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TESTIMONY

OF

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MYCUMORTGAGE

BEFORE THE

COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS

UNITED STATES SENATE

AT A HEARING ENTITLED,

"HOUSING FINANCE REFORM: MAINTAINING ACCESS FOR SMALL LENDERS"

JULY 20, 2017

Testimony

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Senior Vice President/Chief Lending Officer

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Chairman Crapo, Ranking Member Brown, Members of the Committee:

Thank you for the opportunity to testify on this important topic. My name is Tim Mislansky, and I am the Chief Lending Officer for Wright-Patt Credit Union, headquartered in Beavercreek, Ohio, as well as the President of its wholly-owned Credit Union Service Organization (CUSO), myCUmortgage. I am also Chair of the Housing Subcommittee of the Credit Union National Association (CUNA)[1], on whose behalf I testify today.

Wright-Patt Credit Union has approximately $3.6 billion in assets, and proudly serves over 337,000 members. We are located primarily in the Dayton and Columbus, Ohio markets. This gives us a unique perspective on the marketplace as we make home loans available in the

[1] Credit Union National Association represents America’s credit unions and their 110 million members.

urban core, the suburbs and the rural areas of our markets. We are a relatively large credit union mortgage lender, and helped 4,631 families in 2015 with $616 million in balances, of which 3,072 were originated to Wright-Patt Credit Union members, and an additional 1,340 families with second mortgages, totaling $55 million.

In addition to my role at Wright-Patt, I serve as president of our wholly-owned CUSO myCUmortgage, which provides a variety of mortgage related services to nearly 200 credit unions. These credit unions range in asset size from $6 million to $1 billion and are located in 25 different states. Through the CUSO, we facilitated nearly 9,000 closings for $1.2 billion making myCUmortgage one of the largest aggregators of credit union mortgage loans in the country. These responsibilities give me a unique perspective of the mortgage lending needs of small lenders and their members.

As member-owned, not for profit financial cooperatives, many credit unions offer mortgages to satisfy member demand, and credit unions represent an increasingly significant source of mortgage credit nationally. In 2016, more than two-thirds of credit unions were active in the first mortgage arena, collectively originating over $143 billion worth of these loans – an amount equal to 7.5 percent of the total market. By comparison, in 1996 only 43 percent of credit unions were active and originated a total of less than $20 billion in first mortgages.

And third party data supports credit unions' growing presence as a mortgage lender. Most recently, Experian, one of the major credit reporting bureaus, indicated in a report that in the first quarter of 2017, credit unions accounted for 13% of the first mortgages originated, representing an increase for its 7% market share in the first quarter of 2015. [2]

It is clear that consumers are choosing credit unions more and more to be their mortgage lenders, and as Congress considers housing finance reform, it is critical that credit unions have

[2] http://www.experian.com/assets/credit-unions/reports/cu-state-of-credit-report.pdf

equitable and readily-available access to a functioning, well-regulated secondary market and a system that will accommodate member-demand for long term fixed rate mortgage products in order to ensure they can continue meeting their members' mortgage needs.

Historically, credit unions have been largely portfolio lenders. From 2000 to 2008, credit unions sold only a third of first mortgage originations, ranging from a low of 26% in 2007 to a high of 43% in 2003. The decision of whether to hold or sell a loan depends primarily on asset-liability-management issues, essentially the need to manage interest rate risk, but also at times, depends on the availability of liquidity in the credit union. Asset liability management hinges on such factors as the level of interest rates, the relative demand for fixed versus adjustable loans from members, the amount of fixed rate loans and other longer-term assets already on a credit union's books and the maturity of the credit unions funding sources. Managing credit risk is a primary concern of the credit union prudential regulator. Without a functioning secondary market, credit unions would most likely severely limit the amount of first mortgage lending conducted on behalf of their members as they simply would not have the liquidity to fund and hold the loans.

As long-term interest rates plunged in 2009 and again in 2011, credit unions found it increasingly important to sell longer-term, fixed rate mortgages to avoid locking in very low earning assets for the long term. As a result, whereas in 1996 only about 16 percent of mortgage lending credit unions sold loans into the secondary market, by 2016, nearly 30 percent of mortgage lending credit unions sold $56 billion into the secondary market, or 40 percent of total first mortgages originated by credit unions.

