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Government-sponsored enterprises at the crossroads

The value of the Treasury's interest in the GSEs should be used to increase affordable housing and advance racial equity, and the GSEs should be regulated as utilities

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ABSTRACT

More than a dozen years after the government-sponsored enterprises (GSEs) were rescued and placed into conservatorship their future operation is still being determined. The government's assistance to the GSEs and their subsequent return to profitability have created up to $100 billion of value held by the U.S. Treasury. That money should be used to make an historic investment in addressing the affordable housing crisis and advancing racial equity in housing. In addition, the GSEs should operate as utilities to best serve these goals as well as their overall mission to support the financing of the nation's housing.

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CONFLICT OF INTEREST DISCLOSURE

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EXECUTIVE SUMMARY

Fannie Mae and Freddie Mac (the government-sponsored enterprises, or GSEs) play a foundational role in the U.S. housing market, providing financing to lenders for nearly half of current U.S. mortgages by buying the mortgages from lenders and packaging and selling them to investors. This makes mortgages cheaper and more available across the country.

During the housing boom of the 2000s and the crash in 2008, the GSEs were woefully undercapitalized. They were rescued by the federal government and placed into conservatorship with strict oversight by their regulator the Federal Housing Finance Agency (FHFA). Subsequently, multiple proposals emerged to restructure or replace the GSEs to reduce their risk of failure and advance the public mission that is the basis for their public support. While administrative reform of the GSEs has been ongoing since conservatorship began, in the past year FHFA has hastened the process of releasing them from conservatorship.

Any changes to the GSEs' structure or operation will determine how well they are able to serve their public mission. These changes are taking place in the context of the current COVID crisis, a long lasting and broad affordable housing crisis, and a national reckoning on historic and ongoing racial discrimination. As discussed in this paper, several essential steps are necessary for the GSEs to best serve their important role.

Conservatorship has created an historic opportunity for addressing the nation's affordable housing crisis and advancing racial equity in housing. As part of the assistance plan for the GSEs, the government received stock interests in the GSEs, now valued at $48 to $98 billion by the Congressional Budget Office.[1] The value of these assets comes from fees collected from GSE loans and that value should remain in the housing market to further affordable housing. In particular, the government's stock interests in the GSEs should be exchanged for a comparable commitment by the GSEs of additional affordable housing measures and a restorative justice housing program that provides targeted down payment and other assistance aimed at closing the racial homeownership gap.

While most home values and equity rebounded from the 2008 recession and withstood the COVID crisis, many families have struggled, particularly lower wealth families and families of color. A widespread affordable housing crisis limited opportunities for many across the country going into the COVID crisis, with homeownership far below pre-housing boom levels and more than 20 million families struggling with unaffordable rent.[2] Conditions worsened in 2020.

A primary statutory purpose of the GSEs is to advance affordable housing. While the GSEs have maintained their affordable housing programs in recent years, conservatorship has constrained these activities. The GSEs have operated with limited capital at a time when the country needed substantially increased focus on and support of affordable housing from the GSEs. Now they must greatly increase their work to meet the country's pressing affordable housing needs.

The past year has also seen a national reckoning on the history and continuation of racial discrimination, exclusion, and segregation in our country. Systemic racial barriers exist in all facets of American life, including policing, healthcare, and housing. The housing market profoundly manifests these barriers, including in the huge gap between white homeownership, at 72%, and Black and Latino homeownership, at 42% and 48% respectively.[3] This disparity is as great as that existing before the passage of the Fair

[1] Congressional Budget Office, *Effects of Recapitalizing Fannie Mae and Freddie Mac Through Administrative Actions* (August 2020), available at https://www.cbo.gov/system/files/2020-08/56496-GSE.pdf.

[2] Joint Center for Housing Studies at Harvard University, *State of the Nation's Housing 2020*, available at https://www.jchs.harvard.edu/sites/default/files/reports/files/Harvard_JCHS_The_State_of_the_Nations_Housing_2020_Report.pdf

[3] Alanna McCargo and Jung Hyun Choi, *Closing the Gaps: Building Black Wealth Through Homeownership*, Figure 3, Urban Institute (November 2020), available at https://www.urban.org/sites/default/files/publication/103267/closing-the-gaps-building-black-wealth-through-homeownership_0.pdf.

Housing Act in 1968 and even going back to the 1890s.[4] For the GSEs, only a small percentage of their home purchase loans have gone to Black and Latino homebuyers in recent years, with less than 5% of their loans made to Black families in 2019.[5] The GSEs' charters include a duty to advance fair lending and equity, and much more has to be done by them to advance that national responsibility.

The success of the GSEs in conservatorship – in which they have operated as de facto utilities and stabilized the housing market following the 2008 housing crash – establishes that utility oversight is the best structure for the GSEs going forward. During the COVID public health and economic crisis, a utility structure has enabled the GSEs to provide critical relief to the housing market and the overall economy – assistance that was possible only due to the GSEs' special status, their substantial resources, and the enhanced oversight authority granted to FHFA under conservatorship. A utility structure should be implemented permanently in order to secure the GSEs as an emergency backstop during a crisis, enhance operation of the GSEs in regular times, and advance the GSEs' public mission.

Increased affordable housing support, racial equity programs and utility oversight should be solidified and formalized during conservatorship while the GSEs build up capital. It is critical for these reforms to be implemented before release of the GSEs occurs. While GSE reform can be implemented legislatively or by administrative action, enacting GSE legislation has proven difficult. Thus, continuing administrative reform is more likely. Central to the reform process is resolution of the GSEs' obligations for the aid it received following the 2008 crisis and the ongoing backup support the government will continue to provide in the future. Any amendments to the documents governing these issues will lock in the terms of the GSEs' operation and obligations going forward and will be difficult to change. Thus, bolstered affordable housing and racial equity measures and utility oversight must be baked into these steps.

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4 Adam Levitin, *How to Start Closing the Racial Wealth Gap*, The American Prospect, June 17, 2020, available at https://prospect.org/economy/how-to-start-closing-the-racial-wealth-gap/; Alanna McCargo and Jung Hyun Choi, *Closing the Gaps: Building Black Wealth Through Homeownership*, Figure 3, Urban Institute (November 2020), available at https://www.urban.org/sites/default/files/publication/103267/closing-the-gaps-building-black-wealth-through-homeownership_0.pdf; *see also* Laurie Goodman, Jun Zhu, and Rolf Pendall, *Are Gains in Black Homeownership History?*, Urban Institute (February 14, 2017), available at https://www.urban.org/urban-wire/are-gains-black-homeownership-history.

5 *See* FHFA Annual Housing Report, at p. 11, Table 6 (October 2020), available at https://www.fhfa.gov/AboutUs/Reports/ReportDocuments/Annual-Housing-Report-2020.pdf (noting that in 2019, 4.8% of Fannie Mae and 3.6% of Freddie Mac loan purchases were from Black borrowers, and 12.1% and 9.4% were from Latino borrowers).

The GSEs' path to conservatorship

The GSEs were created with special charters and privileges to carry out a public mission of supporting the overall mortgage market, advancing affordable housing, and ensuring racially inclusive lending. Prior to Fannie Mae's creation in 1938, mortgage credit was often constricted and unduly expensive in many parts of the country. Today, by buying loans from many lenders in different parts of the country, packaging them into mortgage-backed securities, and guaranteeing the payment of the interest and principal to investors, Fannie and Freddie support a deep and liquid market for these securities. Consequently, the GSEs reduce costs to homeowners and enabled the wide availability of the 30-year, fixed-rate, freely prepayable mortgage.[6]

The GSEs support affordable housing through several measures.[7] Consistent with their role as quasi-insurance companies, the GSEs pool risk nationally. This reduces the difference in the fees charged to different groups of borrowers, thus lowering the amount of the extra charges assessed to lower wealth borrowers with lower down payments and credit scores. The GSEs also engage in special lending programs and outreach targeted to affordable housing borrowers and underserved markets. For many years, they have contributed hundreds of millions of dollars to affordable housing funds through a statutory assessment.[8] In the 1990's the GSEs substantially contributed to an expansion of sustainable homeownership, broadly and particularly for families of color, measurably helping to increase homeownership for Black and Latino families to nearly 50% before the subprime crisis.[9] Finally, they purchase and securitize multifamily loans, financing over 40% of multifamily lending.[10]

However, there is a tension in the structure of the GSEs and their public mission. They have operated as privately-owned shareholder corporations, and accordingly have a duty to serve the interests of their shareholders, including maximizing returns, yet they are granted special privileges and have a public mission. At times, the GSEs have used their special status granted by the government to unfairly benefit their shareholders, disadvantage other participants in the housing market, and put taxpayers at risk. In addition to the critical government backing of the GSEs that reassures investors in their mortgage securities and supports the foundation of their business, the GSEs enjoy numerous other market advantages unavailable to other market participants.[11] These advantages include an exemption from

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[6] National Housing Act Amendments of 1938, Pub. L. 75-424 (Feb. 3, 1938); Mike Konczal, *In Defense of the 30-year Mortgage*, Washington Post, August 10, 2013, available at https://www.washingtonpost.com/news/wonk/wp/2013/08/10/in-defense-of-the-30-year-mortgage/.

[7] The Federal Housing Enterprises Financial Safety and Soundness Act of 1992 amended Fannie and Freddie's charters, requiring them to meet an affirmative obligation to facilitate the financing of affordable housing for low-income and moderate-income families. In 1995, U.S. Department of Housing and Urban Development (HUD) began to require the GSEs to meet certain mortgage purchase goals each year. For additional information on the history of the GSEs, see FHFA Office of Inspector General, *A Brief History of the Housing Government-Sponsored Enterprises*, available at https://www.fhfaoig.gov/Content/Files/History%20of%20the%20Government%20Sponsored%20Enterprises.pdf; Theresa R. DiVenti, *Fannie Mae and Freddie Mac: Past, Present, and Future*, United States Department of Housing and Urban Development, Office of Policy Development and Research, Volume II, Number 3 (2009), available at www.huduser.org/periodicals/cityscpe/vol11num3/ch11.pdf.

