private sector confidence in the program. With Congress focused on austerity measures, insufficient funding is expected to be worse in the near-term budget cycles.

Commonsense reforms that could help control costs, improve the program for both renters and property owners and increase private housing participation include: (1) putting a reliable funding formula in place; (2) streamlining the property inspection process; (3) simplifying rent and income calculations; (4) reducing costly Limited English Proficiency (LEP) translation requirements; and, (5) extending the contract term for project-based vouchers from 15 to 20 years. According to the Congressional Budget Office (CBO), these reforms would reduce Section 8 program costs by more than $3 billion over 5 years.

FHA Multifamily Programs

The FHA multifamily programs (Section 221(d)(3) and (4) and Section 232/223(f)) continue to be a credible and reliable source of construction and mortgage debt. FHA not only insures mortgages, but it also builds capacity in the market, providing developers with an effective source of construction and long-term mortgage capital. In normal capital markets, FHA plays a limited, but important, role in the rental housing sector. During the economic crisis, however, FHA became virtually the only source of apartment construction capital. Applications have increased from $2 billion annually to $10 billion, and HUD anticipates that demand for FHA multifamily mortgage insurance will remain high for the next several years.

Since its inception in 1934, FHA has insured over 53,000 multifamily mortgages and has been a cornerstone for the construction and permanent financing and refinancing of apartments. According to HUD, FHA holds approximately 13,000 multifamily mortgages in its portfolio (compared to 4.8 million single-family mortgages). While it accounts for 9.2 percent of the total outstanding multifamily mortgage debt, it is a material and important source of capital for underserved segments of the rental market.

FHA multifamily is best known for offering an alternative source of construction debt to developers that supplements bank and other private construction capital sources. It also serves borrowers with long-term investment goals as the only capital provider to offer 35–

40-year loan terms. FHA lending is essential to borrowers in secondary markets, borrowers with smaller balance sheets, new development entities, affordable housing developers and nonprofit firms, all of which are often overlooked or underserved by private capital providers.

FHA's Multifamily Programs have continually generated a net profit, and have met all losses associated with the financial crisis with reserves generated by premiums paid through the loan insurance program structure. Because premiums have consistently reflected the risk associated with the underlying loans, and because underwriting requirements have remained strong within the program, FHA's Multifamily Programs are able to operate as self-funded, fully covered lines of business at HUD. Some programs have struggled during the real estate downturn, however, any losses have been covered by the capital cushion the multifamily programs collectively generate.

Rural Rental Housing Programs

The Guaranteed Rural Rental Housing Program (Section 538) and Rental Housing Loan Program (Section 515), administered by the Rural Development Housing and Community Facilities Programs within the U.S. Department of Agriculture, are important programs that encourage commercial financing of rural rental housing.

The Section 538 program is focused on affordable housing for low- and moderate-income rental populations. While HUD has several multifamily mortgage insurance programs, none of these programs can take the place of the Section 538 program. HUD's programs are designed for larger, more expensive properties than are generally seen in rural areas.

Section 515 is one of the few resources that enable very low-income and low-income renters in rural America to access decent, safe and affordable housing. The Section 515 program also reduces homelessness and overcrowding.

LIHTC and Tax-Exempt Housing Bonds

Finally, the question above specifically asks whether the LIHTC and tax-exempt housing bonds have the same purpose and overlap. Just as is the case with the various housing incentives, tax-exempt bonds enable a key prong of the LIHTC program, the so-called 4-percent credit, to operate.

The LIHTC has two components: (1) a 9-percent tax credit that subsidizes 70 percent of new construction and cannot be combined with any additional Federal subsidies; and (2) a 4-percent tax credit that subsidizes 30 percent of the unit costs in an acquisition of a project or a new development financed in conjunction with tax-exempt private activity housing bonds.

Whereas States are limited in the amount of 9-percent LIHTCs they may award, there is no limit applicable to 4-percent LIHTCs. Thus, so long as a State has not exceeded its overall cap on private activity bonds, the 4-percent LIHTC program can enable the overall LIHTC program to finance the production of additional units. Investors are willing to accept lower returns applicable to private activity bonds because tax is not owed on interest paid. These lower returns, however, are exactly what make the underlying tax credit projects economical.

Q.3. Would you agree consolidation of these programs could achieve efficiencies with which the Federal Government could do "more with less," i.e., help more families without needing to increase program funding?

A.3. Ensuring taxpayer dollars are utilized in the wisest possible manner must be of paramount concern to Congress and all Americans, particularly at a time of high national deficits. While we welcome the opportunity to work with policy makers to improve the effectiveness of the Nation's housing programs, ensuring all Americans have access to quality rental housing is critical, particularly when current demand for such housing is literally surging and supply is falling short.

Given the discussion above that makes the case that the various housing programs complement one another, we believe that policy makers should look to improve these programs before they look to consolidation. The bursting of the housing bubble exposed serious flaws in our Nation's housing finance system. Yet, those shortcomings were largely confined to the residential home mortgage sector. The multifamily housing programs administered by the GSEs, HUD, RHS, and others worked in concert to meet America's increasing demand for rental housing during the crisis, and continue to address the needs of underserved or unserved populations today. Because the financing structures used by the multifamily industry are often as varied as the properties themselves, programs designed to meet the needs of a certain rental class often do so in the absence of other programs. This dynamic must be acknowledged in any debate over consolidation or elimination of housing programs, taking in to account the populations that stand to be harmed by such actions.

While our testimony before the Committee outlines our recommendations for reforming the Government-Sponsored Enterprises' multifamily programs, we would like to use this opportunity to offer our support to make a critical improvement to the Low-Income Housing Tax Credit (LIHTC) program. As is noted above, the LIHTC is composed of a 9 percent and a 4-percent credit. However, because these rates float and are not fixed, their value can be reduced by as much as 50 basis points, which, in turn, reduces the amount of resources available to finance affordable housing. Notably, in January 2013, Congress enacted the American Taxpayer Relief Act of 2012 that extends the temporary fixed rate on the 9-percent tax credit, which was first enacted as part of the Housing and Economic Recovery Act of 2008, for projects that received a LIHTC allocation prior to January 1, 2014. Given the current low interest rate environment, the actual value of the credit is likely to fall below the 9-percent mark for projects receiving an allocation following the deadline, reducing investors' activity in the affordable housing sector. In fact, in the absence of the temporary 9-percent credit, the credit would actually be worth 7.59 percent as of November 2013. The 4-percent credit is currently worth 3.25 percent.

For this reason NMHC and NAA propose to make the fixed 9-percent credit permanent and to extend the fixed rate policy to the

4-percent tax credit, keeping financing flowing for acquisitions. S.1442, Improving the Low Income Housing Tax Credit Rate Act, introduced by Senator Cantwell, makes these changes, and we urge Congress to enact it as soon as possible.

In addition, NMHC and NAA have continued to support cost effective reforms to the Section 8 Housing Choice Voucher programs.

RESPONSES TO WRITTEN QUESTIONS OF CHAIRMAN JOHNSON FROM E.J. BURKE

Q.1. Can you share with us any recommendations you have regarding the multifamily housing provisions in S.1217?

A.1. The recent financial crisis and recession demonstrated that only the Federal Government can ensure liquidity through all market cycles. The provisions of S.1217 appropriately provide for a Federal backstop to ensure liquidity for multifamily housing finance in all markets. We also support the provision that would require the Federal guarantee to be paid for—thereby helping capitalize the Federal insurance fund, as well as promoting competition among capital sources in the multifamily finance market. In addition, S.1217's approach that preserves and carries over the GSEs' multifamily businesses (e.g., the Delegated Underwriting and Servicing (DUS) and Capital Markets Execution/K-Deal programs), with a Government backstop, would continue to provide liquidity in a broad range of markets, geographic locations, and through various market conditions. We strongly support these provisions.