Servicing member loans is very important to credit unions, for a number of reasons. As member owned cooperatives, credit unions are driven by a desire to provide high quality member service. Many credit unions are reluctant to sell the core function of serving members to others. Credit unions may service loans in-house or outsource to a trusted third-party, but in doing so they maintain a say in how the loans are serviced. This is especially important when borrowers run into financial challenges so that the credit union may work to keep the borrower in their home. Credit unions are also concerned that if they sell the servicing of the mortgage loan, that the third-party servicers will use the data they gather about credit union members to market competing products or services. In addition, credit unions benefit from the steady servicing income stream. As such, many credit unions service both the substantial portfolios of loans they hold on their own balance sheets, and the loans they have sold to the secondary market. Currently, in addition to the $366 billion of first mortgages that credit unions hold in portfolio, they also service $198 billion of loans they have sold.

The credit quality of credit union first mortgages held up remarkably well during the recent financial crisis, especially when compared to the experience of other lenders. Other lenders experienced net charge-off rates four times higher than those at credit unions. Prior to the Great Recession, annual net charge-off rates on residential mortgage loans at both banks and credit unions were negligible, less than 0.1%. However, as the recession took hold, losses mounted. At credit unions, the highest annual loss rate on residential mortgages was 0.4%. At commercial banks, the similarly calculated loss rate exceeded 1% of loans for three years, reaching as high as 1.58% in 2009.

There are two reasons for this remarkable record at credit unions. First, as cooperatives, credit unions are generally locally owned, community based institutions and tend to be more borrower-centric than other lenders. This equates to credit unions generally being more risk-averse than stock-owned or privately-owned institutions. The environment faced by credit union management (generally uncompensated volunteer boards, the absence of stock options for senior management and board members, the absence of pressure from stockholders to maximize profits) discourage management from adopting high-risk, higher-return strategies in pursuit of high profits. As a result, credit union operations are more consumer-friendly, less risky and subject to less volatility over the business cycle. This largely explains why credit unions were able to increase lending as the financial crisis deepened.

Second, credit unions are member-owned cooperatives and the financial transactions involving a member's home are typically the biggest of their lives, credit unions tend to be concerned with not only the member's ability to obtain the home loan, but also to maintain the home loan. This leads credit unions to pay particular attention to such factors as a member's ability to repay a loan, proper documentation and due diligence, and collateral value before granting loans.

Credit Union Principles for Housing Finance Reform

As we have testified in the past, CUNA supports the creation of an efficient, effective, and fair secondary market with equal access for lenders of all sizes. To this end, CUNA supports housing finance reform proposals that are consistent with the following principles, and have been subject to full and fair consideration with respect to potential impact as well as unintended consequences on all market participants:

Neutral Third Party

There must be a neutral third party or parties in the secondary market, with the sole role as a conduit to the secondary market. This entity must be independent of any firm that has any other role or business relationship in the mortgage origination and securitization process, to ensure that no market participant or class of participants enjoys an unfair advantage in the system. In addition, this party must be prohibited from holding mortgage loans as individual loans or mortgage backed securities to avoid additional interest rate risk being held and managed by the entity. Some proposals have suggested that the new solution would allow financial companies to own up to 10% of an entity. This idea is troublesome as it could create potential conflicts of interest and increases the likelihood that larger lenders could band together to create and own a secondary market entity, thereby controlling the market and forcing their financial will on smaller lenders.

Equal Access

The secondary market must be open to lenders of all sizes on an equitable basis. Access should not only be provided to individual lenders, but to companies that act as loan aggregators. Despite today's relatively equal access to the GSEs, some lenders choose to work with an aggregator, such as a company like myCUmortgage, which buys loans to pool and sell to the GSEs. These institutions find it a better financial and operational alternative to partner with an aggregator than to sell directly to the GSEs. The secondary market must remain open to both direct lenders and aggregators to allow small lenders to continue making mortgage loans in the manner they choose to help consumers with home ownership.