[8] The Housing and Economic Recovery Act of 2008 created the National Housing Trust Fund and Capital Magnet Fund. The law requires the GSEs to set aside 4.2 basis points for each dollar of unpaid principal balance on total new loan purchases, which are then allocated to the two funds. 65% is allocated to the Housing Trust Fund and 35% to the Capital Magnet Fund. *See* 12 U.S.C. §§ 4567-4569. However, after the GSEs were placed in conservatorship in 2008, former FHFA Director Edward DeMarco suspended the allocation of funds pursuant to section 4567(b) of HERA. On December 11, 2014, former FHFA Director Mel Watt lifted the suspension and directed the GSEs to begin setting aside and allocating funds. *See* FHFA, *Fannie Mae and Freddie Mac Affordable Housing Allocations*, available at https://www.fhfa.gov/PolicyProgramsResearch/Policy/Pages/Fannie-Mae-Freddie-Mac-Affordable-Housing-Allocations.aspx.

[9] *See* Brent W. Ambrose, Thomas G. Thibodeau, and Kenneth Temkin, *An Analysis of the Effects of the GSE Affordable Goals on Low- and Moderate-Income Families* (May 2002), available at https://www.huduser.gov/Publications/pdf/gsegoals.pdf ("In analyzing homeownership rate changes between 1991 and 1997 in 80 cities, we found that the GSEs, by purchasing loans originated to low-income families, helped to reduce the disparity between homeownership rates for low-income and higher income families.").

[10] *See* Remarks from Eric S. Rosengren, President and Chief Executive Office of the Federal Reserve Bank of Boston, *Trends in Commercial Real Estate*, May 9, 2017, at p. 3, available at https://www.bostonfed.org/news-and-events/speeches/2017/trends-in-commercial-real-estate.aspx (stating that the GSEs, including their securitized vehicles, hold or guarantee approximately 44% of multifamily loans).

[11] Prior to 2008, private investors assumed that the government stood behind GSE MBS with an implicit guarantee – that is, in an economic crisis, the government would be compelled to honor the guarantee. This implicit government backing lowered the GSEs'

security filing requirements at the state and federal level for their mortgage backed securities (MBS). The GSEs are also exempt from state income tax and general regulation. During their existence they have accumulated valuable data, infrastructure, and intellectual property, far beyond the scope of private participants in the mortgage market. These advantages are extraordinarily valuable in a time when big data and analytic capacity are key determinants of success in the financial markets.

The tension between public mission and maximizing private gains brought down the GSEs in the housing boom of the 2000s. The GSEs' targeted annual rates of return were unchecked, approaching 20%, and they took on too much risk.[12] First, the GSEs began holding loans, senior tranches of subprime private-label securities, and their own mortgage securities in portfolio rather than selling them to investors. Although it distorted the market, these large, retained portfolios, $1.6 trillion between both GSEs, enabled them to arbitrage their lower cost of borrowing due to their implicit government guarantee and maximize their earnings.[13] Subsequently, in the early 2000s the housing market was transformed by unsustainable subprime and alternative (Alt A) mortgages packaged into private label securities. Initially, the GSEs resisted this lending as it did not meet their underwriting standards. After losing much of their market share to these loans, they misguidedly facilitated subprime lending by buying the senior tranches of these securities and directly funding no-document Alt A loans.[14] Alt A loans were 10% of the GSEs' business but were responsible for half of their losses in the financial crisis, pushing the GSEs into conservatorship and requiring massive government assistance. The subprime lending boom devastated low and moderate-income communities and borrowers of color, and these toxic loans and associated speculative financial instruments pushed the entire U.S. economy into a deep recession.[15] Many communities and families have yet to recover.

In September 2008, the federal government stepped in using its authority under the Housing and Economic Recovery Act of 2008 (HERA), which had been enacted in July 2008. It placed the GSEs into conservatorship and began a program of massive infusions of capital, providing hundreds of billions of dollars of equity and backup commitments and purchases by the Federal Reserve of GSE mortgage securities to support their price.[16]

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funding costs. In 2008, FHFA placed the GSEs in conservatorship and Treasury purchased a large stake in the GSEs' common stock. In the PSPA agreements between FHFA and Treasury, Treasury agreed to bear GSE losses in exchange for all GSE profits. These agreements act as an explicit government guarantee to GSE MBS holders during conservatorship. *See* Wayne Passmore and Alexander H. von Hafften, *GSE Guarantees, Financial Stability, and Home Equity Accumulation*, Federal Reserve Bank of New York Economic Policy Review 24, No. 3 (Dec. 2018), available at https://www.newyorkfed.org/medialibrary/media/research/epr/2018/epr_2018_gse-guarantees_passmore.pdf.

[12] Eric Stein and Bob Ryan, *Treat the GSEs as Utilities*, Center for Responsible Lending (March 2020), at p. 3, available at https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-gse-utilities-report-mar2020.pdf

[13] The GSEs grew enormous portfolios, deriving much of their profit from them and underpricing their guarantee fees in order to obtain more loans. In 2008, Fannie Mae held $729 billion in mortgage assets and Freddie Mac held mortgage assets value at $805 billion. *See* Congressional Research Service, *Fannie Mae and Freddie Mac in Conservatorship: Frequently Asked Questions*, Updated May 31, 2019, at p. 16, available at https://fas.org/sgp/crs/misc/R44525.pdf.

[14] The GSEs were found to be contributors, though not the leads in the unsustainable lending that caused the housing crisis. *See* Financial Crisis Inquiry Commission, *The Final Report of the National Commission on the Causes of the Financial and Economic Crisis in the United States* (2011), available at https://www.govinfo.gov/content/pkg/GPO-FCIC/pdf/GPO-FCIC.pdf. Controls have been established to prevent a recurrence of such lending through the CFPB QM rule and strong oversight of the GSEs by FHFA.

[15] Debbie Gruenstein Bocian, Wei Li, Carolina Reid, and Roberto G. Quercia, *Lost Ground: Disparities in Mortgage Lending and Foreclosures*, Center for Responsible Lending (2011), available at http://www.responsiblelending.org/mortgage-lending/research-analysis/Lost-Ground-2011.pdf (finding that Black Americans and Latinos were consistently more likely to receive high-risk loan products, even after accounting for income and credit status); Center for Responsible Lending, *The Spillover Effects of Foreclosures* (Aug. 19, 2013), available at https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/2013-crl-research-updateforeclosure-spillover-effects-final-aug-19-docx.pdf (finding that communities of color have lost or will lose $1.1 trillion in home equity as a result of spillover from homes that have started the foreclosure process).

[16] For the GSEs, when they were placed into conservatorship the Treasury initially agreed to provide lines of credit of $100 Billion each to Fannie and Freddie. In exchange, the GSEs each issued $1 Billion of senior preferred stock and provided warrants for up to 79.9% of the GSE's common stock. In addition, the Treasury received a "liquidation preference" equal to the amount of new capital infusions from the line of credit and the GSEs were required to in addition pay 10% annual dividends based of the value of the liquidation preference. In May 2009, the lines of credit for each of the GSE were doubled to $200 billion each and pursuant to a subsequent amendment the total lines of credit expanded to $445.5 billion, of which $191 billion has been drawn, and $254 billion remains available. In addition to this support, the Federal Reserve has purchased GSE MBS and bonds to stabilize those markets. By the end of 2011, the 10% dividends totaled nearly $19 billion per year and were being added to the total outstanding on the line of credit since the GSEs were not then producing a profit. In August 2012, the terms were again amended with the 10% annual dividend being replaced by a "net sweep" under which all profits of the GSEs were due to Treasury as a dividend, indefinitely. Also, in this amendment, the GSEs were limited to holding minimal capital, with this scheduled to decline to zero in 2019. This was

These necessary administrative actions stabilized the GSEs and the overall housing market. As a result, while portfolio lenders were severely tightening credit and private label mortgage securitizers exited the secondary market, the GSEs fulfilled their countercyclical role by continuing to provide financing, thus preventing the overall recession from being far more severe.[17] Furthermore, starting in 2012, the GSEs produced significant net profits that have largely been paid to the Treasury in the form of dividends on its investment. To date, these have totaled $301 billion paid back to the government on the $191 billion of capital infusions provided by the government.[18]

Conservatorship has created a historic opportunity to advance affordable housing and housing equity programs through use of the large value of the government's stock rights in the GSEs

As part of the support of the GSEs in 2008, the government received shares of preferred stock and warrants for 79.9% of their common stock. The value of these stock interests depends on several variables, including the terms and timing of recapitalization and release from conservatorship, but they are significant assets. The value of the GSE preferred stock and warrants should be used for affordable housing and racial equity programs as detailed below.

The Congressional Budget Office (CBO) analyzed these assets' value in a wide range of circumstances. In 2020, under scenarios based on CBO macroeconomic forecasts and expected required GSE capital levels, CBO estimated the value of the government's preferred shares and common stock warrants of $48 billion if the GSEs issued a new stock offering in 2023, and a value of $98 billion if they did so in 2025 with two additional years to build up retained earnings.[19] A later stock offering with time for additional retained earnings would likely further increase the value of these interests. Dedicating all or a substantial share of these assets to affordable housing and racial equity would provide critically needed aid to millions of households, boost the housing and construction industry and the overall economy, and provide a means to measurably close the racial homeownership gap and the resulting wealth gap.

The GSEs' placement into conservatorship coincided with the provision of extensive federal aid for banks and other financial institutions from the Troubled Asset Recovery Program (TARP). Conservatorship of the GSEs began in September 2008 and in October the TARP program was established.[20] The insurer AIG, which had been already receiving massive assistance from the Federal Reserve, then became a large recipient of TARP assistance. TARP was also ultimately used to rescue auto manufacturers, including General Motors and Chrysler.

TARP aid, like the GSE support under different legislation (HERA), was aimed at stabilizing markets and aiding the overall economy. AIG and the auto manufacturers were central entities critical to their industries, as the GSEs are to housing finance. The investments in AIG and the auto manufacturers helped stabilize not only these individual companies but also the overall economy, which was in freefall,

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subsequently amended to permit them to hold $3 billion of capital each. The permissible capital retention was raised in 2019 to $25 billion for Fannie Mae and $20 billion for Freddie Mac. In January 2021 this was dramatically increased to capital of 3%, totalling approximately $243 billion combined for the GSEs.

[17] David Min, *How Government Guarantees in Housing Finance Promote Stability*, 50 Harv. J. Legis. 437 (2013), at p. 467, available at https://scholarship.law.uci.edu/cgi/viewcontent.cgi?referer=https://www.google.com/&httpsredir=1&article=1036&context=faculty scholarship.

[18] Under the 2012 arrangement, Treasury has received payments totaling $301 billion compared to its total capital investment through the line of credit of $191 billion. However, since these net sweep payments are all treated as dividend payments to Treasury, the total of amount of the disbursements on the line of credit of $191 Billion remains outstanding. The Federal Reserve has also earned a profit on its investment in the GSE Bonds and MBS.