We note, however, that the multifamily businesses of both GSEs go beyond the DUS and CME/K-Deal programs identified in S.1217. For example, the GSEs operate affordable lending programs with additional lender networks. Thus, we recommend that any legislation specify that the multifamily businesses of Fannie Mae and Freddie Mac be moved over to new or successor entities pursuant to the legislative proposal. By doing so, the activities that the GSEs engage in to serve various geographic regions, specialized housing (e.g., seniors housing, student housing) and smaller properties could be transferred to the entities and serve as a foundation to serve such markets going forward—if so directed by Congress.

We also note that S.1217 provides that the GSE's multifamily businesses would be transferred to the Regulator (FMIC) in their entirety and there would be no private capital at risk for multifamily backed securities. Importantly, legislators should distinguish the roles between the Government guarantor/regulator and private sector participants. The Government agency should retain the role of regulator, Government guarantor and administrator of an insurance fund(s)—but other business roles should be transferred to private sector entities. Specifically, the bill should direct the Government agency to establish/approve multiple (at least two) secondary mortgage market entities to serve as issuers in the multifamily housing finance market. In contrast, S.1217 provides that for single family mortgage loans, these functions would be performed by privately capitalized secondary market entities with access to a limited Government guarantee. Authorizing multiple secondary market entities that pay guarantee fees to access the Government guarantee would foster competition among such entities and with other sources of capital in the multifamily finance market.

Q.2. Each of you propose to establish new issuers in a reformed multifamily housing finance system. Can you discuss how the new issuers will attract private capital, how many you anticipate to form, and how small lenders could participate in this system?

A.2. As we pointed out in our written and oral testimony, there is strong demand for multifamily housing in the U.S. today and this demand is expected to continue for many years to come. To meet this demand, a significant amount of capital must be raised to finance a growing population of renter households. This capital must be longer term in nature. With access to a limited Government guarantee, private issuers can fund a significant portion of their capital structure without being required to pay onerous liquidity premiums that are associated with longer duration liabilities. With strong demand for mortgages and a stable funding source, private capital can focus on managing credit risk instead of managing liquidity risk.

With respect to private capital, we believe that the new issuers should seek to attract private capital in three respects.

First, they should attract private capital to share in the credit risk of the multifamily finance transaction. To the extent that the GSEs' existing multifamily platforms are preserved and carried over into the new system, the new private issuers should be able to continue to attract private capital that provides a buffer to protect taxpayers as part of core business of the new issuers.

Second, the historical credit performance and prospects going forward (dependent on policy maker decisions) will likely attract private investors to fund the capital structure of the new issuers and/or successors to the current GSE multifamily businesses. The existing multifamily books of the GSEs (multifamily loans and securities) could be used to transition to the future state where, for example, the new issuers could earn an asset management fee to help capitalize its new operations.

Third, that the approved new issuers (whether successors to the GSE multifamily platforms or new market entrants) would be able to access a Government guarantee would attract capital to the sector and to the entities themselves. In this regard, we would recommend that the platforms of the new issuers be broad enough (and the regulatory regime be flexible enough) to attract private capital to the new entities. That these entities would be mono-line institutions (in the housing finance sector, whether as multifamily or single-family and multifamily finance entities), charged premiums when accessing the Government guarantee, subject to significant regulation, and required to hold meaningful capital, would appropriately confine their scope. Because private capital is opportunistic, policy makers should exercise care in order to enable the new entities to attract capital and operate as viable entities.

With regard to the number of such entities, we believe that the regulator should be authorized to approve enough entities that would provide stability to the multifamily finance market, but balanced with the goals of competition among the range of capital sources that support this market, as well as the financial viability of approved, privately capitalized entities. At a minimum, we believe there should be no less than two issuers and likely more than two.

For the small multifamily loan market, we would note that there is a significant amount of lending that occurs today. According to MBA research, small multifamily loan lenders (typically, community banks/depository institutions), defined as lenders with an average loan size of $1 to $3 million, made 47 percent of all 2012 multifamily loans (over 19,000 loans; $34 billion in volume) and the very small loan lenders (those with an average loan size of $1 million or less) made an additional 26 percent of all 2012 multifamily loans (approximately 10,800 loans; $6 billion in volume). These loans typically have shorter terms, simpler loan documentation, and often are recourse loans. However, a large portion of this lending is believed to occur in larger, urban markets. Attracting multifamily capital to rural areas or very small markets is difficult today. Part of this difficulty may be attributed to the fact that without access to longer term capital, Community Banks have avoided long term multifamily loans. Other natural sources of long term mortgage capital (Life Insurance Companies and CMBS lenders) have difficulty with the economics of small loans. To remedy this, the Regulator could work with issuers to create programs where local lenders could partner with issuers that either specialize in small loans or offer small loans as part of a broader loan offering.

RESPONSES TO WRITTEN QUESTIONS OF SENATOR WARREN FROM E.J. BURKE

Q.1. According to a September 2012 GAO report, multifamily housing programs played a large role in helping Fannie Mae and Freddie Mac achieve their annual affordable housing goals. As the report states, "multifamily mortgages had a disproportionate importance for the housing goals because most multifamily housing serves targeted groups." Meanwhile, the delinquency rates on the GSEs' multifamily mortgages were extremely low. Even during the height of the housing crisis, less than 1 percent of the GSEs' multifamily mortgages were delinquent. Does this demonstrate that a Government-backed multifamily housing program can pursue affordable housing goals without creating excessive risk of delinquency or default?

A.1. By its very nature, multifamily rental housing tends to be affordable, with 93 percent of multifamily units having rents affordable to households earning area median incomes or less. Overall, renters' median household income is about half of that of homeowners. As a result, the GSEs' multifamily finance activities historically assisted their efforts to meeting the affordable housing goals, particularly when compliance with the affordable housing goals were based on the combined affordability of their single-family and multifamily mortgage purchase transactions. We agree that the GSEs' multifamily businesses have largely been able to meet applicable affordable housing requirements (which have changed over time by regulation or statute) while maintaining strong credit performance—with current delinquency rates at less than 20 basis points.

We support affordability in the multifamily rental housing and believe that new or successor issuing entities should focus on the workforce segment of the multifamily housing market. We recommend an affordability approach in which the vast majority of the annual cohort of an entity's multifamily activities would finance properties with units affordable to families at or below 100 percent of area median income (i.e., the lower half of the income spectrum). Other affordability thresholds also could be appropriate. Overall, we recommend a rational approach that clearly advances policy objectives to support workforce rental housing and provides flexibility, as determined by the regulator subject to market conditions, during periods of market disruption and illiquidity. Affordability standards, including the overall number of such requirements, should also be balanced with the need of the new or successor entities to attract private capital, mitigate potential market distortions, and prudently manage credit risk.

To the extent that Congress establishes new affordable housing goals or other affordability requirements, we would support a regime that would incentivize the new issuers to serve the broad multifamily housing finance market, rather than restricting the entities to narrow market segments. Importantly, neither the statute nor the regulatory regime should be overly prescriptive or excessive in implementing an affordability objective. For example, any affordability requirement should not be structured to apply on a property-by-property basis (such as loan or AMI limits at the property level). In addition, the Government guarantee on a particular transaction or security should not be tied to compliance with a particular affordability standard, as this could create significant uncertainty for investors relying on the security-level guarantee. (If an issuer pays a guarantee fee/premium to the regulator/guarantor for a particular transaction, the guarantee should attach.) The issuer itself would be subject to any governing affordability requirements. We would be pleased to discuss in greater detail possible affordability-related requirements.