CUNA understands that the users (lenders, borrowers, etc.) of a secondary market will be required to pay for the use of such market through fees, appropriate risk premiums and other means. However, guarantee fees or other fees/premiums should not have any relationship to lender volume. The fees must be tied to the risk of the individual loan or pools of loans.

Additionally, CUNA cautions strongly against regimes that require lenders to retain significant amounts of risk beyond that represented by actuarially appropriate guarantee fees, as these risk retention arrangements may have a disproportionately negative impact on small lenders that are less able to manage such risk or who have the balance sheet capacity to hold such risk, and could therefore result in less consumer choice.

One such example is a client of myCUmortgage, TopMark Federal Credit Union in Lima, Ohio is on pace to help their members with over $16 million in mortgage loans this year. TopMark is a $30 million depository, yet manages to generate nearly half its assets per year in mortgage loans. Without a functioning secondary market, or if onerous risk retention arrangements were imposed, TopMark may have to stop helping its members with home financing in just a few short years.

Strong Oversight and Supervision

The entities providing secondary market services must be subject to appropriate regulatory and supervisory oversight to ensure safety and soundness by ensuring accountability, effective corporate governance and preventing future fraud; they should also be subjected to strong capital requirements and have flexibility to operate transparently and develop new programs in response to marketplace demands.

Durability

Any new system must ensure mortgage loans will continue to be made to qualified borrowers even in troubled economic times. Without the backstop of an explicit federally insured or guaranteed component of any revised system, CUNA is concerned that private capital could quickly dry up during difficult economic times, as it did during the financial crisis, effectively halting mortgage lending altogether. In addition, the introduction of private capital, in a highly-regulated industry, such as mortgage lending, will be discouraged without the explicit federal guarantee. The costs and barriers to entry for other entities will most likely be high and the potential returns may not justify entry with the guarantee. This could lead to higher risk lending in order to gain short-term larger profits at great potential long-term risk as we saw during the financial crisis with exotic mortgage products and tremendously relaxed underwriting standards.

Financial Education

Credit unions have a noble history of offering a wide variety of financial counseling and other educational services to their members, and numerous studies, including an analysis from

HUD in 2016[3], have shown that first time home buyers who complete pre-ownership home buying courses perform statistically better in terms of default risk and repayment than those who do not. In one case, a study cited by HUD indicated that those who took pre-purchase education had a 1/3 less chance of ending up in default. Any new housing finance system should emphasize consumer education and counseling as a means to ensure that borrowers receive appropriate mortgage loans.

Predictable and Affordable Payments

Any new system must include consumer access to a variety of products that provide for predictable, affordable mortgage payments to qualified borrowers. Traditionally this has been through fixed-rate mortgages (such as the 30-year fixed rate mortgage), but other products that may be more appropriately tailored to a borrower's specific circumstances, such as certain borrower-friendly, standardized adjustable rate mortgages, should also be available.

We believe that in addition to ensuring access to the secondary market for credit unions, it is also important that the housing finance system Congress puts in place accommodates the demand of credit union members and other consumers for long term, fixed rate mortgage products. The data suggest that credit union members overwhelmingly prefer fixed rate mortgages. Over the past 10 years, our members have chosen a fixed rate mortgage about 80% of the time. Congress should acknowledge that the American homebuyer prefers fixed rate mortgages and do everything in its power to ensure this important mortgage product remains a valuable part of housing finance.

Loan Limits

Our nation's housing market is diverse, with wide variation geographically and between rural and urban communities. Any new housing finance system should apply reasonable

[3] The Evidence of Homeownership Education and Counseling https://www.huduser.gov/portal/periodicals/em/spring16/highlight2.html

conforming loan limits that adequately take into consideration local real estate prices in higher cost areas. It should also ensure that lower balance mortgage lending is not discouraged. Many lenders have established minimum loan amounts as the profitability of a mortgage loan is impacted by loan size. These smaller loan amounts can be typical in urban areas where the cost of a home is significantly less. For example, in Dayton, Ohio, a member can buy a home for less than $50,000 but often cannot find a lender available to them. Wright-Patt Credit Union does not have minimum loan amounts as we believe, as a financial cooperative, that we should help every qualified member buy a home regardless of the size of the home or the mortgage loan.