[19] Congressional Budget Office, *Effects of Recapitalizing Fannie Mae and Freddie Mac Through Administrative Actions* (August 2020), available at https://www.cbo.gov/system/files/2020-08/56496-GSE.pdf.

[20] The Trouble Asset Relief Program (TARP) was established under the Emergency Economic Stabilization Act of 2008, 12 U.S.C. § 5201 *et seq*. Additional government support was also provided to the financial institutions through guarantees provided by the Federal Deposit Insurance Commission and Federal Reserve programs.

and prevented the failure of key industries that are foundational to the country's financial and industrial sectors. Much of the aid to AIG was immediately passed through to bond holders and others who held insurance backed by AIG, enabling them to avoid absorbing losses. Similarly, aid to the auto manufacturers avoided huge job layoffs as well as preserved parts manufacturers, auto dealers and other companies that were dependent on the auto companies' survival.

The legislation creating TARP granted the Treasury Secretary broad authority and discretion over the terms and conditions of assistance and the adjustment and resolution of that aid.[21] In resolving and winding down its investments in AIG and the auto companies, the government waived and relinquished assets, including stock warrants and other rights.[22] This was done even though the government's TARP investments to AIG and the auto manufacturers resulted in net losses of nearly $30 billion to the government on its investments to them.[23] The concessions aided the companies' recoveries, but more importantly, the concessions furthered the goal of strengthening the specific markets they operated in and the overall economy.

The concessions to these TARP recipients and the use of the value of the GSE stock interests both carry out the goal of bolstering critical markets. This GSE assistance would be a more direct targeting of public benefit than the concessions provided to AIG and auto manufacturers but both are done with the goal of advancing overall markets. The concessions to AIG and the auto manufacturers benefited the companies themselves, helping ensure they would continue operation, whereas concessions to the GSEs for housing programs would directly benefit the housing market and homebuyers. Moreover, while AIG, the auto manufacturers, and the GSEs are all privately held for-profit companies, the GSEs are congressionally chartered and required to further a public benefit making them quasi-private entities for the government support they receive. Affordable housing and fair lending are specific statutory priorities of their mission. Therefore, providing the value of the government stock interests in the GSEs to affordable housing and racial equity programs furthers these explicit statutory public purposes.

Such concessions to the GSES also would not result in a net loss to the government, as the GSEs have already returned $110 billion more than the government's investment, making it the most profitable government investment in the crisis recovery efforts. Furthermore, requiring increased affordable housing and racial equity programs and utility oversight furthers the GSEs' mission impact and financial security, and these are appropriate conditions of Treasury reducing the large debt claim it holds against the GSEs and continuing to provide its essential financial backing.

The large net returns already realized by the government from its GSE investments and the extreme current affordable housing crisis make it compelling for the government to amend the Preferred Stock Purchase Agreements (PSPAs) to waive the government's GSE stock interests in order to expand these efforts. The funds returned to the government were a product of GSE fees paid by homebuyers, including lower-wealth consumers. Moreover, during the time these fees were earned, the GSEs well-served the higher end of the mortgage market while not adequately serving affordable single-family housing, lower wealth borrowers and families of color.

Operationally, the value of the government GSE stock interests could be placed in an independent joint affordable housing entity of the GSEs, similar to the organization of the GSEs' Common Securitization Solutions, which houses the GSEs' common securitization platform that issues and services GSE mortgage securities. FHFA should oversee this entity and approve its board members. The stock interests could be

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[21] *See, e.g.*, 12 U.S.C. § 5211 (authorizing the Treasury Secretary to purchase, and to make and fund commitments to purchase, troubled assets from any financial institution, on such terms and conditions as are determined by the Secretary, and in accordance with this chapter and the policies and procedures developed and published by the Secretary).

[22] Assistance under TARP included capital purchases through acquiring preferred stock, totaling over $200 billion, guarantees of assets, and loans. Under the capital purchase program, dividends of 5% were required for the first five years, and 9% thereafter. Overall, these programs were successful in both stabilizing critical industries and permitting the government to recover its investments. For two key industries, AIG and assistance to the auto companies, the agreements with the companies were restructured, with the government waiving rights, including warrants, and ultimately absorbing losses of $15 billion and $14 billion, respectively. Excluding the cost of assistance to homeowners, the government disbursed over $400 billion under TARP and received back that amount plus a $3 billion gain.

[23] Congressional Budget Office, *Report on the Troubled Asset Relief Program* (March 2020), available at https://www.cbo.gov/publication/56300.

waived by Treasury and the GSEs could place equivalent stock, money, or an obligation from the GSEs into the housing entity. If stock were transferred by the GSEs it could be held or eventually sold by the new joint GSE affordable housing entity, with the income and proceeds used for affordable housing.[24] Housing assistance could be implemented in a manner similar to the process used by the Federal Home Loan Banks (FHLBs) under their affordable housing program. The FHLBs, which are also government sponsored enterprises supervised by FHFA, direct funds to other entities for affordable housing programs, rather than operating housing programs themselves.[25]

Importantly, the aid should be targeted to homeownership and provide significant down payment assistance aimed at reducing the racial home ownership gap. This should include a restorative justice homeownership fund for Black families and others excluded from homeownership by previous discriminatory federal housing policies.[26] Wealth required for down payment and closing costs is a major barrier to homeownership for many potential homebuyers, particularly Black, Latino, and other families of color, and this assistance is effective for those who have been excluded from homeownership opportunities.[27] For example, white families are far more likely to benefit from inheritance or family assistance for down payments due to historical wealth accumulation and on average white families buy homes and start acquiring equity eight years earlier than Black families.[28] Other affordable housing programs outlined in the sections below, including increasing housing supply, should also be supported.

The assistance from this new program would be a meaningful increase to affordable housing and racial equity efforts.

To meet their public mission and the needs of the country, the GSEs' overall affordable housing programs must be expanded

The primary purpose of the GSEs is to support a broad and resilient national mortgage market. Importantly, in exchange for government support, the GSEs have an explicit public interest mission, including specific obligations to advance affordable housing.[29] They are charter-bound to promote access to credit throughout the nation, with an emphasis on housing for low- and moderate-income families and underserved areas, including communities of color. This includes a specific authorization to achieve lower returns on these efforts.[30]

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[24] If the warrants are sold by Treasury itself, the proceeds would go to the general fund for deficit reduction. *See* 12 U.S.C. § 1719(g)(2)(C). "The Secretary of Treasury shall deposit in the General Fund of the Treasury any amounts received by the Secretary under this subsection, where such amount shall be "(i) declared for the sole purpose of deficit reduction; and (ii) prohibited from use as an offset for other spending increases or revenue reductions." Alternatively, Congress could mandate this use of the warrants. The TARP programs in which administrative modifications and waivers were made to the agreements include a similar provision regarding the disposition of the proceeds. *See* 12 U.S.C. § 5216(d).
[25] 12 U.S.C. § 1421 *et seq.*; Federal Housing Finance Agency, *Federal Home Loan Bank Affordable Housing Program*, available at https://www.fhfa.gov/PolicyProgramsResearch/Programs/AffordableHousing/Pages/Affordable-Housing-Home-Loan-Banks.aspx. These banks can also do more to support affordable, inclusive housing.
[26] Regulation B of the Equal Credit Opportunity Act authorizes the use of Special Purpose Credit Programs that allow for targeted lending to underserved borrowers. See Lisa Rice, *Using Special Purpose Credit Programs to Advance Equality*, National Fair Housing Alliance, November 4, 2020, available at https://nationalfairhousing.org/using-spcps-blog/.
[27] Laurie Goodman, Alanna McCargo, Bing Bai, Edward Golding, and Sarah Strochak, *Barriers to Accessing Homeownership Down Payment, Credit, and Affordability*, Urban Institute (September 2018), https://www.urban.org/research/publication/barriers-accessing-homeownership-down-payment-credit-and-affordability-2018.
[28] Thomas Shapiro, Tatjana Meschede, and Sam Osoro, *The Roots of the Widening Racial Wealth Gap: Explaining the Black-White Economic Divide*, Brandeis University Institute on Assets and Social Policy (Feb. 2013), available at https://heller.brandeis.edu/iasp/pdfs/racial-wealth-equity/racial-wealth-gap/roots-widening-racial-wealth-gap.pdf; Thomas Shapiro, The Hidden Costs of Being African American: How Wealth Perpetuates Inequality (2004), at pp. 113-14.
[29] *See* 12 U.S.C. § 1716 (Fannie Mae charter); 12 U.S.C. § 1451 (Freddie Mac charter); 12 U.S.C. § 4561 (affordable housing goals); 12 U.S.C. § 4565 (duty to serve underserved markets).
[30] 12 U.S.C. § 1716 (providing authority to engage in "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").

Aided by the GSEs' support, in the period since the 2008 recession, the broad housing market stabilized and overall home equity grew to record levels.[31] However, many families and communities have been left behind. Lower wealth families, families of color, and especially Black families, have not only failed to advance, but many are worse off now compared to where they were at the onset of the 2008 recession. For example, the inflation adjusted net worth of those in the bottom quintile of income earners dropped by 30%, while the wealth of the top quintile of income earners has increased by 78%.[32] Families of color lost a generation of home equity and their homeownership rates remain below pre-recession levels.[33]

The nation faces a broad affordable housing crisis

Presently there is a widespread affordable housing crisis across the country, facing both homeowners and those who rent, in both urban and rural areas.[34] There was already a broad affordable housing crisis before the COVID crisis, and it has worsened since its onset.

In the 1990s substantial progress was made increasing the percentage of all families owning their homes, including progress for families of color. These gains were erased in the Great Recession with homeownership dropping to its lowest level in decades.[35] In the subsequent years, homeownership only partially rebounded, with lower wealth households recovering the least. In the years following the Great Recession, lenders and the GSEs tightened credit standards and the number of mortgages made to lower wealth and credit score families plummeted. This prevented families that did not meet these standards from benefiting from the strengthening housing market.

Today, financing remains a challenge, with down payments a major obstacle. It is difficult for families to save for a down payment, with it taking more than a decade for workers such as teachers, first responders and others to save the necessary down payment.[36] This is due to a combination of factors including insufficient income for middle- and lower-income earners, increased living expenses, including high rents and student debt payments, and the unavailability of intergenerational wealth transfers to people who are not born to wealth families.