Q.2. Could you describe what the multifamily housing market would have looked like—before, during, and after the crisis—if the GSEs had not had affordable housing goals?

A.2. While the affordable housing goals have clearly had an impact on the GSEs and the mortgage market, it is difficult to determine what the market would have looked like absent the goals. This is further complicated by the fact that the affordable housing goals were modified a number of times since they were first statutorily enacted in 1992. A fundamental change also occurred as part of the Housing and Economic Recovery Act of 2008, which decoupled the single-family mortgage housing goals from those that govern the GSEs' multifamily finance activities.

A core strength of the GSEs' multifamily businesses has been that they were a countercyclical source of liquidity to the broad multifamily housing market, including to affordable rental units, while maintaining strong credit and underwriting discipline. The affordable housing goals, along with other mission requirements, influenced the businesses lines to provide liquidity to market segments that, absent such requirements, may not have been pursued, such as mortgages on very low-income properties or loans that were less economically attractive. In the multifamily business lines, the GSEs were largely able to balance the various mission requirements, while running profitable businesses. To the extent that Congress considers any affordability regime, we urge a balanced approach that supports a sustainable multifamily finance system.

Q.3. It appears the GSEs played an important countercyclical role during and after the 2008 housing crisis. In 2009, the GSEs financed about 80 percent of the multifamily loans originated that year—preventing a terrible crisis from getting even worse. But by 2012, the GSEs had reduced their role and were only financing 44 percent of the multifamily loans originated that year. What factors allowed the GSEs to play such an effective countercyclical role?

A.3. The GSEs served a countercyclical role during the financial crisis as providers of liquidity in the multifamily housing finance market, when other capital sources pulled back. And since the crisis, their market share has trended downward, even as overall multifamily origination volumes have increased. As the market has stabilized, other lending sources have increased market share, with non-GSE capital sources competing vigorously with Fannie Mae and Freddie Mac to finance multifamily properties. We believe several factors allowed the GSEs to serve a countercyclical role.

Government Guarantee. A Government guarantee (an explicit guarantee beginning in September 2008) that backed the multifamily finance activities of the GSEs enabled them to provide this countercyclical role in the market. To ensure that there is countercyclical liquidity in the market, the Federal Government should provide a guarantee on mortgage-backed securities. We believe that this Government backstop should be available at the mortgage-backed securities level at all times to ensure liquidity in the multifamily market.

Scalability, Infrastructure, and Expertise. The infrastructure and resources (including their DUS and Program Plus partnerships) of the GSEs were scalable, enabling them to play the countercyclical role that they did during the financial crisis. Such resources include the talent and expertise of their staff that have enabled the multifamily businesses to provide ongoing liquidity, maintain credit discipline, and serve a countercyclical role.

While private capital sources should clearly continue to play a substantial and predominant role in the multifamily finance market (as is increasingly the case), new entities with access to a security-level Government guarantee should have the capability to scale up as necessary when market disruptions occur. This effectively requires that the entities be viable, privately capitalized business that can function during "normal" market conditions as well. The nature of multifamily lending (and commercial real estate finance generally) is such that it is extremely difficult to expand activities in an expedited manner. A mechanism that remains dormant, but called to rapidly expand during market disruptions in order to meet the needs of a deep and complex market, would not be a viable option.

Broad Mission Purposes. The public mission of the GSEs, particularly their "liquidity" mission specified by statute, enabled the GSEs to play a countercyclical role in multifamily finance. The charters of both GSEs specify the following public purposes: (1) To provide stability in the secondary market for residential mortgages; (2) to respond appropriately to the private capital market; (3) to provide ongoing assistance to the secondary market for residential mortgages (including activities relating to mortgages on housing for low- and moderate-income families involving a reasonable economic return that may be less than the return earned on other activities) by increasing the liquidity of mortgage investments and improving the distribution of investment capital available for residential mortgage financing; and (4) to promote access to mortgage credit throughout the Nation (including central cities, rural areas, and underserved areas) by increasing the liquidity of mortgage investment and improving the distribution of investment capital available for residential mortgage financing.

The GSEs' mission—to provide liquidity, stability, and affordability to the residential (both single-family and multifamily) mortgage markets—has remained in effect during the financial crisis. While we do not believe that the status quo should be maintained in the future state of housing finance—and Congress should proceed with deliberate speed to determine the scope and purposes of any future secondary market entities—we believe that a sufficiently broad scope and purpose would be necessary to ensure liquidity in all markets and economic cycles.

Q.4. What steps do you think Congress can take to make sure that some entity—whether it is Fannie Mae, Freddie Mac, or some new entity—plays the same kind of countercyclical role in the multifamily housing market as we move forward?

A.4. All of the factors identified in response to question three above would facilitate the ability of future entities to play a countercyclical role in the multifamily housing market moving forward. In other words, (1) a Government guarantee, (2) scalability, stable infrastructure and multifamily finance expertise, and (3) broad business/mission scope, would all be critically important in ensuring countercyclical liquidity in the future of multifamily housing finance.

In addition, we believe that policy makers should ensure the ongoing stewardship of resources that support the multifamily market, utilizing them to transition to a sustainable multifamily housing finance system. While the current state of the GSEs should not last indefinitely, the resources of the GSEs, as taxpayer assets, should be preserved to support an orderly transition to a new mortgage finance system. The value in the multifamily platforms should be preserved in order to ensure an orderly, stable transition that does not foreclose options for Congress. With the importance of liquidity, stability and affordability in the multifamily housing market, we believe that FHFA, the Administration and Congress should proceed with caution, avoiding risks that come with experimentation. Regulatory or legislative actions that could substantially jeopardize the viability and value of key resources within the GSEs' multifamily businesses should be avoided. Blunt or dramatic changes imposed in conservatorship, for example, would be highly disruptive, risk the loss of significant talent at the GSEs, and reduce the value of taxpayer assets. While policy makers should take steps to facilitate the transition forward, the do no harm principle should equally govern.

RESPONSES TO WRITTEN QUESTIONS OF SENATOR COBURN FROM E.J. BURKE

Q.1. In your written testimony, you supported privatizing the multifamily businesses of the GSEs. Please describe why you believe the Federal Government should not operate a securitization process in the multifamily sector.

A.1. MBA strongly supports an explicit Government guarantee for multifamily loans. We also support an overall approach that supports establishment of premiums paid into a Government-administered FDIC-like insurance fund, oversight by the FMIC as a strong regulator, and recognition of the value and retention of the GSEs' multifamily executions (e.g., Delegated Underwriting and Servicing and Capital Markets Execution/K-Deals).

We believe, however, that the actual business of financing multifamily properties should be performed by private sector entities, and we would urge that the statutory language explicitly distinguish between the roles of the Government guarantor/regulator and new private sector multifamily entities. That is, the Federal Government agency should serve as regulator, guarantor and administrator of an insurance fund—but other roles should be performed by private sector businesses.

Among other things, we believe that the Federal Government's footprint in housing finance should be reduced. Placing and operating the multifamily businesses within a Government agency would be counterproductive toward this objective.