Affordable Housing

The important role of government support for affordable housing (defined as housing for lower income borrowers but not necessarily high risk borrowers) should be considered a function separate from the responsibilities of the secondary market entities. The requirements for a program to stimulate the supply of credit to lower income borrowers are not the same as those for the more general mortgage market. We believe that a connection between these two goals could be accomplished by either appropriately pricing guarantee fees to minimize the chance of taxpayer expense, and/or adding a small supplement to guarantee fees, the proceeds of which could be used by some other federal agency in a more targeted fashion in furtherance of affordable housing goals.

Credit unions historically have played an important part in low and moderate income mortgage lending. An analysis of publically available HMDA data from 2013 to 2015 shows that 25% of credit union lending is considered “CRA” lending. This compares to 23% for non-credit union institutions. While the difference is a relatively minor 2%, it must be remembered that credit unions are not subect to the Community Reinvestment Act, yet a larger percentage of our loans are CRA equaivelent compared to those lenders that are primarily subject to CRA.

Mortgage Servicing

In order to ensure a completely integrated mortgage experience for member-borrowers, credit unions should continue to be afforded the opportunity to retain or sell the right to service their members' mortgages, at the sole discretion of the credit union, regardless of whether that member's loan is held in portfolio or sold into the secondary market. Consumers align the mortgage loan with where they make their payment and this impacts their choices in selecting a mortgage lender. To lose control over this servicing relationship would be detrimental not only to a large majority of credit union member-borrowers, but could also result in fewer mortgage choices available to credit unions and their members, with higher interest rates and fees alike. Moreover, to the extent national mortgage servicing standards are developed, such servicing standards should be applied uniformly and not result in the imposition of any additional or new regulatory burdens upon credit unions.

Reasonable and Orderly Transition

Whatever the outcome of the debate over the housing finance system in this country, the transition from the current system to any potential new housing finance system must be reasonable and orderly, in order to prevent significant disruption to the housing market which would harm homeowners, potential homebuyers, the credit unions who serve them, and the nation's housing market as a whole.

Small Lender Access to the Secondary Market

The secondary market must be open to lenders of all sizes on an equitable basis. Credit unions need to know that as long as they produce even a single eligible mortgage, they will be able to sell it to an issuer of government-backed securities, directly or through an aggregator, at market prices, for cash, without low-volume penalty, or through the TBA market, and with the option to retain servicing on the loans. In addition, standardization of all steps of the process is very important to credit unions.

Some form of issuer should be established so that small lenders, including credit unions, will have unfettered access to the secondary market. This entity should be independent of any firm that has any other role or business relationship in the mortgage lending process..

Government Guarantee

The new system must include consumer access to products that provide for predictable, affordable mortgage payments to qualified borrowers. Traditionally this has been provided through fixed-rate mortgages (such as the 30-year fixed rate mortgage), and it is important that qualified borrowers continue to have access to products that provide for predictable and affordable mortgage payments.

In order to facilitate the continued availability of affordable, long-term, fixed rate mortgages for American homeowners, some form of ultimate government guarantee should be available for qualifying mortgage-backed securities. However, the taxpayer must be protected from the unnecessary exercise of this guarantee by appropriate standards in mortgage lending, and by layers of sufficient private capital for loss absorption. The government guarantee should be the last, not the first line of defense.