Families have also struggled for many years to find affordable housing as a result of too few affordable homes. Since the Great Recession home building has lagged well behind household growth, creating a housing shortage. This shortage has expanded in recent years, with the supply of homes hitting a near record low due to historically low interest rates adding to the demand for homes.[37] A variety of factors at the federal, state, and local level contribute to this shortage, including land and labor shortages, local and state regulations, and obstacles to financing housing development.

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31 CoreLogic, *Borrowers Gained Over $6 Trillion in Home Equity Since the End of the Great Recession*, June 11, 2020, available at https://www.corelogic.com/news/corelogic-reports-borrowers-gained-over-6-trillion-in-home-equity-since-the-end-of-the-great-recession.aspx.

32 USA Facts, Wealth in America: How it has Grown and How it is Distributed, November 13, 2019, available at https://usafacts.org/articles/wealth-america-how-it-has-grown-and-how-it-distributed/.

33 *See* Alanna McCargo, Jung Hyun Choi, and Edward Golding, *Building Black Homeownership Bridges: A Five Point Framework for Reducing the Racial Homeownership Gap*, Urban Institute (May 2019), available at https://www.urban.org/sites/default/files/publication/100204/building_black_ownership_bridges_1.pdf; Sarah Burd-Sharps and Rebecca Rasch, *Impact of the US Housing Crisis on the Racial Wealth Gap Across Generations*, Social Science Research Council and ACLU (June 2015), available at https://www.aclu.org/sites/default/files/field_document/discrimlend_final.pdf.

34 Joint Center for Housing Studies at Harvard University, *State of the Nation's Housing 2020*, available at https://www.jchs.harvard.edu/sites/default/files/reports/files/Harvard_JCHS_The_State_of_the_Nations_Housing_2020_Report.pdf; National Rural Housing Coalition, *Housing Need in Rural America*, available at https://ruralhousingcoalition.org/overcoming-barriers-to-affordable-rural-housing/.

35 U.S. Government Accountability Office, *Preliminary Analysis of Homeownership Trends for Nine Cities*, June 25, 2020, at p. 2, available at https://www.gao.gov/assets/710/707835.pdf (noting that national homeownership rates peaked at about 70% in the years before the financial crisis, then dropped to a 30-year low of 63% in 2016).

36 *See* Center for Responsible Lending, *Qualified Residential Mortgages: How long does it take to save 10%?*, available at https://www.responsiblelending.org/research-publication/qrm-saving-years-huge-down-payment

37 Joint Center for Housing Studies of Harvard University, *The State of the Nation's Housing 2020*, at p. 11-13, available at https://www.jchs.harvard.edu/sites/default/files/reports/files/Harvard_JCHS_The_State_of_the_Nations_Housing_2020_Report.pdf.

For renters, the situation is also difficult, especially for lower income families and renters of color. The percentages of households rent burdened and severely rent burdened were already high pre-COVID.[38] This reflected a shortage since the 2008 recession in the building of affordable rental units and a longstanding underfunding of rental housing assistance.[39]

The COVID crisis has aggravated these conditions. For homeowners, at the beginning of the COVID crisis FHFA and the Federal Housing Administration (FHA) took immediate action to reduce the impact for mortgage borrowers. However, families dealing with COVID related job loss and long-term unemployment will not be able to pay even a modified mortgage payment when loan forbearance ends. This crisis has coincided with historically low interest rates, fueling a refinance boom that has benefited millions of homeowners who qualify. However, these refinance loans and their benefits have gone disproportionately to higher wealth GSE borrowers, excluding many borrowers of color, as these have been the easiest and most profitable loans to make.[40]

Families that rent face a severe crisis. More than 20 million households are rent burdened, paying over 30% of their total income on rent. Sixty two percent of those with incomes under $25,000 are severely rent burdened, paying over 50% of income for rent.[41] In the COVID crisis, more than 10 million families are behind in rent and could face eviction if substantial additional assistance does not come through. While the most recent COVID stimulus aid package included $25 billion for rental assistance, much more will be required to prevent mass evictions once federal and state moratoria terminate.

Families of color have been disproportionately impacted by the affordable housing crisis, over the past years and in this COVID crisis. As a result of longstanding structural discrimination, these families have lower average incomes, greater crisis-induced income disruptions,[42] and less wealth and reserves to absorb financial shocks. Their homeownership rates have recovered the least since the 2008 recession, especially for Black families, and families of color are more likely than white households to be struggling with their mortgage or rent payment due to being heavily employed in the service sector that has been hardest hit by COVID-19.[43]

Actions the GSEs should take to increase their support of affordable housing

The GSEs should do significantly more to help address the affordable housing crisis in both immediate and long-term measures. While many factors contribute to the crisis, the GSEs are among the primary entities with the responsibility, authority, and resources to significantly improve it. Given their prominence in the market, financing nearly half of all mortgage loans, the GSEs have historically played a

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[38] *Id.* at 1. Approximately 20.4 million renter households paid more than 30% of their incomes for housing in 2019. For households with income under $25,000, 62% paid more than half their incomes for housing.

[39] *Id.* at 6 and 11.

[40] In Q2 2020, refinance lending was up more than 60% from Q1 2020 and more than 200% from the same time last year, accounting for nearly 70% of all first lien originations by dollar value. Black Knight, July 2020 Mortgage Monitor, available at https://www.blackknightinc.com/black-knights-july-2020-mortgage-monitor/. *See also* Fortune, *Why It's Suddenly Harder to Get a Mortgage Than It's Been in Years*, May 10, 2020, available at https://fortune.com/2020/05/10/coronavirus-getting-a-mortgage-refinancing-credit-score/ (noting tightened lending environment and more stringent requirements).

[41] Joint Center for Housing Studies at Harvard University, *State of the Nation's Housing 2020*, at 1, available at https://www.jchs.harvard.edu/sites/default/files/reports/files/Harvard_JCHS_The_State_of_the_Nations_Housing_2020_Report.pdf.

[42] *See* Steven Brown, *The COVID-19 Crisis Continues to Have Uneven Economic Impact by Race and Ethnicity*, Urban Institute (July 1, 2020), available at https://www.urban.org/urban-wire/covid-19-crisis-continues-have-uneven-economic-impact-race-and-ethnicity; Steven Brown, *How COVID-19 is Affecting Black and Latino Families' Employment and Financial Well-Being*, Urban Institute (May 6, 2020), available at https://www.urban.org/urban-wire/how-covid-19-affecting-black-and-latino-families-employment-and-financial-well-being.

[43] Michael Neal and Caitlin Young, *Delinquent Homeowners in Neighborhoods of Color Are Less Likely to be Protected by Forbearance*, Urban Institute (December 2, 2020), available at https://www.urban.org/urban-wire/delinquent-homeowners-neighborhoods-color-are-less-likely-be-protected-forbearance; Jung Hyun Choi and Daniel Pang, *Six Facts You Should Know about Current Mortgage Forbearances*, Urban Institute (August 18, 2020), available at https://www.urban.org/urban-wire/six-facts-you-should-know-about-current-mortgage-forbearances;Center on Budget and Policy Priorities, *Tracking the COVID-19 Recession's Effects on Food, Housing, and Employment Hardships*, Updated December 18, 2020, available at https://www.cbpp.org/research/poverty-and-inequality/tracking-the-covid-19-recessions-effects-on-food-housing-and.

leading role in setting standards in the market for the terms of mortgages, the requirements to qualify for them, and the prices homeowners pay for their mortgages.

Yet, during conservatorship and with limited capital, the loans the GSEs finance have dramatically trended to higher credit scores and increased mortgage costs for lower wealth borrowers despite their clear important public interest mission of affordability in the housing market.[44] During conservatorship, the GSEs have focused on reducing risk, resulting in overly tight credit requirements for borrowers. The median credit score of the GSEs' loan purchases have been extraordinarily high, 758 in February 2020 prior to the COVID crisis and 772 at the end of 2020.[45] Overly stringent lender credit overlays exacerbate the problem. The Urban Institute has found that lenders would have issued 6.3 million additional mortgages between 2009 and 2015 if lending standards had been at historically safe levels.[46]

Additionally, the mix of the mortgages financed by the GSEs during conservatorship has been impacted by higher capital requirements for lower wealth borrowers that were imposed on private mortgage insurers. These insurers provided coverage to the GSEs for part of the risk of default on mortgages with less than 20% of down payment. In the 2008 crisis, heavy losses and undercapitalization strained the ability of the mortgage insurers to pay for these losses. FHFA responded in 2015 with increased capital requirements for these insurers that raised the insurance fees and cost of mortgages, particularly for lower wealth borrowers with smaller down payments and lower credit scores.[47] Mortgages made through the Federal Housing Administration have government insurance with a subsidized cost of capital, and the FHFA action made these FHA mortgages less expensive compared to GSE mortgages. This creates an additional challenge for the GSEs in serving this portion of the market.

GSE affordable housing efforts have also been diminished during conservatorship. In the 1990s, the GSEs engaged in widespread, effective outreach campaigns to reach lower wealth families and connect them with lenders. In recent years, these efforts have been far more modest. In addition, the GSE statutory contributions to affordable housing funds were suspended from 2008 through 2013 as they recovered from the housing crash, resulting in a loss of $2.5 billion of affordable housing assistance.[48]

There are a host of steps the GSEs and FHFA should take to increase the GSEs' support of affordable housing. While none of these by itself is a solution to this complex and challenging problem, collectively they would materially increase families' housing opportunities and security and move toward more racial equity in homeownership.

In response to the continuing COVID crisis, extended forbearance and increased support for homeowners is critical to avoid a foreclosure crisis in 2021. While the existing GSE forbearance programs have helped many who are recovering from this crisis, millions of jobs have been lost, many permanently. Additional forbearance and more assistance will be essential to prevent those homeowners from being displaced by this national health disaster. More outreach must be conducted to ensure that borrowers are aware of the Coronavirus Aid, Relief and Economic Security Act (CARES Act) provisions. For those able to refinance their home, support for smaller loan refinances and refinance loans to lower wealth borrowers, many who are families of color, is required. With regard to renters, the GSEs provide their support indirectly,

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44 *See* FHFA Annual Housing Report (October 2020), at p. 40-41, available at https://www.fhfa.gov/AboutUs/Reports/ReportDocuments/Annual-Housing-Report-2020.pdf (noting share of mortgage purchases by FICO score group).