The nature of multifamily finance lends itself to private sector-driven activities. Multifamily loans have much larger balances than single-family mortgages, have heterogeneous collateral and involve in-depth property-specific underwriting. The staff resources and expertise necessary (e.g., underwriters, credit officers, asset managers) would be extensive and would be more efficiently executed by private sector participants, rather than through a large Federal workforce.

Thus, privately capitalized secondary market entities would underwrite (directly and/or through delegation to originators), purchase multifamily mortgages, aggregate loans, manage and distribute credit risk, credit enhance, and structure and issue Government-backed MBS that support the multifamily market. These entities, of course, would be subject to comprehensive regulation by the Government agency/guarantor.

Authorizing multiple secondary market entities—that pay guarantee fees to access the Government guarantee—would also foster competition among such entities and with other sources of capital in the multifamily finance market. By contrast, a Government-run multifamily finance operation would be less nimble and run a greater risk of either crowding out other sources of capital or having a diminished impact.

Finally, the current multifamily platforms of the two GSEs could be transferred into new privately capitalized entities. Moving these businesses to the private sector (through a sale or public offering) with continued access to a Government guarantee would likely return substantial capital to the U.S. Treasury.

RESPONSES TO WRITTEN QUESTIONS OF CHAIRMAN JOHNSON FROM TERRI LUDWIG

Q.1. Can you share with us any recommendations you have regarding the multifamily housing provisions in S.1217?

A.1. We are pleased that S.1217 preserves an explicit, limited and paid-for Government guarantee on qualifying multifamily mortgage-backed securities. That said, we have three serious concerns about the bill's impact on the multifamily market as currently written.

First, as envisioned in the legislation, the Federal Mortgage Insurance Corporation (FMIC) is primarily an insurance and regulatory entity, with no apparent expertise in underwriting, purchasing or securitizing multifamily mortgages. The securitization business requires expertise in identifying and negotiating deals, an intimate knowledge of investor demands and the ability to respond to changes in the market—which are not common characteristics of a typical Government agency. By simply transferring Fannie Mae's and Freddie Mac's current multifamily businesses into the FMIC, Congress would be putting those businesses at risk.

That's why we recommend spinning off Fannie's and Freddie's multifamily businesses into private entities, eventually with the option of purchasing Government insurance on the securities they issue. My written testimony discusses this proposal in more detail.

Second, we are concerned with S.1217's lack of affordability requirements for the multifamily securitization business. We believe that any issuer of Government-guaranteed multifamily securities must have a clear public purpose and be required to serve people across the rental market spectrum, including people in need of affordable housing. Without such a mandate, Congress could meaningfully reduce the availability of affordable rental housing at a time when supply is already dwindling nationwide.

There are several ways to accomplish this goal, but none as clear and fair as a firm requirement. For example, for each issuer at least 60 percent of the units financed by FMIC-insured multifamily securities should be affordable to households earning 80 percent of Area Median Income (AMI) or below. Such a requirement can be enforced efficiently through the annual approval and reporting process for all approved issuers without adding onerous property-level compliance requirements. Again, my written testimony discusses this proposal in more detail.

Third, we are concerned with S.1217's lack of clear incentives to serve traditionally underserved segments of the rental market, including rural and Native American communities, subsidized affordable rentals and small multifamily properties. Today there is very little investment in these market segments beyond the GSEs, and without some sort of incentive or requirement, private capital is not likely to serve these markets.

That's why we recommend establishing a third multifamily issuer that provides access to small banks and community banks, which are most likely to serve smaller and more underserved markets. We also recommend requiring each approved issuer to lay out a forward-looking strategy for serving each of these segments of the market, then report on the results at the end of the year.

Q.2. Can you discuss how Fannie Mae and Freddie Mac currently support/ending to affordable housing, including deals to preserve and improve existing affordable housing, and how these functions can be supported in your proposed new system?

A.2. Fannie and Freddie are critical partners in many of Enterprise's efforts to build and preserve affordable housing. For example, in our mortgage originations business, roughly half of our multifamily production in 2012 went to one of the two companies. Fannie and Freddie offer a range of financing options that make affordable deals possible, including both long-term, fixed-rate loans and shorter-term, floating-rate loans.

In general terms, life insurance companies and CMBS conduits almost exclusively deal with Class A properties, and rarely touch deals that involve Government subsidy. So when financing is needed for those Class B or C properties that serve as "workforce" housing, or for properties involving the Low-Income Housing Tax Credit (also known as the Housing Credit), Section 8 or another form of subsidy, the GSEs and the FHA are often the only execution options.

Nearly every unit of affordable housing created in the U.S. since the late 1980s has been financed through the Housing Credit. These deals involve a long mandatory affordability period, and the long-term, fixed-rate loans offered by the GSEs help make that possible. At the same time, the GSEs' shorter-term, floating-rate loans are useful when a Housing Credit property reaches the end of its affordability period. They help keep the building affordable as the owner recapitalizes.

In addition to their securitization businesses, Fannie and Freddie promote the creation and preservation of affordable housing through structured transactions, credit enhancements on bonds issued by State Housing Finance Agencies and equity investments. Because of their public mission, the companies have helped Enterprise and similar organizations invest in several underserved communities, including rural and Native American communities. Over the past two decades, Enterprise has partnered with Fannie to build or preserve nearly 700 affordable homes on Native Lands, including in South Dakota and Idaho.

Prior to conservatorship, Fannie and Freddie were also key equity investors in the Housing Credit—in addition to providing affordable, long-term debt to make the project pencil out. At one point the two companies accounted for 40 percent of annual Housing Credit investments.

Our proposal maintains these core functions by preserving Fannie's and Freddie's current multifamily products. Both entities—as well as any other approved issuers in the future—would also have a specific requirement to continue serving the affordable segment of the market. They will also be allowed to maintain a limited and carefully monitored investment portfolio for small multifamily loans, Housing Credit equity investments and other investments in affordable housing. My written testimony discusses each of these proposals in more detail.

RESPONSES TO WRITTEN QUESTIONS OF SENATOR WARREN FROM TERRI LUDWIG

Q.1. According to a September 2012 GAO report, multifamily housing programs played a large role in helping Fannie Mae and Freddie Mac achieve their annual affordable housing goals. As the report states, "multifamily mortgages had a disproportionate importance for the housing goals because most multifamily housing serves targeted groups." Meanwhile, the delinquency rates on the GSEs' multifamily mortgages were extremely low. Even during the height of the housing crisis, less than 1 percent of the GSEs' multifamily mortgages were delinquent. Does this demonstrate that a Government-backed multifamily housing program can pursue affordable housing goals without creating excessive risk of delinquency or default?

A.1. Yes. For nearly two decades, Fannie and Freddie have shown that private investors can provide financing to affordable rental housing safely, effectively, and profitably—particularly for people with incomes in the 50–80 percent of AMI range. However, we cannot assume that purely private companies will be willing to serve this segment of the market on their own. We must make it a firm requirement.

The GSE multifamily businesses are able to limit risks to taxpayers through strong underwriting and a high degree of accountability through risk sharing with private investors. Freddie Mac's K-Series deals typically require private investors to cover the first 15 percent of losses in a pool without a guarantee. Fannie Mae holds licensed lenders at risk on a pari passu basis, sometimes with first-loss requirements. Under both models, private capital takes a significant loss before either company has to pay out of pocket. And under the Fannie model, lenders have significant skin in the game, which promotes careful underwriting and servicing of each loan.

Enterprise believes that the Government guarantee can be structured in a way that poses very little risk to taxpayers. That starts with preserving the Fannie and Freddie multifamily businesses as they are today. These models have proven to be safe, effective, and sustainable.