In addition to an 80% maximum loan-to-value for each mortgage in a covered security (provided by down payment, private mortgage insurance or a combination of the two), sufficient private capital should be available to absorb the first loss on any mortgage in a covered security. The amount of private capital necessary to protect the taxpayer is of course important. Too little capital places the taxpayer at risk. Too great a capital requirement unnecessarily raises the cost of mortgages to borrowers. The appropriate amount depends on: the amount of capital held by the ultimate government guarantor, the amount of loss on any security that the private capital will be responsible for (the attachment point), and the maximum loan-to-value of mortgages in covered securities and required underwriting standards for eligible mortgages. Assuming an attachment point of 10%, the amount of private capital necessary to cover a maximum 10% loss on any covered security will be substantially less than the amount necessary to cover a maximum 10% on all covered securities. So long as eligible mortgages must have maximum loan-to-value ratios of 80%, or private loan-level mortgage insurance and must comply with the Qualified Mortgage (QM) rule, the likelihood that all covered mortgage backed securities would simultaneously suffer losses of at least 10% during anything short of a total economic and financial collapse (such as the Great Depression of the 1930s) is negligible. Further, the required amount of capital or reserve funds should depend on the seasoning of the securities on which a bond guarantor provides first loss coverage. Older securities should require lower (not zero) reserve funds.

For all the reasons just listed, substantially less than 10% of the total exposure of private bond guarantors would be necessary to provide the 10% first loss coverage. Legislation should require the 10% first loss coverage, but leave it to the federal guarantor to determine the amount of private capital or reserve funds necessary to provide that 10% first loss coverage under conditions no less severe than the recent Great Recession.

In the event of the failure of a mortgage in a covered security, the federal guarantor should ensure timely payment of principle and interest to investors in covered securities, and immediately demand payment from the bond guarantor. The fact that investors could look to the federal guarantor rather than a collection of private bond guarantors for payment would contribute to the homogeneity of covered securities, increasing the liquidity of the securities. Payment from the private guarantor to the federal guarantor would be required so long as total losses on a security (or a defined group of securities, such as a vintage) had reached 10% of the value of the security. In the event total losses on mortgages in a security or group exceed 10% of the value of the security or group, the government backup fund should cover losses in excess of 10%.

It is likely that under this arrangement there could actually be instances when the government backup fund covered losses on covered securities without the bond guarantor itself having to fail, i.e., if one or more but not all of the securities covered by a private bond guarantor experienced losses of greater than 10%, but the private guarantor's capital was not depleted. Indeed, a properly reserved guarantee fund should be able to cover losses up to 10% of the balance of covered securities and still remain in business. In other words, the payment of losses by federal guarantor after the 10% first loss coverage should not require a catastrophic event, i.e., the exhaustion of a pool of private capital.

A 10% attachment point would likely make recourse to the government backup fund extremely rare, but not unheard of. A reformed housing finance system that envisages no payments out of the privately funded reserve balance of the government guarantor would be erring on the side of being too conservative. The goal should be absolute protection of taxpayers, and that should allow the federal guarantor to occasionally operate as a shock absorber, using funds it has collected from market participants. This would be similar to the way the National Credit Union Share Insurance Fund (NCUSIF) and the Federal Deposit Insurance Company (FDIC) pay depositors in failed federally insured credit unions and banks, not with taxpayer funds, but with reserves paid for by insured institutions.

The government should be prohibited from assisting private guarantors. In other words, the government should insure the mortgage bonds but not the mortgage bond issuer. Instead, the government should be prepared to quickly pay all legitimate claims not covered by a private guarantor, and to resolve the private guarantor if the government is not reimbursed for such claims in a timely fashion. The government should also be prepared to temporarily sell first loss coverage to issuers in times of market stress.

The entity that provides the government guarantee should also have regulatory responsibility. Since the entity that provides the government guarantee will be responsible for protecting the taxpayer from losses resulting from that guarantee, that entity must have the authority to establish regulations to ensure that all of the many players in the complex housing finance system act in a fashion that does not expose the taxpayer to any losses.