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

46 Laurie Goodman, *Overly Tight Credit Killed 1.1 Million Mortgages in 2015*, Urban Institute (November 2016), available at https://www.urban.org/urban-wire/overly-tight-credit-killed-11-million-mortgages-2015 ; Laurie Goodman, *Squeaky-Clean Loans Lead to Near-Zero Borrower Defaults – And That is Not a Good Thing*, Urban Institute (August 2016), available at https://www.urban.org/urban-wire/squeaky-clean-loans-lead-near-zero-borrower-defaults-and-not-good-thing

47 FHFA News Release, *Fannie Mae and Freddie Mac Issue Revised Private Mortgage Insurer Eligibility Requirements*, April 17, 2015, available at https://www.fhfa.gov/Media/PublicAffairs/Pages/Fannie-Mae-and-Freddie-Mac-Issue-Revised-Private-Mortgage-Insurer-Eligibility-Requirements-4-17-2015.aspx.

48 See discussion in n. 9.

through their support of loans to landlords. They have offered forbearance to those landlords for their mortgages on the condition that is passed through with relief to tenants. This needs to likewise be extended.

To make affordable, sustainable home mortgages more available to lower wealth households, the GSEs can take a number of steps. First, the GSEs should expand the availability of their low down payment mortgages as well as other programs to assist homeowners with less wealth to obtain a mortgage and sustain potential financial volatility during the mortgage. The GSEs should also remove so-called credit overlays that are additional loan restrictions beyond the qualifications otherwise required for loans, as these exclude sustainable loans.[49] In addition they can increase their purchases of small balance mortgages and eliminate surcharges for these loans and loans to single borrowers. Price differentials for mortgages, especially those based on the risk of national catastrophes such as the COVID crisis, should be reduced. Finally, far more outreach to families on their eligibility for home loans, how to qualify and where to apply is needed as Freddie Mac's data shows that there are millions of Black and Latino mortgage ready consumers, including many millennials. [50]

Increasing the supply of affordable homes is an especially challenging problem. The GSEs can add to these efforts, though, in several ways. These include: increasing the availability and workability of loans to purchase and rehab single-family homes in need of repair; providing more effective assistance to those living in manufactured housing communities and supporting increased quality manufactured housing; and stopping the sale of tens of thousands of delinquent and foreclosed home loans to investors who hold the homes long term rather than resell them to new homeowners. The GSEs should also seek to provide financing for homeownership and rental housing developers through construction-to-permanent loans, as this remains a barrier to new construction. With the financing of new rental units, the GSEs should target their assistance to projects that have the greatest impact on housing for lower income households.

Importantly, this increased focus and activity on affordable housing by the GSEs must be mandated by FHFA. These activities will further the GSEs' public mission but produce lower financial returns, which is statutorily permissible. Mandating them both ensures that they occur in light of the other competing interests of the GSEs, and it also safeguards that neither GSE is disadvantaged compared to the other by concentrating on a less lucrative portion of the housing market.

The impacts of racial discrimination are manifest in the housing market and the GSEs must take significant steps to advance housing equity

For the majority of middle-class families, homeownership is the most important means to build family wealth and stability. Yet, the ability to build wealth through homeownership has not been provided equitably throughout most of our country's history and discrimination remains a pervasive problem.

In the creation of New Deal housing programs in the 1930s, the federal government promoted home ownership opportunity for white Americans only, while families of color were intentionally excluded.[51] These discriminatory policies were instituted in the housing finance system in 1933 with the underwriting guidelines of the Home Owners Loan Corporation (HOLC) that redlined African American neighborhoods

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[49] Eric Stein and Michael Calhoun, *A Smarter Qualified Mortgage Can Benefit Borrowers, Taxpayers and the Economy* (July 2019), available at https://www.responsiblelending.org/sites/default/files/nodes/files/research-publications/crl-a-smarter-qualified-mortgage-july2019.pdf

[50] Data from Freddie Mac and the Urban Institute show that there are 6.3 million mortgage ready Black and Latino millennials in the 31 largest MSAs. *See* Alana McCargo, *America's Persistent Racial Homeownership Gaps*, Urban Institute (February 6, 2020), available at https://www.nar.realtor/sites/default/files/documents/policy-forum-2020-presentation-racial-homeownership-gaps-02-06-2020.pdf.

[51] Testimony of Nikitra Bailey, Executive Vice President, Center for Responsible Lending, Before the U.S. House of Representatives, Committee on Financial Services, Subcommittee on Housing, Community Development, and Insurance, A Review of the State of and Barriers to Minority Homeownership (May 8, 2019), available at https://financialservices.house.gov/uploadedfiles/hhrg-116-ba04-wstate-baileyn-20190508.pdf.

and other communities of color, denying them access to mainstream banking services.[52] The government also subsidized the mass-production of subdivisions, where builders included a requirement that no homes be sold to Black Americans.[53] Consequently, the suburbanization of America following the Great Depression financially benefited white Americans and excluded people of color. White homeowners were able to gain home equity appreciation, but for decades families of color were not provided the same opportunity. Although discrimination was made unlawful by the Fair Housing Act in 1968, these long-standing discriminatory policies produced segregated housing patterns across the nation and disinvestment from Black communities. This legacy has limited Black borrowers' and other families of color's access to traditional credit and unduly exposed them to predatory lending sources.[54]

Families of color were then devastated by the subprime lending boom in the early 2000s, in which lenders sold millions of families abusive loans that were not sustainable.[55] Leading up to the 2008 financial crisis, these dangerous niche products that lenders mass-marketed included interest-only loans, ARM loans that combined "teaser" rates with subsequent large jumps in payments, negative amortization loans, and loans made with limited or no documentation of the borrower's income or assets.[56] Studies have shown that these products in and of themselves caused about half of the increased risk in mortgage lending that led to the Great Recession.[57]

Center for Responsible Lending research demonstrated that Black and Latino families disproportionately received subprime loans at a greater rate than whites and that borrower characteristics did not explain the differences in lending.[58] About half of all mortgages made to Black and Latino families during the run-up to the crisis were subprime loans with patently unsustainable terms.[59] Indeed, much evidence indicates that borrowers of color, including higher-income borrowers, were disproportionately steered into toxic

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[52] Bruce Mitchell and Juan Franco, *HOLC "Redlining" Maps: The Persistent Structure of Segregation and Economic Inequality*, National Community Reinvestment Coalition (March 20, 2018), available at https://ncrc.org/holc/.

[53] Terry Gross, *A 'Forgotten History' of How the U.S. Government Segregated America*, NPR Fresh Air, May 3, 2017, https://www.npr.org/2017/05/03/526655831/a-forgotten-history-of-how-the-u-s-government-segregated-america.

[54] *See* Cheryl Young and Felipe Chacon, *50 Years After the Fair Housing Act – Inequality Lingers*, Trulia (April 19, 2018), available at https://www.trulia.com/research/50-years-fair-housing/.

[55] The GSEs' affordable housing goals and loans counting for Community Reinvestment Act credit did not cause the crisis, although it is a much-repeated myth. As the Financial Crisis Inquiry Commission concluded, the affordable housing goals "only contributed marginally to Fannie's and Freddie's participation in [risky mortgages]." Financial Crisis Inquiry Commission, Final Report of the National Commission on the Causes of the Financial and Economic Crisis in the United States, at xxvii (2010), https://www.gpo.gov/fdsys/pkg/GPO-FCIC/pdf/GPO-FCIC.pdf. Furthermore, "none of Fannie Mae's 2004 purchases of subprime or Alt-A securities were ever submitted to HUD to be counted toward the goals." *Id.* at 123. Additionally, the Federal Reserve Bank of St. Louis determined that there was "no evidence that the affordable housing goals of the CRA or of the GSEs affected" the volume, pricing, and performance of securitized subprime mortgages originated in the sample studied. Rubén Hernández-Murillo, Andra C. Ghent, and Michael T. Owyang, Federal Reserve Bank of St. Louis, *Did Affordable Housing Legislation Contribute to the Subprime Securities Boom?* (March 2012), available at https://files.stlouisfed.org/ files/htdocs/wp/2012/2012-005.pdf.

[56] Financial Crisis Inquiry Commission, The Final Report of the National Commission on the Causes of the Financial and Economic Crisis in the United States, at pp. 104-111 (2011), available at https://www.govinfo.gov/content/pkg/GPO-FCIC/pdf/GPO-FCIC.pdf.

[57] Morris A. Davis, William D. Larson, Stephen D. Oliner, and Benjamin R. Smith, *A Quarter Century of Mortgage Risk*, FHFA Staff Working Paper 19-02, at p. 35, October 2019 (revised) January 2019 (original) (finding that "risky product features accounted for more than half of the rise in risk during the boom years", defining "risky product features" as those ineligible for QM status). For characteristics of subprime loans, see Testimony of Eric Stein before the U.S. Senate Committee on Banking, Housing and Urban Affairs, Turmoil in the U.S. Credit Markets: The Genesis of the Current Economic Crisis, Center for Responsible Lending (October 16, 2008) at pp. 11-14, 34-39, available at https://www.responsiblelending.org/sites/default/files/nodes/files/researchpublication/senate-testimony-10-16-08-hearing-stein-final.pdf.

[58] Debbie Gruenstein Bocian, Keith Ernst and Wei Li, *Race, Ethnicity and Subprime Loan Pricing*, Center for Responsible Lending, Journal of Economics and Business, at pp. 110-124, Vol. 60, Issues 1-2, January-February 2008.