Specifically, any Government guarantee should be limited (with private capital at risk before taxpayers) and paid for through an actuarially sound insurance fee. The Government's multifamily insurance fund should only be tapped when the issuer of the insured security fails and all private at-risk capital is wiped out. In other words, only the security would be backed by the Government, not the institution that issues it.

Under the current "affordable housing goals" system, Fannie and Freddie are expected to finance a certain number of affordable multifamily units each year, as established by their regulator. We recommend tweaking that system in the future, making it a firm requirement for any issuer to maintain their approved status. Each year, each issuer must show that a certain percentage of all multifamily units financed through insured securities are affordable to families earning 80 percent of AMI or below. My written testimony discusses this proposal in more detail.

Q.2. Could you describe what the multifamily housing market would have looked like—before, during, and after the crisis—if the GSEs had not had affordable housing goals?

A.2. By way of background, more than two-thirds of the units financed by the GSEs in recent years were affordable to tenants earning 80 percent of AMI or below, according to our analysis. Between 10 and 15 percent of GSE multifamily units were affordable to people earning less than 50 percent of AMI.

We don't have data on the GSEs' overall share of the affordable market or the affordability of units financed through the purely private execution channels. However, we know that life companies, banks and thrifts primarily deal with Class A properties in first-tier housing markets, and they rarely finance properties that require Government subsidy, such as the Housing Credit or Section 8.

It is unclear how much of this lending activity was due directly to affordable housing goals. That said, there is absolutely no indication that any entity on their own would be willing to finance affordable housing without some additional incentive or an explicit requirement. Indeed, recent analyses from Fannie Mae, Freddie Mac and outside consultants found that, without affordability requirements and access to a Government guarantee on their multifamily businesses, lending for affordable housing at the GSEs would decrease dramatically.

In the absence of specific data, the following is our view on what the market would have potentially looked like without the affordable housing goals:

Before the crisis: In the run-up to the most recent housing crisis, some private investors were willing to enter the affordable segments of the multifamily market, mostly banks, thrifts, and conduits of commercial mortgage-backed securities. However, these investors did not offer the same long-term, fixed-rate products or risk protections as the GSEs (in part because of the affordable housing goals), which eventually led to significantly higher default rates. So we might have seen investment in affordable housing without the goals, but under riskier terms.

During the crisis: Starting in 2008, purely private capital all but abandoned the multifamily mortgage market, as investors were leery of any mortgage debt without a Government guarantee. Even in the midst of the worst housing crisis since the Great Depression, a significant portion of Fannie's and Freddie's multifamily business was affordable to low-income and very low-income families—and there's reason to believe that the affordable housing goals played a role in those business decisions.

After the crisis: Banks, thrifts, and life companies have mostly returned to the multifamily market, but they are less likely to invest in affordable deals. In contrast, the GSEs in 2012 alone financed 675,000 multifamily units that were affordable to people earning

80 percent of AMI or below, and 169,000 units that were affordable to people with incomes at 50 percent of AMI or below. It's reasonable to assume that many of the 80 percent of AMI units, and most of the 50 percent of AMI units were pursued at least in part because of the affordable housing goals.

RESPONSES TO WRITTEN QUESTIONS OF SENATOR COBURN FROM TERRI LUDWIG

Q.1. In your written testimony, you supported new funding for the National Housing Trust Fund and the Capital Magnet Fund by placing a 5–10 basis point tax on all FMIC-insured multifamily securities. However, a number of Federal programs and tax expenditures already target affordable housing. Would you agree adding a new funding stream from a tax on FMIC insured multifamily securities would duplicate tens of billions of dollars in existing Federal resources supporting affordable housing?

A.1. While other meaningful Federal programs exist, the resources available fall well short of the need. By one estimate, only a quarter of eligible low-income families receive rental assistance today, resulting in decade-long waiting lists and sometimes even lotteries for rare openings. In the wealthiest country in the world, people shouldn't have to win the lottery to have an affordable home.

In fact, it's never been harder for working families to find one. According to the Harvard Joint Center for Housing Studies, 27 percent of renters—nearly 11 million renter households—pay more than half their income on housing, often leaving them one paycheck away from losing their home. That's an all-time high. Meanwhile, in housing markets across the country, annual increases in rent are far outpacing increases in wages.

This is especially true for families living in poverty. The number of very low-income renters in the U.S. increased by 17 percent since the crisis began, while the supply of affordable units available to them actually decreased.

The Housing Trust Fund and Capital Magnet Fund focus specifically on serving low-income renters in affordable apartments, which often require some sort of outside subsidy to cover operating costs. They do so by leveraging private capital, which is a cost-effective way to deliver affordable units without deep taxpayer subsidies.

The issuer of an insured security benefits in several ways from the Government guarantee, so it is fair to impose a very modest fee to achieve a broader public purpose. It's also worth noting that both the Housing Trust Fund and the Capital Magnet Fund were created by Congress years ago. As originally envisioned, both funds should have received funding through fees on the GSEs' ongoing business, but those obligations were suspended when Fannie and Freddie were put into conservatorship. So in a way, we're simply proposing that future issuers of insured securities make good on that requirement. The initial fee was set up as 4.2 basis points on ongoing business. We're increasing it slightly to 5 to 10 basis points.

Q.2. You noted in your written testimony rental units for very low-income renters require outside subsidies. To better utilize Federal resources to support affordable, would you support stronger targeting requirements in the Low-Income Housing Tax Credit (LIHTC) program? Tax-exempt rental housing bonds? The Community Development Block Grant (CDBG) program? Please identify other existing Federal programs or tax expenditures you believe could be more adequately targeted or consolidated to streamline Federal assistance for very and extremely low-income borrowers.

A.2. The Housing Credit reaches people who really need it. A recent New York University study on Housing Credit tenant incomes makes clear that 80 percent of households served by these properties are very low income, earning 50 percent or less of Area Median Income (AMI)—and a majority of Housing Credit properties serve households earning less than 40-percent AMI (which is roughly $21,000 on a national basis).

In addition, the National Housing Trust Fund, which was established under the 2008 Housing and Economic Recovery Act, has yet to be funded. It is designed to provide safe, decent and affordable housing for very low- and extremely low-income families through supporting the production, preservation, rehabilitation, and operation of rental homes. Under statute, a minimum of 75 percent of the funds must be dedicated to the needs of extremely low-income families.

Q.3. Enterprise Community Partners is a strong supporter of affordable housing projects. A key component of the company's investments includes Low-Income Housing Tax Credits (LIHTC). An analysis by the Government Accountability Office (GAO) found the LIHTC program to be more expensive per multifamily housing unit than the Section 8 voucher program. Do you agree with GAO's analysis?

A.3. Both the Housing Credit and Section 8 programs are absolutely essential to building and maintaining stable, affordable homes for low-income families. However, the two programs serve different purposes in that effort and often support very different populations. There are several factors that complicate a direct comparison of their per-unit costs.

That said, we find that the Housing Credit is not "more expensive per multifamily housing unit than the Section 8 voucher program" for the following reasons.

First, the GAO study focuses on the all-in cost of building and maintaining a rental unit through each program, not the ultimate cost to taxpayers. Even if the overall costs were higher for Housing Credit-supported units, Federal dollars usually cover a much smaller percentage of those costs compared to Section 8. In fact, the same report found that the Housing Credit program typically costs taxpayers less per unit than the voucher program. Of all the programs analyzed, the Housing Credit had the lowest Federal share of costs.