Underwriting and Other Mortgage Standards

Ultimately, the underwriting standards for a loan to qualify for inclusion in a covered security should be controlled by the government entity responsible for covering losses on such securities. A similar system has worked fairly well for the FDIC and NCUSIF in establishing prudential standards for bank and credit union operation. Therefore, the less explicitly underwriting standards are prescribed in legislation, the better. Whereas QM standards could serve as a starting point for standards established by the federal issuer, the law should not explicitly require that only QM loans could be eligible mortgages. The ability of a borrower to repay a loan depends on a number of characteristics; not just the absolute level of each characteristic, but also the interplay among those characteristics. Many of the underwriting standards of the QM rule are appropriate for an eligible mortgage: documentation requirements, payment and debt ratio calculation methods, prohibition of harmful loan features such as negative amortization, etc. But a bright line ceiling of 43% on the debt-to-income ratio, without any ability to consider other factors, would exclude too many qualified borrowers from enjoying the benefits of covered mortgages. For example, consider a borrower applying for an adjustable rate mortgage with annual adjustments after one year, a low down payment and a barely prime credit score. For such a borrower, even a 43% debt ratio could be far too high. However, for another borrower applying for a 30-year, fixed-rate loan with a large down payment, an active and pristine credit record and other positive characteristics, a 50% debt ratio could be completely acceptable.

The federal issuer should be instructed by Congress to create standards that facilitate consumer access to mortgage credit consistent with the overriding goal of minimizing risk to the taxpayer of paying for losses on covered securities, recognizing that those standards should evolve through time. Those standards may be similar to QM standards, but should not be required to be the same as QM standards.

This system currently exists with Fannie Mae and Freddie Mac. Their underwriting standards are the standards of the mortgage industry. A new or revised system should build upon these standards rather than start from scratch. In addition, the current GSE system has developed standardization across the mortgage industry in the Uniform Residential Loan Application, loan documents, appraisal standards, income calculation and many other areas. These standardizations have benefited consumers and lenders by creating consistency and efficiency in the market place and contribute to a well-functioning secondary market. As a new secondary market is envisioned, these standardizations must be considered so that standardization in mortgage lending remains. The unintended consequences of a failure to continue the standardization would be higher costs to borrowers and a sort of wild-west of mortgage lending in relation to a secondary market.

Regulatory Structure

The entities providing secondary market services must be subject to appropriate regulatory and supervisory oversight to ensure safety and soundness, for example by ensuring accountability, effective corporate governance and preventing future fraud; they should also be subjected to strong capital requirements and have flexibility to operate well and develop new programs in response to marketplace demands.

The regulator created through any reform of the housing finance system must have a role centered on supporting securitization that does not duplicate the role of other regulators in the process. Both issuers and servicers are heavily regulated by a myriad of federal agencies, including the Bureau of Consumer Financial Protection (CFPB), Department of Housing and Urban Development, Department of Veteran Affairs and Department of Agriculture, in addition to the supervision performed by prudential regulators. Credit unions and other small lenders are drowning in regulation in the mortgage area, and we fear curtailing products and services as a result. Credit union members, and our housing recovery, lose as a result of regulatory burden. It is essential that any housing finance reform not create additional regulatory burden at the originator or servicer level; in fact, if done properly, the implementation of a new housing finance system could provide an opportunity to reduce credit unions' and other small lenders' regulatory burden, as we discuss later in this testimony.

That said, the secondary market needs strong regulatory oversight to ensure equal access for small institutions and an orderly functioning of the system. At a high level, the regulator should be a neutral third party that would ensure the secondary market is open to lenders of all sizes on an equitable basis, with equal pricing regardless of lender volume. Ideally, the regulator would provide issuers who feel they are not receiving equal treatment in the secondary market with an administrative process to protest. In turn, the regulator should have substantial authority to order a remedy, including banning a violating secondary market participant from accessing the federal issuer.

We envision a regulator in the mold of the National Credit Union Administration (NCUA) or the Federal Deposit Insurance Corporation (FDIC), with direct examination and supervisory authority, given that the full faith and credit of the United States stands behind the federal backstop, as it does with NCUA or FDIC insurance. The entities providing secondary market services must be subject to appropriate supervisory oversight to ensure safety and soundness, for example by ensuring accountability, effective corporate governance and preventing future fraud; they should also be subjected to strong capital requirements and have flexibility to operate well and develop new programs in response to marketplace demands. In terms of specific powers, at a minimum, the regulator should have the authority to make rules, examine and supervise secondary market participants, suspend or revoke the power of any secondary market participant to enjoy a federal backstop, place any secondary market participant into conservatorship or involuntary liquidation and study the operation of the secondary mortgage market to determine if its regulations are leading to the most efficient operation.