[59] Federal Reserve researchers, using data from 2004 through 2008, have reported that higher-rate conventional mortgages were disproportionately distributed to borrowers of color, including African-American, Latino, American Indians, Alaskan Natives, Native Hawaiians, Pacific Islanders, and Hispanic borrowers. See R.B. Avery, K.P. Brevoort, and G.B. Canner, Higher-Priced Home Lending and the 2005 HMDA Data, Federal Reserve Bulletin (September 2006), available at http://www.federalreserve.gov/pubs/bulletin/2006/hmda/bull06hmda.pdf. For example, in 2006, among consumers who received conventional mortgages for single-family homes, roughly half of African-American (53.7 percent) and Hispanic borrowers (46.5 percent) received a higher-rate mortgage compared to about one-fifth of non-Hispanic white borrowers (17.7 percent). According to the researchers, "[F]or higher priced conventional first-lien loans for an owner-occupied site-built home, the mean APR spreads were about 5 percentage points above the yields on comparable Treasury securities both for purchase loans and refinancings". R.B. Avery, K.P. Brevoort, and G.B. Canner, The 2006 HMDA Data, at p. A88, Federal Reserve Bulletin (December 2007), available at http://www.federalreserve.gov/pubs/bulletin/2007/pdf/hmda06final.pdf.

mortgages despite qualifying for safer and more responsible loans with cheaper costs.[60] Because of these lending practices, Black and Latino families lost over $1 trillion dollars in wealth during the crisis.[61] Moreover, Black homeownership has been the slowest to recover from the Great Recession. In fact, there would be 770,000 more Black homeowners if the homeownership rate recovered to its pre-crisis level in 2000.[62]

President Biden has called for acknowledgment and redress of the impacts of this long history of the nation's and the Federal Government's housing discrimination including the racial gap in homeownership. He stated in one of his early executive orders: "Throughout much of the 20th century, the Federal Government systematically supported discrimination and exclusion in housing and mortgage lending. While many of the Federal Government's housing policies and programs expanded homeownership across the country, many knowingly excluded Black people and other persons of color, and promoted and reinforced housing segregation. Federal policies contributed to mortgage redlining and lending discrimination against persons of color."[63]

However, in recent years rather than remediating the damage done by this history of discrimination against families of color, lenders' overcorrections to lending standards and more restrictive GSE credit policies have instead closed off lending options for these families. Data from the Home Mortgage Disclosure Act and the GSEs themselves continues to demonstrate low levels of conventional mortgage loans to Black and Latino families. For example, in 2019, 4.8% of Fannie Mae and 3.6% of Freddie Mac home purchase loans were from Black borrowers, and 4.1% and 3.7% of refinance loans.[64] Since the financial crisis, many lenders and the GSEs have limited lending and increased prices for borrowers with lower credit scores and/or lower down payments. Borrowers of color, low and moderate-income families, and first-time homebuyers tend to have both lower FICO scores and fewer resources to put towards a down payment due to lower levels of family wealth, which in turn is due in large part to generations of systemic discrimination, including by the federal government.

Discrimination in the mortgage market is also by no means a relic of the past and can manifest in multiple ways. For example, a recent Center for Investigative Reporting Reveal report analyzed 31 million mortgage records and found that, controlling for income and other available characteristics, in 61 U.S. metro areas African Americans and Latinos are more likely to be turned down for a loan than whites in conventional mortgage applications.[65] Furthermore, testing has repeatedly demonstrated housing discrimination. In 2019, Newsday published the results of a three-year undercover investigation which exposed widespread discriminatory home-selling practices by Long Island real estate agents.[66] Two similarly situated testers of different racial backgrounds independently approached the same agent to test whether they were treated differently based on their race. Black testers experienced disparate treatment

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[60] Rick Brooks and Ruth Simon, Subprime Debacle Traps Even Very Credit-Worthy, Wall Street Journal (December 2007), available at https://www.wsj.com/articles/SB119662974358911035.

[61] Debbie Gruenstein Bocian, Peter Smith, and Wei Li, *Collateral Damage: The Spillover Costs of Foreclosures*, Center for Responsible Lending, at p. 2 (Oct. 24, 2012), available at https://www.responsiblelending.org/mortgagelending/research-analysis/collateral-damage.pdf.

[62] Alanna McCargo, Jung Hyun Choi, and Edward Golding, *Building Black Homeownership Bridges: A Five Point Framework for Reducing the Racial Homeownership Gap*, Urban Institute, at p. 1 (May 2019), available at https://www.urban.org/sites/default/files/publication/100204/building_black_ownership_bridges_1.pdf.

[63] The White House, *Memorandum on Redressing Our Nation's and the Federal Government's History of Discriminatory Housing Practices and Policies* (January 26, 2021) available at https://www.whitehouse.gov/briefing-room/presidential-actions/2021/01/26/memorandum-on-redressing-our-nations-and-the-federal-governments-history-of-discriminatory-housing-practices-and-policies/

[64] FHFA Annual Housing Report, at p. 11, Table 6 (October 2020), available at https://www.fhfa.gov/AboutUs/Reports/ReportDocuments/Annual-Housing-Report-2020.pdf.

[65] Emmanuel Martinez and Aaron Glantz, *Kept Out: For People of Color, Banks Are Shutting the Door to Homeownership*, Center for Investigative Reporting (Feb. 15, 2018), available at https://revealnews.org/article/for-people-of-color-banks-are-shutting-the-door-to-homeownership/ (the study did not have available data on credit scores, but it controlled for nine economic and social factors, including an applicant's income, the amount of the loan, the ratio of the size of the loan to the applicant's income, type of lender, racial makeup and median income of the neighborhood where the applicant wanted to purchase the property).

[66] Ann Choi, Keith Herbert, Olivia Winslow, and Arthur Browne, *Long Island Divided*, Newsday (November 17, 2019), available at https://projects.newsday.com/long-island/real-estate-agents-investigation/.

49% of the time, compared with 39% for Latino and 19% for Asian testers.[67] And in 8% of the tests, the agents accommodated white testers while imposing more stringent conditions on other testers.[68]

Moreover, Black Americans pay more to be homeowners. The overall differences in mortgage interest payments ($743 per year), mortgage insurance premiums ($550 per year), and property taxes ($390 per year) total $13,464 over the life of the loan, which amounts to $67,320 in lost retirement savings for Black homeowners.[69] Nearly a quarter of the disparity in homeownership costs for Black homeowners is due to local property tax assessments. A research study relying on a national data set found that Black homeowners bear a 13% higher property tax burden than white homeowners in the same jurisdiction; the study identified large tax assessment areas and an appeal process that tends to benefit white homeowners as the key factors resulting in higher relative property tax burden on Black homeowners.[70] Furthermore, Black families realize less growth in home equity as homes in Black neighborhoods of similar quality and amenities as other neighborhoods are worth 23% less, $48,000 per home on average, amounting to $156 billion in cumulative losses.[71]

As a result of this troubled history of inequity and continuing discrimination, Black homeownership levels, the primary asset of Black families, is at levels similar to when the Fair Housing Act was passed in 1968.[72] In fact, the gap between white and Black homeownership rates today is the largest it has been since 1890.[73] The homeownership rate for Black Americans is 42%, compared to white homeownership of 72.1%, and 48.1% for Latinos.[74] In large part because families of color were not afforded the opportunity to build wealth through federally supported investment in homeownership and were later devastated by the financial crisis, the median white family has 10 times the wealth of the median Black family and eight times the wealth of the median Latino family.[75] It will require focused and bold action to reverse these inequities.

The GSEs must be leaders in rectifying the long history of racial discrimination in the mortgage market, not only because it is the right thing to do, but because the future of the housing market depends on it. Demographic projections for the United States point to future increases in the population shares of people of color, making the need to serve these groups increasingly important for the health and future growth of the housing market. For example, over the past decade, Latinos have accounted for over 40% of all household formation growth and 58% of all population growth. Despite representing 18% of the

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[67] Id.
[68] Id.
[69] Michelle Aronowitz, Edward L. Golding, and Jung Hyun Choi, *The Unequal Costs of Black Homeownership*, MIT Golub Center for Finance and Policy (Oct. 1, 2020), available at http://gcfp.mit.edu/wpcontent/uploads/2020/10/Mortgage-Cost-for-Black-Homeowners-10.1.pdf.
[70] Carlos Avenancio-León and Howard Troup, *The Assessment Gap: Racial Inequalities in Property Taxation*, Washington Center for Equitable Growth (2020), available at https://equitablegrowth.org/working-papers/the-assessment-gap-racialinequalities-in-property-taxation/.
[71] Andre M. Perry, Jonathan Rothwell, and David Harshbarger, *The Devaluation of Assets in Black Neighborhoods*, Brookings (November 27, 2018), available at https://www.brookings.edu/research/devaluation-of-assets-in-black-neighborhoods/.
[72] Alanna McCargo and Jung Hyun Choi, *Closing the Gaps: Building Black Wealth Through Homeownership*, Figure 3, Urban Institute (November 2020), available at https://www.urban.org/sites/default/files/publication/103267/closing-the-gaps-building-black-wealth-through-homeownership_0.pdf; *see also* Laurie Goodman, Jun Zhu, and Rolf Pendall, *Are Gains in Black Homeownership History?*, Urban Institute (February 14, 2017), available at https://www.urban.org/urban-wire/are-gains-black-homeownership-history.
[73] Adam Levitin, *How to Start Closing the Racial Wealth Gap*, The American Prospect (June 17, 2020), available at https://prospect.org/economy/how-to-start-closing-the-racial-wealth-gap/.
[74] Alanna McCargo and Jung Hyun Choi, *Closing the Gaps: Building Black Wealth Through Homeownership*, Figure 3, Urban Institute (November 2020), available at https://www.urban.org/sites/default/files/publication/103267/closing-the-gaps-building-black-wealth-through-homeownership_0.pdf. For additional information on the various homeownership metrics, *see* Sarah Strochak, Laurie Goodman, and Sheryl Pardo, *Is the Sudden Increase in Black Homeownership Too Good to be True*, Urban Institute, February 4, 2020, https://www.urban.org/urban-wire/sudden-increase-black-homeownership-too-good-be-true (noting that the often-cited quarterly Census Housing Vacancy Report is more volatile and has a larger margin of error; furthermore, this year the survey has the additional challenge of the COVID crisis requiring many of the usual in-person interviews to be conducted by phone, which may result in differing response rates from homeowners and renters). Despite the measure, however, the approximately 30-point Black-white homeownership gap persists.
[75] Asset Building Policy Network, *The Hispanic-White Wealth Gap Infographic* (September 2019), available at https://prosperitynow.org/sites/default/files/resources/ABPN_Hispanic_White_Racial%20Wealth%20Gap%20Infographic_Final.pdf; Nick Noel, Duwain Pinder, Shelley Stewart III, and Jason Wright, The Economic Impact of Closing the Racial Wealth Gap, McKinsey & Company (August 2019), Exhibit 1 at p. 5, available at https://www.mckinsey.com/industries/public-and-social-sector/our-insights/the-economic-impact-of-closing-theracial-wealth-gap.

population, Latinos accounted for more than 60% of new homeowner gains over the past decade.[76] Furthermore, recent studies show that increasing homeownership to Black homeowners as well as addressing other structural discrimination has the potential to grow the economy by at least $1 trillion per year over the next five years.[77] A further study shows that addressing discrimination in mortgage lending targeted at Black Americans can create 4.9 million more households, 784,000 jobs, and $400 billion in tax revenue.[78]

As discussed in the previous section, the GSEs have the power to bolster affordable housing in numerous ways and these will benefit families of color. However, in addition to those efforts, more targeted aid is required to overcome discrimination. As research from Freddie Mac and Urban Institute demonstrates, there are millions of mortgage-ready borrowers of color, based on borrowers' current credit scores and debt-to-income ratios, though not funds available for a down payment. In fact, there are 6.3 million mortgage ready Black and Latino millennials in the 31 largest metropolitan statistical areas.[79] Given that many of these borrowers do not have family wealth for a down payment because of the lack of intergenerational wealth, targeted down payment assistance will be critical to enable mortgage-ready borrowers of color to become homeowners.