Second, we have some methodological concerns with the GAO study. The study assumes that tenants of LIHTC and Section 8 units have the same income, which is not the case. In fact, elsewhere in the report the authors acknowledge that voucher recipients' incomes were roughly two-thirds that of Housing Credit residents. That assumption likely inflates the cost to taxpayers of the

Housing Credit program while underestimating the cost of the Section 8 program.

That income disparity remains true today. A recent study by the Furman Center for Real Estate and Urban Policy found that 43 percent of Housing Credit apartments provide housing for extremely low-income households, compared to 75 percent of Section 8 apartments.

ADDITIONAL MATERIAL SUPPLIED FOR THE RECORD

STATEMENT OF THE NATIONAL ASSOCIATION OF HOME BUILDERS

NAHB
National Association of Home Builders

Statement of the
National Association of Home Builders to the

Senate Committee on Banking, Housing and Urban Affairs
Hearing on

"Housing Finance Reform: Essential Elements of the Multifamily Housing Finance System"

October 9, 2013

Written Statement

Statement from the National Association of Home Builders Housing Finance Reform: Essential Elements of the Multifamily Housing Finance System

Introduction

The National Association of Home Builders (NAHB) appreciates the opportunity to submit a statement for the record regarding the future of multifamily finance. NAHB represents over 140,000 members who are involved in building single family and multifamily housing, remodeling, and other aspects of residential and light commercial construction. NAHB's multifamily members build affordable and market-rate rental apartments, and many also actively use the programs of the Department of Housing and Urban Development (HUD) (largely the Federal Housing Administration's (FHA)); the U.S. Department of Agriculture's Rural Development; and the Low Income Housing Tax Credit program in order to help provide decent, safe, and affordable housing to many of our fellow citizens. NAHB's multifamily members also use private sources of capital to finance their properties, including portfolio lenders, insurance companies, pension funds and state and local government housing programs.

As NAHB has testified and provided statements to other committees, NAHB believes that a stable, effective and efficient housing finance system is critical to the housing industry's important contribution to the nation's economic performance and to the achievement of America's social goals. Residential construction - including the building of new structures as well as the remodeling of existing ones - has direct, positive impacts on the U.S. economy. The most obvious impacts are the work opportunities created in the housing industry, as well as in other industries that provide products or services to home builders and buyers. Workers are employed to directly engage in the construction activity. Jobs are generated in the industries where lumber, concrete, lighting fixtures, heating equipment, and other products that go into a home are produced. More jobs are created when real estate agents, lawyers, brokers and property managers provide services to home builders, home buyers and renters. NAHB estimates that the impacts include the following:

- 3.05 jobs from building an average new single family home.
- 1.16 jobs from building an average new multifamily rental unit.
- 1.11 jobs from $100,000 spent on residential remodeling.

As members of Congress and the administration move forward on restructuring the nation's housing finance system, NAHB reiterates its longstanding belief that it is crucial for the federal government to continue to provide a backstop to ensure a reliable and adequate flow of affordable housing credit for both single and multifamily housing. A federal backstop must be a permanent fixture to guarantee a consistent supply of mortgage liquidity, as well as to allow rapid and effective responses to market dislocation and crises.

In NAHB's view, the federal government should provide an explicit guarantee of the timely payment of principal and interest on securities backed by conforming conventional mortgages (single family and multifamily), in the same manner that Ginnie Mae now provides guarantees for investors in securities representing interests in government-backed mortgages. NAHB stresses that the federal government should only be called on under catastrophic situations when the capital and self-funded insurance resources of private secondary market entities are exhausted.

Further, NAHB believes that the U.S. housing finance system should be multifaceted with both competing and complementary components, including private, federal and state sources of capital. The system should support a reasonable menu of sound mortgage products for both single family and multifamily housing, governed by prudent underwriting standards and adequate oversight and regulation.

The focus of the discussion on the future of housing finance reform largely has been on single family homeownership. Less attention has been paid to the multifamily rental housing segment of the housing finance system, even though almost one-third of Americans live in rental housing, and demand for rental housing in the future is expected to increase.

In particular, NAHB estimates that the aging of the "echo boom" generation will result in demand for between 300,000 and 400,000 multifamily housing units on average per year over the next ten years. The timing of this demand will depend on the pace of economic recovery, but the housing needs of these households will not be postponed indefinitely. The current average pace of multifamily housing starts of less than 120,000 annually is insufficient to meet this demand. Production of multifamily housing will undoubtedly increase above the current extraordinary low levels. It is important that the financing mechanisms to support that production are available.

Role of Fannie Mae and Freddie Mac

In spite of the crisis affecting single family housing, the multifamily sector has performed well. Multifamily loans held or guaranteed by Fannie Mae and Freddie Mac (collectively the Enterprises) have very low default rates, and both businesses are profitable. Both of the Enterprises' multifamily businesses involve risk-sharing with private capital, and both businesses have practiced disciplined underwriting. In addition, the multifamily business of the Enterprises finance a wide range of multifamily rental properties, which provide housing for very-low to middle income households.

It is precisely because the Enterprises have built such strong multifamily executions that they have been able to meet the demand for multifamily financing throughout the economic crisis, as other private sources of capital exited. The presence of the Enterprises, as well as FHA's multifamily mortgage insurance programs, has kept the multifamily finance market liquid throughout the economic crisis. In fact, the Enterprises' current multifamily operations seem to embody the principles of safety and soundness with default rates that are exceptionally low and businesses models that are profitable. The taxpayer, rather than having to subsidize the operations, is in fact benefitting from the substantial amount of funds that are being transferred from the Enterprises to the federal government.

It is important to understand that not all private market sources of capital for multifamily financing are available for all segments of the multifamily market. Life insurance companies tend to focus on large projects in the strongest markets (usually urban) and typically serve the highest income households. Once they meet their own portfolio investment targets, life insurance companies retract their lending. Banks do not provide long-term financing and are subject to significant restrictions in terms of capital requirements. While the commercial mortgage backed securities (CMBS) market was significant at one time, it has not recovered from the financial crisis and is not expected to resume its past levels of volume.

These facts point to the need to maintain a viable, liquid and efficient secondary market for multifamily rental financing where the federal government continues to play a role. In addition, the secondary market must be structured to ensure that the appropriate range of products is available to provide the capital needed to develop new and preserve existing rental housing, as well as to refinance and acquire properties. An adequate flow of capital will ensure that demand for rental housing is met and that affordable options are available for a range of households and communities.

Principles for the Future of Multifamily Finance

NAHB and several of the most prominent trade associations representing multifamily developers, owners, property managers and lenders have prepared a set of principles under which we believe the future multifamily finance system should be framed. (The set of principles accompanies this statement.)

Key principles include:

- The nation's multifamily housing finance system should rely primarily on private capital.
- The federal government is the only entity that can ensure the availability of liquidity in all market cycles, and the appropriate mechanism to do that is through a catastrophic backstop role.
- The government guarantee-related market should be subject to strong and independent regulatory oversight and risk-based capital requirements.
- Policy makers should protect and preserve existing resources, as well as support greater transparency, during the transition to an overhauled housing finance system.

NAHB cautions against over-reaching in regard to reforming the multifamily finance system. This component of the nation's housing finance system has performed, and continues to perform, very well. NAHB does not believe it is necessary to take draconian steps that are not needed to "fix" an unbroken system. Such steps would include setting income or rent restrictions on loans as a condition of access to a federal government backstop, standardizing products, or requiring only one securitization platform. NAHB believes that the critical consideration in a new system is broad and continued liquidity during all economic cycles and for all geographic areas.