In terms of the regulator's governance structure, we recommend a board appointed by the President with the advice and consent of the Senate that would serve for fixed terms of five or more years (so as to be longer than the term of any one President). It is important for credit unions that, by statute, the board be required to include credit union representation. The board members should have minimum qualifications set by statute and come from the private marketplace, not be representatives of another regulatory agency. We leave it to Congress to set the minimum criteria for service on the board, but note that a minimum of 10 years of mortgage lending experience should provide the operational knowledge necessary to understand issuer concerns. Staggering terms of service makes sense to ensure continuity of the board.

The regulator could be funded by a small portion of the guarantee fee. We believe the regulator should have an Office of Small Lender Access and Equality, dedicated to the concerns of credit unions and banks under a certain threshold in assets. That office should have the authority to study the pricing small institutions receive in the secondary market to determine if small institutions receive fair pricing.

In terms of the regulatory issues surrounding "too big to fail" and the housing regulator's interaction with other regulators, the new housing regulator should have a seat on Financial Stability Oversight Council (FSOC) and generally should be given similar authority as the FDIC and Federal Reserve over systemically important entities under the Dodd-Frank Act. The regulator should be required to consult with FSOC before placing a systemically important secondary market participant into conservatorship. To the extent not already the case under current law, any non-bank that is a participant in the secondary market should be subject to a possible systemically important designation, and should have to draft a “living will” if so designated. The new regulator should have a direct role in reviewing the living wills of any secondary market entity, as is the case with the FDIC and Federal Reserve. Where state-chartered entities, including insurance companies, are concerned, the company would be resolved under state law, but the federal housing regulator would have the authority to step in to handle that resolution if the appropriate state authority did not take what the regulator deemed to be the necessary action, as is true of the FDIC’s similar authority under the Dodd-Frank Act.

Servicing Standards

Credit unions should continue to be afforded the opportunity to provide mortgage servicing to their members in a cost-effective and member-service oriented manner, in order to ensure a completely integrated mortgage experience for credit union members. To lose this servicing relationship would be detrimental not only to a vast majority of credit union members, but could also result in fewer mortgage choices available to credit unions and their members, with higher interest rates and fees being imposed on both.

Initial national mortgage servicing standards will likely be part of the common securitization platform being developed under the auspices of FHFA. They should be applied uniformly and not result in the imposition of any additional or new regulatory burdens upon credit unions. Going forward, private market participants should be able to revise servicing standards subject to oversight by the successor issuer(s), which should also have legal authority to ensure that the development and implementation of all servicing standards are reasonable and fairly applied for all servicers; legislation should ensure that eligibility requirements, compensation to or fees collected from servicers are not strictly based on volume but also reflect other reasonable factors such as in the case of compensation, the performance of the loans serviced.

To ensure that all servicers are treated fairly and appropriately by the mutual securitization company, the legislation should establish an ombudsman to interact with servicers and create a review process under which complaints raised by servicers will be investigated and resolved in a timely manner.

The regulation of servicing should be bifurcated with the successor federal issuer(s) overseeing how standards for servicing necessary to support securitization are developed while the protection of consumers in the servicing process should be left to the CFPB. In other words, no entity should be granted authority to impose any additional consumer protection servicing requirements on regulated financial institutions that service mortgage loans. Such protections have already been established under a statutory and regulatory framework under the purview of the CFPB. While improvements to the current framework, such as changes to the servicers' exemption levels to ensure regulatory burdens on smaller servicers are minimized, should be considered, the regulation and oversight of the servicing process, including standards, should be left to the CFPB.

Transition Issues

The transition from the current system to any new housing finance system must be reasonable and orderly. The transition should end when the new system is fully functional, rather than after any specified period. Further, we recommend that the common securitization platform now being developed under the direction of the FHFA should be available to all market participants. Finally, once the earnings of the GSEs have fully paid back all government costs of their conservatorship, any further GSE earnings during the transition should be available to cover costs of standing up the new system, and beginning the funding of the reserve balance of the successor issuer(s).