The GSEs should support a restorative justice homeownership fund that should be initiated administratively using the value of stock interests described above, and other possible funding, such as a proposal to repurpose an existing GSE fee that was used to pay for the 2010 payroll tax and is scheduled to expire in October 2011.[80] Moreover, the GSEs should reduce excessive credit score pricing that perpetuates discrimination, facilitate a secondary market for Special Purpose Credit Programs that authorize lending focused on underserved markets to encourage more lenders to utilize these programs to target loans to borrowers of color long denied access. In addition, robust fair lending reviews of all of their policies should be conducted and reported on a regular basis.[81]

Experience during the GSEs' conservatorship has demonstrated that a utility structure is optimal

Under conservatorship FHFA obtained broad control of the GSEs, having the authority of the GSE boards, officers, and shareholders.[82] Using the statutory authority under HERA for conservatorship and under the Preferred Stock Purchase Agreements (PSPA) that set out the terms of the government's investment,

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[76] Laura Kusisto and Ben Eisen, *Wave of Hispanic Buyers Shores Up U.S. Housing Market*, Wall Street Journal (July 15, 2019), available at https://www.wsj.com/articles/wave-of-hispanic-buyers-boosts-u-s-housing-market-11563183000.
[77] Dana M. Peterson and Catherine L. Mann, *Closing the Racial Inequality Gaps, The Economic Cost of Black Inequality in the U.S.*, Citi GPS: Global Perspectives and Solutions (September 2020), available at https://ir.citi.com/NvIUklHPilz14Hwd3oxqZBLMn1_XPqo5FrxsZD0x6hhil84ZxaxEuJUWmak51UHvYk75VKeHCMI%3D.
[78] Jeff Cox, *Morgan Stanley Says Housing Discrimination Takes a Huge Toll on the Economy*, CNBC (November 13, 2020), available at https://www.cnbc.com/2020/11/13/morgan-stanley-says-housing-discrimination-has-taken-a-huge-toll-on-the-economy.html.
[79] Alanna McCargo, *America's Persistent Racial Homeownership Gaps*, Urban Institute, available at https://www.nar.realtor/sites/default/files/documents/policy-forum-2020-presentation-racial-homeownership-gaps-02-06-2020.pdf. *See also* National Association of Hispanic Real Estate Professionals, *2019 State of Hispanic Homeownership Report*, available at https://nahrep.org/downloads/2019-state-of-hispanic-homeownership-report.pdf; Alanna McCargo, Jung Hyun Choi, and Edward Golding, *Building Black Homeownership Bridges: A Five Point Framework for Reducing the Racial Homeownership Gap*, Urban Institute, at p. 8 (May 2019), available at https://www.urban.org/sites/default/files/publication/100204/building_black_ownership_bridges_1.pdf.
[80] In the Temporary Payroll Tax Cut Continuation Act of 2011, Congress imposed an annual 10-basis point fee on new single-family mortgage purchases as a pay-for for the extension of the payroll tax cut. Once this fee expires in October 2021, the proceeds from this fee could be directed to other purposes. Rather than letting the statutory obligation expire, there are proposals for Congress to extend it in permanently and direct the funds to affordable housing programs.
[81] According to their charters, the GSEs are required to report to Congress on how they "assess underwriting standards, business practices, repurchase requirements, pricing, fees, and procedures, that affect the purchase of mortgages for low- and moderate-income families, or that may yield disparate results based on the race of the borrower, including revisions thereto to promote affordable housing or fair lending." 12 U.S.C. § 1456(f)(2)(G). Additionally, for more information on Special Purpose Credit Programs, see Lisa Rice, *Using Special Purpose Credit Programs to Expand Equality*, National Fair Housing Alliance, November 4, 2020, available at https://nationalfairhousing.org/using-spcps-blog/.
[82] 12 U.S.C. § 4617(b)(2).

FHFA implemented key administrative reforms and operated the GSEs as de facto utilities. The GSEs' retained portfolios were reduced to necessary business purposes rather than arbitrage and shrank to a quarter of their prior level.[83] Volume discounts that favored large lenders were prohibited. Guarantee fees were set based on robust capital levels and structured to reduce costs for lower wealth and credit borrowers. Much of the credit risk held by the GSEs has been transferred to third parties through their credit risk transfer programs to lower taxpayer risk of another bailout.

Despite the GSEs' critical role in keeping the mortgage market afloat and their return to profitability, proposals to wind down the GSEs and replace them with a system of private guarantors were made after the great financial crisis. The structure of the government's aid to the GSEs, which progressively reduced their capital levels to zero by 2018, reflected a view that the role of the GSEs should be fundamentally altered through future legislation, including shrinking their role and potentially winding them down.[84] Several bills were introduced in Congress to transfer the GSEs' role to multiple private guarantors with reduced regulatory oversight, including weakened fair lending oversight.[85] These bills failed to move forward due to concerns regarding the terms and feasibility of the proposed substitute system and the substantial transition risks that could disrupt the market.[86] Support has thereafter coalesced around continuing to operate the GSEs with utility-like regulation, with many leading trade groups and advocates endorsing the approach.[87]

Utility oversight may vary in its components and operation in different settings. For the GSEs, utility oversight contains several essential elements. First, the return paid to GSE private shareholders must be set at a level sufficient to attract investors, but not excessive as a result of their use of their special position provided by the government. The return must also ensure fair and inclusive pricing for lenders and homebuyers. Smaller lenders should not be charged more to access the GSEs' financing, so the GSEs should not grant volume discounts or otherwise favor large lenders, even when serving small lenders may be more expensive.

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[83] In 2008, Fannie Mae held $729 billion in mortgage assets, compared with $231 billion at the end of 2017. Freddie Mac held mortgage assets value at $805 billion in 2008 and $253 billion in 2017. *See* Congressional Research Service, *Fannie Mae and Freddie Mac in Conservatorship: Frequently Asked Questions*, Updated May 31, 2019, at p. 16, available at https://fas.org/sgp/crs/misc/R44525.pdf.

[84] See Treasury Press Release, Obama Administration Plan Provides Path Forward for Reforming America's Housing Finance Market, Winding Down Fannie Mae and Freddie Mac (Feb. 11, 2011), available at https://www.treasury.gov/press-center/press-releases/pages/tg1059.aspx; Senior Preferred Stock Purchase Agreements, available at https://www.fhfa.gov/Conservatorship/Pages/Senior-Preferred-Stock-Purchase-Agreements.aspx.

[85] *See, e.g.*, Housing Finance Reform and Taxpayer Protection Act of 2014, S.1217, 113th Cong. (2013), referred to as the Johnson-Crapo bill, which prohibited the regulator from interfering with the unbridled discretion of the new government-backed guarantors. *See also* Joint Statement of Civil Rights Organizations, *Johnson-Crapo Does Not Provide Credit Access for Communities of Color*, March 21, 2014, available at https://www.responsiblelending.org/media/johnson-crapo-does-not-provide-credit-access-communities-color.

[86] *See* Don Layton, *What Should We Do With the GSEs? Common- Sense Reform Recommendations for the Biden Administration*, Joint Center for Housing Studies of Housing University, at p. 8 (November 12, 2020), available at https://www.jchs.harvard.edu/research-areas/working-papers/what-should-we-do-gses-common-sense-reform-recommendations-biden (discussing transition risks).

[87] Independent Community Bankers of America, *ICBA Principles for GSE Reform and a Way Forward*, at p. 6, available at https://www.icba.org/docs/default-source/icba/advocacy- documents/priorities/icbaprinciplesforgsereform.pdf ("Congress should change the GSE corporate charters…to regulated financial utilities that are shareholder owned."); Civil Rights Organizations Letter to National Economic Council (September 4, 2019), available at [https://www.banking.senate.gov/imo/media/doc/FINAL%20Civil%20Rights%20Organizations%20Principles%20for%20GSE%20Reform%20Letter%20%209.4.1.. .pdf ("Provide utility-type regulation, including regulation of products, pricing, and rates of return to further the GSEs' public mission and curb risky business practices."); Richard Cooperstein, Ken Fears, and Susan Wachter, *Working Paper: A Vision for Enduring Housing Finance Reform*, The National Association of REALTORS® (February 7, 2019), available at https://www.nar.realtor/sites/default/files/documents/2019-Working-Paper-A-Vision-For-Enduring-HousingFinance-Reform.pdf; U.S. Mortgage Insurers, *Areas of Alignment for Administrative Reform* (2019), available at http://www.usmi.org/wp-content/uploads/2019/01/White-Paper_Areas-of-Alignment-for-Administrative-Reform.pdf; Testimony of Robert D. Broeksmit, President and CEO of the Mortgage Bankers Association before the U.S. Senate on Banking, Housing and Urban Affairs, Chairman's Housing Reform Outline: Part 2, at p. 11 (March 27, 2019), available at https://www.mba.org/advocacy-and-policy/gse-reform ("MBA believes that an appropriate regulatory and supervisory framework for secondary market guarantors would be akin to a utility-style framework, in which guarantors operate as low-volatility companies with regulated rates of return that pay steady dividends over the long term. Private ownership would better encourage ongoing investment to keep pace with market demands and technological developments, but the regulator must have the authority to ensure the companies do not engage in excessive risk taking.").

Likewise, homebuyers across the country should benefit from the GSEs' special privileges, with equal pricing to all areas of the country, equitable distribution of costs from national crises such as the present, and increased pooling of risk rather than excessive pricing differences among borrowers that harm lower wealth families and perpetuate discrimination. In addition, the activities of the GSEs should be monitored so that they do not use their advantaged position to unfairly compete in other areas of the mortgage market to earn excessive returns, including the primary mortgage market. Moreover, the role of public board members should be expanded and strengthened. Finally, there is broad agreement that the GSE portfolios should continue to be limited to necessary business needs rather than holding excessive assets to arbitrage the GSEs' lower cost of debt. Financially, a utility structure produces lower, but less volatile, earnings for the GSEs and returns for their shareholders.[88] This limits the incentive for the GSEs to use their government backing to undertaken excessive risks to boost earnings, while providing support for assuring their secondary market function is stable and available to support mortgage lending.