Legislative Proposals

NAHB recommends establishing a new securitization model for single family and multifamily mortgages where Fannie Mae and Freddie Mac would be transitioned to private housing finance entities that would aggregate mortgages into securities for sale to investors worldwide. Private capital from mortgage originators and securities issuers would be in the first loss position but the principal and interest for investors in the mortgage-backed securities would be guaranteed through a privately capitalized, federally-backed insurance fund. Only mortgages with reasonable and well understood risk characteristics would be eligible to serve as collateral for government-backed mortgage securities and the system would be overseen by a strong and independent regulator.[1]

[1] The full details of NAHB's housing finance system recommendations are contained in "A Comprehensive Framework for Housing Finance System Reform," published by NAHB on February 9, 2012.

NAHB appreciates that S. 1217, the *Housing Finance Reform and Taxpayer Act of 2013*, introduced by Senators Corker and Warner, is consistent with NAHB's views. Of note, the bill recognizes the importance of the Enterprises' multifamily businesses. The bill would transfer both multifamily businesses to the newly created Federal Mortgage Insurance Corporation (FMIC). However, NAHB does not believe it is practical for the regulator to absorb and run the multifamily businesses. A more practical option is to transition the Enterprises' multifamily businesses to private entities, which would then be allowed access to the federal government guarantee through FMIC.

The House Financial Services Committee-passed bill, H.R. 2767, the *Protecting American Taxpayers and Homeowners Act of 2013* (PATH Act), does not address the multifamily conventional market at all. However, the PATH Act does address FHA multifamily; our concerns with these provisions are outlined below.

Federal Housing Finance Agency Concerns

Of great concern to NAHB is that the Federal Housing Finance Agency (FHFA), in the absence of direction from Congress, is seeking to further reduce the Enterprises' multifamily businesses. FHFA is considering limits on product types; restricting available loan terms; simplifying and standardizing loan products; placing limits on property financing; and limiting business activities.

NAHB believes that the FHFA's directive to the Enterprises to further reduce their multifamily businesses beyond the current 10 percent reduction is an arbitrary target and unnecessary. In fact, NAHB strongly believes that it is critical that the Enterprises retain their ability to provide broad liquidity to the market, which includes having a diversified line of products and the ability to address the financing needs for a large range of multifamily property types.

This critical aspect of the Enterprises' mission – to provide liquidity during all economic cycles – should not be regulated by the conservator; that is the job of Congress. To lose any of the successful products or business activities at this point in time – before decisions are made by Congress as to the future of the multifamily housing finance market – means they will have to be rebuilt at a future point. NAHB has urged FHFA not to take unwarranted actions that will result in damage to the multifamily market now and in the future, and NAHB urges members of Congress to convey the same message to FHFA.

The Federal Housing Administration (FHA) Multifamily Mortgage Insurance Programs

The contributions that the FHA has made during this economic downturn underscore the need for a government backstop for both the primary and secondary mortgage markets. In times of crisis, private financial institutions have been unable or unwilling to meet housing capital needs. Without government support for home purchasing and refinancing and for the financing of multifamily rental housing, the nation's mortgage markets will grind to a halt in times of economic stress and uncertainty, throwing the economy back into recession.

In 2008, FHA endorsed just over $2 billion in multifamily loans (excluding health care programs), which grew to $14.6 billion in FY2012. This unprecedented increase in FHA multifamily loan volume occurred as other private market sources of multifamily financing withdrew from the market as economic conditions worsened. FHA, along with Fannie Mae and Freddie Mac, are the primary sources of multifamily financing today. Like in the single family market, the FHA multifamily mortgage insurance programs are fulfilling the function and mission for which Congress originally intended.

FHA historically has played an important role in the financing of multifamily rental housing, and it is especially important now during the current economic crisis. FHA provides an explicit federal government guarantee on multifamily loans for which borrowers pay a mortgage insurance premium set by HUD. The FHA multifamily loans have performed well with low default rates (as published by HUD in May 2013), and the programs generate significant revenue to the federal government in the form of a negative credit subsidy, generating positive cash flow to the U.S. Treasury.

NAHB has long-supported these programs, notably Section 221(d)(4) and Section 223(f), which have enabled the construction of needed affordable and market rate rental housing units over the years, as well as enabled property owners to acquire, refinance, rehabilitate and preserve the nation's existing stock of rental housing. Of importance, FHA financing is often used in smaller markets where Fannie Mae, Freddie Mac and other market participants are less active, and FHA has filled the niche that local banks and thrifts have retreated from in recent years.

It is important to note that over the last three years, HUD has instituted new risk management protocols for the FHA multifamily mortgage insurance programs. The new protocols tightened underwriting requirements and created a national loan review committee. New policies were implemented for large loans, including higher standards for sponsor creditworthiness and experience. Processes and procedures throughout the field offices have been strengthened and standardized. There is closer scrutiny on market strength and FHA presence than before the economic crisis struck.

In addition, HUD revised and tightened lender capitalization, licensing and monitoring requirements, made significant changes as part of the update of the loan closing documents, and finalized several changes to the multifamily mortgage insurance program regulations. Last year, HUD raised the mortgage insurance premiums for programs in the General Insurance/Special Risk Insurance (GI/SRI) fund. This was the first premium increase in 10 years for these programs. Additionally, a new Concentration of Principal Risk policy was implemented which described the procedures lenders must follow to obtain prior approval for borrowers (principals) with greater than $250 million of outstanding FHA-insured debt who plan to submit applications for new loans. Under the new policy, lenders are required to conduct a complete mortgage credit review of principals who meet the threshold.

All of these actions were intended to strengthen risk management practices related to the FHA multifamily mortgage insurance programs, ensure the health of the GI/SRI fund, and attract high quality borrowers, without taking market share from the private sector or endangering taxpayers. NAHB has been actively engaged in working with the department as these requirements have been implemented. Although NAHB has not agreed with every action taken, overall we have supported HUD's objectives and have worked to ensure that borrowers and lenders understand the changes.

HUD's most recent step towards increasing efficiency, further streamlining processes and procedures, and standardizing policies across field offices was the announcement of a major restructuring of the Office of Multifamily Programs. The restructuring in the Office of Multifamily Programs will consolidate its program Hubs and field offices and reorganize the offices within its headquarters in Washington, D.C. The goal of the restructuring is to allow more consistent, efficient processing of loans and servicing of existing assets. A major goal is to even out workloads and ensure that the staff expertise needed to process complex multifamily loans is in place in each Hub and field office.

NAHB has testified previously that, as important as these steps have been towards increasing risk management, the FHA multifamily field offices continue to struggle because of inadequate staffing and resources. NAHB is supportive of HUD's efforts to address these difficult issues, and we urge members of Congress to ensure that the department has the resources it needs to safely and properly manage its large portfolio and to ensure that the programs remain strong and viable.

NAHB expressed great concern to members of Congress recently that the uncertainty related to the availability of commitment authority for the FHA multifamily programs creates the potential for great disruptions in financing important affordable and market-rate rental properties, as well as health care facilities, which are also included under the GI/SRI fund. FHA exhausted its commitment authority for FY2013 in mid-September, which has forced borrowers to wait until new authority is available before they can be assured of a loan commitment. This means needed affordable housing and construction and other related jobs are being delayed, and in some cases, may not even go forward. The government shutdown only makes the situation worse, as the queue of loans waiting for commitment authority is accumulating rapidly and is now in excess of over one-half billion dollars.

NAHB suggests that an area of reform for the FHA multifamily and health care insurance programs is to consider giving FHA multi-year commitment authority, as is the case with the FHA single family programs. Another option would be to devise an automatic trigger of additional commitment authority if certain conditions are met to ensure the uninterrupted operation of the programs during all economic cycles.