Utility oversight is also one of the most impactful affordable housing measures for the GSEs. First, it enables and requires the GSEs to focus on affordable housing rather than trying to maximize net income and investor returns by focusing just on the most profitable mortgages to higher wealth borrowers. In addition, utility oversight substantially reduces the guarantee fees that lower wealth borrowers pay. By far, the largest component of the GSE fees paid by borrowers and added to the price of mortgages is the cost of the catastrophic capital the GSEs hold for systemic crises like the 2008 recession or a pandemic. This capital is in addition to the full loan loss reserves the GSEs hold for expected losses that may be incurred even through an economic downturn, and it is far larger than the reserves. The cost of catastrophic capital is reflected in the rate of the guarantee fees charged to borrowers, and the rate is highest on borrowers with lower credit scores and down payments, disproportionately people of color harmed by systemic discrimination.

The cost of the guarantee fees is largely determined by the amount of capital required for the loan in question multiplied by the rate of return that the GSE needs to earn on that capital. The amount of capital is much higher for lower wealth borrowers with lower down payments and credit scores. A utility structure substantially reduces this cost by lowering the rate of return that is paid to GSE investors. A lower utility return therefore measurably reduces the fee burden for lower wealth GSE borrowers.

The essential assistance provided by the GSEs during the COVID-19 crisis has reaffirmed that the GSEs should operate as utilities

The current COVID crisis has reinforced that the GSEs are critical to the housing finance system and that utility regulation is necessary to ensure they focus on their important public mission.[89] With the onset of the crisis, unemployment skyrocketed, going in March 2020 from under 4% to almost 15%, far higher than experienced in the Great Recession of 2008/9.[90] Congress responded with the CARES Act that granted consumers the right to forbearance on their GSE and federal government mortgages for up to twelve months. It was uncertain how many homeowners would need this relief, and initial estimates ran to 10 million borrowers. While the actual number of borrowers in forbearance have been lower, with a peak of less than half that, FHFA still estimates that forbearance will cost the GSEs more than $10 billion,

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[88] As with other utilities, there are many who would invest in the GSEs under this structure, viewing the GSEs as value-focused companies with sustainable dividend capacity and long-term, stable returns. *See* Eric Stein and Bob Ryan, *Treat the GSEs as Utilities*, Center for Responsible Lending (March 2020), available at https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-gse-utilities-report-mar2020.pdf; Richard Cooperstein, Ken Fears, and Susan Wachter, *Working Paper: A Vision for Enduring Housing Finance Reform*, The National Association of REALTORS® (February 7, 2019), available at https://www.nar.realtor/sites/default/files/documents/2019-Working-Paper-A-Vision-For-Enduring-HousingFinance-Reform.pdf.

[89] Richard K. Green, Anthony W. Orlando, and Susan M. Wachter, *Fannie and Freddie Are Helping American Homeowners During the COVID Recession – So Why Reprivatize Now?*, MarketWatch (Dec. 8, 2020), available at https://www.marketwatch.com/story/fannie-and-freddie-are-helping-american-homeowners-during-the-covid-recession-so-why-reprivatize-now-11607436106.

[90] Congressional Research Service, *Unemployment Rates During the COVID-19 Pandemic: In Brief* (November 6, 2020), available at https://crsreports.congress.gov/product/pdf/R/R46554.

plus carrying over $15 billion in deferred interest on loans in forbearance, a financial burden that would be debilitating to private guarantors.[91]

Because of FHFA's robust oversight of the GSEs and the GSEs' public responsibilities, the GSEs offered a payment deferral for borrowers who could afford to restart mortgage payments after forbearance. Under such a plan, the borrower's missed payments are simply added to the end of the loan, with no additional interest or penalties, rather than being due at the end of the forbearance period in a lump sum or with increased monthly payments. The GSEs absorbed the significant cost of this borrower assistance. Furthermore, FHFA was able to reduce servicer liability to advance payments during forbearance to four months by having the GSEs assume this liability, preventing servicers from collapsing due to a liquidity crisis.

The GSEs also supported continued lending as the COVID crisis hit. This provided ongoing support for home lending as the market tightened in response to the crisis. The support also enabled a massive refinance boom enabling millions of homeowners to lower their mortgage payments to historically low mortgage interest rates, making their mortgages more affordable and relieving stress on the overall economy, though these mortgage refinances have been disproportionately to higher income borrowers with more pristine credit profiles.[92]

FHFA's enhanced power through conservatorship facilitated these important benefits to homeowners and the overall economy. It is vital to maintain the GSEs' ability to respond to future crises as well as provide ongoing support to the entire housing market in normal times. A permanent utility structure would secure the essential secondary market operation that the GSEs support while limiting the conflict of interest of a private company seeking to increase returns by taking excessive risks or focusing only on the most lucrative parts of the housing market.[93]

Increased affordable housing, equity programs, and utility oversight must be implemented as part of any actions that advance the release of the GSES from conservatorship

Further reform of the GSEs may proceed administratively or legislatively, though experience to date has shown that legislative reform is very difficult and thus administrative reform is far more likely. Fortunately, HERA grants the FHFA Director the authority and discretion to place the GSEs in conservatorship, direct their operation in conservatorship, and effectuate their release.[94] Much reform of the GSEs has already been implemented administratively, including curtailing their large portfolios, and prescribing boundaries on the overall level and distinctions in its pricing to lenders and borrowers. In addition, the terms of their PSPA assistance have been amended several times to ensure they can meet their public mission. The remaining reforms, including those set out above, can likewise be executed administratively. Major industry groups, including the Mortgage Bankers Association, the National Association of Home Builders, the National Association of Realtors, and the American Bankers

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[91] ABA Banking Journal, *FHFA's Calabria: GSEs Need a Way to Recover Costs for COVID-19 Relief Programs*, September 15, 2020, available at https://bankingjournal.aba.com/2020/09/fhfas-calabria-gses-need-a-way-to-recover-costs-for-covid-19-relief-programs/; Jung Hyun Choi and Daniel Pang, *Six Facts You Should Know About Current Mortgage Foreclosures*, Urban Wire, August 18, 2020, available at https://www.urban.org/urban-wire/six-facts-you-should-know-about-current-mortgage-forbearances.
[92] In Q2 2020, refinance lending was up more than 60% from Q1 2020 and more than 200% from the same time last year, accounting for nearly 70% of all first lien originations by dollar value. Black Knight, July 2020 Mortgage Monitor, available at https://www.blackknightinc.com/black-knights-july-2020-mortgage-monitor/. *See also* Fortune, *Why It's Suddenly Harder to Get a Mortgage Than It's Been in Years* (May 10, 2020), available at https://fortune.com/2020/05/10/coronavirus-getting-a-mortgage-refinancing-credit-score/ (noting tightened lending environment and more stringent requirements).
[93] Eric Stein and Bob Ryan, *Treat the GSEs as Utilities*, Center for Responsible Lending (March 2020), available at https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-gse-utilitiesreport-mar2020.pdf; Richard Cooperstein, Ken Fears, and Susan Wachter, *Working Paper: A Vision for Enduring Housing Finance Reform*, The National Association of REALTORS® (February 7, 2019), available at https://www.nar.realtor/sites/default/files/documents/2019-Working-Paper-A-Vision-For-Enduring-HousingFinance-Reform.pdf.
[94] *See* 12 U.S.C. § 4617.

Association, have called for administrative steps towards release of the GSEs from conservatorship to continue and for them to be permitted to retain additional capital beyond the limits they will soon reach.[95]

In January 2021, Treasury and FHFA again amended the PSPAs for the GSEs, significantly increasing the permitted retention of capital by the GSEs up to a three percent capital level, which under current operations would be a total of $243 billion.[96] This amendment also tightened and continued restrictions on their retained portfolio, restricted volumes of some mortgages and set out a future dividend regime. Notably, the amendment did not give up any of the government's leverage or debt claims. All of the new retained capital continues to be added to the debt owed by the GSEs to Treasury. In addition, the provisions of the amendment can be revised or replaced in the future by joint agreement of Treasury and FHFA, leaving the ultimate resolution of the GSEs to future determination. Treasury, in an accompanying statement of its plan for the GSEs, called for utility regulation of the GSEs' pricing.

As additional steps towards the resolution of the GSEs continue, regardless of whether on a short or longer-term pace, the reforms of increased affordable housing and equity programs and utility regulation must be included in the interim and final steps or the opportunity to do so will likely be lost. First, any changes subsequently will be embodied in the PSPAs, reflecting a resolution of the positions of the GSEs, Treasury and FHFA and establishing the ongoing legal rights of the parties. Treasury has significant claims and economic leverage over the GSEs at this time, and therefore is in a position to require commitments by the GSEs to both minimize the future risk to taxpayers and ensure the GSEs increase their public mission activities.

Importantly, once the terms of the PSPAs are finally determined and the GSEs are released from conservatorship, including additional reforms will be much more difficult due to the impact on the legal operation of the GSEs. During conservatorship, the FHFA director has the full authority of the GSE officers, directors, and shareholders.[97] Therefore, while the PSPAs are structured as agreements among Treasury, FHFA and the GSEs, effectively Treasury and FHFA control the agreements. When conservatorship ends, the GSEs' authority returns to its officers and directors, and they will owe a fiduciary duty to the stockholders, including reasonable efforts to maximize net income and shareholder returns. This resurrects the conflict between the profit motive of the private shareholder owned GSEs and their public mission. After conservatorship ends, it will be difficult for the GSE officers and directors to agree to additional constraints or public obligations that may reduce their maximizing of returns. The time to include conditions and reforms is during the amendment of the PSPAs and before the release of the GSEs from conservatorship.

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[95] Letter to Treasury Secretary Steven Mnuchin from the Americans Bankers Association, Mortgage Bankers Association, National Association of Home Builders, and National Association of Realtors, Housing and Mortgage Industries' Views Regarding the Status of the GSE Conservatorship (December 14, 2020) available at https://www.aba.com/-/media/documents/comment-letter/jointltrgse20201215.pdf?rev=44e20b1f07ae45fc8d0856e0dc641775.

[96] U.S. Department of Treasury, *Treasury Department and FHFA Amend Terms of Preferred Stock Purchase Agreements for Fannie Mae and Freddie Mac*, (January 14, 2021) available at https://home.treasury.gov/news/press-releases/sm1236

[97] 12 U.S.C. § 4617(b)(2).

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