PATH Act Proposals

NAHB is concerned about proposals to more narrowly limit FHA's current mission. The PATH Act, recently passed by the House Financial Services Committee, would allow FHA to provide mortgage insurance for residential properties having five or more dwelling units – multifamily rental housing – subject to occupancy and rent restrictions which are applied during the life of the mortgages. The bill restricts occupancy to families having incomes no greater than 115 percent of area median income (AMI). It allows for higher income limits (up to 150 percent of AMI) in high cost areas. The bill gives FHA the discretion to establish lower occupancy, income and rent restrictions.

NAHB does not support setting occupancy and rent restrictions based on AMI for the FHA multifamily mortgage insurance programs. The Census Bureau's 2012 Rental Housing Finance Survey shows that an overwhelming majority of tenants in properties with FHA-insured mortgages have incomes of 115 percent or less of area median income. However, the FHA multifamily mortgage insurance program is also a key source of liquidity, so the imposition of income limits would impede that portion of FHA's mission, particularly in higher-cost markets.

The FHA multifamily mortgage insurance programs are subject to statutory mortgage loan limits, which effectively serve to focus the provision of FHA multifamily mortgage insurance on affordable and workforce rental housing. Imposing burdensome provisions that require developers, lenders and property managers to track and document incomes and rents on unsubsidized properties is costly and unnecessary, given that the proposed targeted population is already being served by the programs.

Conclusion

NAHB thanks the Committee for the opportunity to submit its views on the future of the multifamily finance system. Whether they rent or own, Americans want to choose where they live and the type of home that best meets their needs. Rental housing is a choice for millions from all ages and walks of life. We appreciate that Congress is taking a closer look at this important sector of the housing finance system.

Given the significant role that housing plays in the economy, we urge Congress to take a long-term, holistic approach to housing finance reform. NAHB also urges Congress to carefully consider the differences between the single family and multifamily market and not apply solutions to one piece of the market that are not appropriate for the other.

NAHB thanks the Committee for its leadership on this important issue, and stands ready to work with you to achieve such reforms and provide much-needed stability for this critical sector of the economy.

PRINCIPLES FOR MULTIFAMILY HOUSING FINANCE REFORM AND THE GOVERNMENT SPONSORED ENTERPRISES

Principles for Multifamily Housing Finance Reform and the Government Sponsored Enterprises

Our organizations respectfully request that policy makers address the needs of the multifamily rental housing sector as a fundamental component of any effort to reform the American housing finance system and the activities of the government sponsored enterprises. While each organization may have a policy viewpoint on multifamily housing reform, we collectively agree with the key principles that follow.

Overview

More than one in three American households rent their home, and the Federal Government estimates that between 16 million and 17.4 million[1] of those households live in multifamily rental housing, a development with five or more units. Renters include workers who want to live near their jobs, young professionals, empty-nesters, retirees on a fixed income, families with children, students, and households who value the convenience and mobility that renting offers. Notably, the vast majority of multifamily rental housing provides homes for households earning modest incomes, with 93 percent of multifamily rental apartments having rents affordable to households earning at or below the area median income.[2] This underscores the importance of reliable debt financing for this market, which is estimated to have been in excess of $140 billion for 2012.[3]

Capital sources that finance the multifamily housing market include Fannie Mae and Freddie Mac (GSEs), life insurance companies, commercial banks, commercial mortgage-backed securities (CMBS) issuers, REITs, pension funds, the Federal Housing Administration's (FHA) multifamily programs and others. While all sources play an integral role in supporting the multifamily market, each has its own focus, strength, and limitations. Importantly, when most private capital sources exited the multifamily finance market during the recent economic downturn, the GSEs and FHA, with their government backing, continued to provide liquidity during this period of unprecedented market disruption.

As policy makers deliberate the future of the government's role in the secondary market for multifamily mortgages, it is vital they ensure that capital continues to be available in all markets.

Key Principles

Recognizing the unique attributes of the multifamily market, our respective organizations, representing lenders, owners, operators, and developers of multifamily housing, recommend that policy makers pursue the following principles in shaping

1 2011 American Housing Survey and 2011 American Community Survey, 1-year Estimates updated September 2012, US Census Bureau.

2 Joint Center for Housing Studies tabulations of 2009 American Housing Survey, US Census Bureau.

3 Total 2012 multifamily originations are currently estimated to have been $140 billion, with institutional multifamily lending accounting for $105 billion of the total. 2013 Commercial Real Estate Finance Forecast, Mortgage Bankers Association.

MBa MORTGAGE BANKERS ASSOCIATION

NMHC National Multi Housing Council Apartments: Smart Communities, Smarter Living

NAHB National Association of Home Builders

NAA National Apartment Association

American Seniors Housing Association

the government's role in the multifamily housing finance system.

1. **Our nation's multifamily housing finance system should rely on private capital.** Private capital should be the primary source of financing for multifamily rental housing. Private capital has historically been brought to bear through the range of lending institutions that have supported multifamily finance, such as portfolio lenders and CMBS issuers, the GSEs' multifamily programs that require loss sharing with originators and with investors, and the capitalization of the GSEs themselves. Government policies should maintain this reliance on private capital going forward.

2. **Past experience shows that the federal government is the only entity that can ensure the availability of liquidity in all market cycles.** The recent credit crunch and recession demonstrated that only the federal government can ensure liquidity through all market cycles, and as demonstrated by the conservatorship of Fannie Mae and Freddie Mac, as well as programs like TALF and the Federal Reserve's asset purchases, the federal government will fill this role when necessary. Government policies should anticipate and prepare for this role.

3. **The government should ensure liquidity for multifamily mortgages through a carefully crafted guarantee on multifamily mortgage-backed securities.** The federal government should provide a catastrophic backstop guarantee on mortgage-backed securities. The catastrophic backstop role would be similar to that of the U.S. government in a number of sectors and markets, including federal deposit insurance in the banking system. This government backstop should be available at the mortgage-backed securities level (rather than at the level of the issuer, as it is today with the GSEs) at all times to ensure liquidity in the multifamily finance market.

4. **Taxpayers and the mortgage finance system itself should be protected through a strong regulatory framework and multiple layers of private capital.** To protect taxpayers and the system itself, the government-guarantee-related market should be subject to strong and independent regulatory oversight and risk-based capital requirements. Taxpayers also should be protected through multiple layers of private capital, including the equity in the multifamily property itself and the entity-level capital of the security-issuing entity and any risk sharing it may undertake. A federal risk insurance fund should also be established, capitalized by risk-based premiums paid by participating firms. Only when all layers of capital are exhausted would a draw on the U.S. Treasury be authorized.

5. **Policy makers should protect and preserve existing resources, as well as support greater transparency, during the transition to an overhauled housing finance system.** Given the significant role of the GSEs in the multifamily market, their infrastructures, capacities and resources should be carefully managed to avoid disrupting capital flows, as well as to ensure an orderly transition to a new housing finance system. Additionally, prudent management of existing multifamily mortgage portfolios is important due to its quality and positive cash flow. Greater understanding of the performance and role of the government in the multifamily mortgage market, especially as private capital re-enters is important. To support this understanding, enhanced transparency through expanded reporting and information about the GSEs' multifamily activities will serve policymakers in their decision-making about the future state of housing finance.

We underscore that as policy makers deliberate the future of the government's role in multifamily housing finance, it is vital they ensure that capital continues to be available to support this essential source of housing.