The Federal Credit Union Act limits the types of investments that credit unions can hold. Since government agency securities are one of the few investments allowed, they tend to purchase and hold many of these securities. Therefore, in order to ensure the safety and soundness of credit unions, and to ensure the new securities perform on par as the current GSE securities we suggest a phased in approach to issuing the new security that would be blended with the Fannie and Freddie issued securities to ensure the investments hold their value and market stability is maintained.

To minimize market disruption, we would suggest that Fannie Mae, Freddie Mac and the new issuer be allowed to operate simultaneously so that all parties can get acquainted with the new system. In addition to gaining familiarity with the new system, it would be appropriate for both the GSE's and the new issuer to start issuing securities with each trying to mirror or have very similar characteristics of the other. As the last step in the process before Fannie Mae and Freddie Mac are wound down, blending the two securities together and selling them for a period of time under the new issuer name may provide the market the necessary time to become comfortable with the new security. Ideally, market participants will not notice any sudden changes on the day that the GSEs are shuttered and the new system takes over. The many changes necessary to move from the old to the new system would already have happened gradually during the transition.

Finally, the common securitization platform now being developed under the direction of the FHFA should be available to all market participants. It could be "owned" and controlled by the new issuer, or a separate entity made up of all issuers of covered securities. Its use should be required for all covered securities, which would likely make it the default for private label securities. Regardless of who owns it, if its use were required for all covered securities, the new issuer would have de facto regulatory control over it.

Additional Concerns Specific to Credit Unions

Statutory limitations restrict the ability of credit unions to more fully serve their members and may inhibit their ability to be complete participants in the reformed housing finance system. Therefore, we would strongly encourage the Committee to consider the following statutory changes specific to credit unions as part of the reform of the housing finance system.

Investment Authority

Section 107(7) of the Federal Credit Union Act (12 USC 1757(7)) limits the types of investment that Federal Credit Unions may make to loans, government securities, deposits in other financial institutions, and certain other limited investments. We believe that depending on the nature of the entity created as a successor to the GSEs, credit unions may need additional investment authority in order to capitalize that entity, and we encourage the Committee to provide that authority.

Multifamily Housing

Credit unions are not significant participants in the multifamily mortgage market primarily because of the statutory cap on business lending imposed in 1998. This cap limits credit unions business loan portfolio to essentially 12.25% of the credit unions assets. Compounding the matter, the Federal Credit Union Act considers a loan made on a 1-4 family non-owner occupied residence a business loan; whereas the same loan made by a bank would be considered a residential loan. Comprehensive housing finance reform legislation may provide the opportunity to correct this disparity in the statute. We encourage the Committee to include language that would amend the Federal Credit Union Act and consider loans made on 1-4 family residential properties as residential loans.

Relief from Dodd-Frank Act Mortgage Regulations

As Congress considers comprehensive housing finance reform legislation, it also may be prudent to consider changes to Dodd-Frank Act related mortgage regulations. The CFPB has finalized many thousands of pages of regulations with which credit unions and other community-based financial institutions must comply, despite the fact that they did not cause the mortgage crisis and have, throughout history, employed the strong underwriting principles the rules are designed to require.

The compliance obligations imposed by these rules – some of which were finalized in September and are effective in January – are simply overwhelming to many credit unions, and the tight timeframe for compliance puts the availability of mortgage credit at risk. While there has been suggestion by the CFPB and other regulators that they may not cite financial institutions for noncompliance for a period of time after the compliance date, the law carries a private right of action which would make credit unions and others vulnerable to lawsuits for noncompliance even as they work in good faith toward compliance. Another year would ensure that mortgage credit remains available to millions of credit union members while credit unions all over the country continue to understand how to implement the most sweeping regulatory changes to mortgage lending in U.S. history, and would be welcome relief to credit unions. We encourage Congress either through this legislation or as a separate bill to address this issue.

In addition to addressing the compliance dates of the mortgage regulations, we encourage the Committee to address several other areas of the mortgage regulations, including the definition of points and fees for the purposes of the CFPB's ability-to-repay rule, the credit risk retention requirements for the "qualified residential mortgage" rule and changes to the qualified mortgage rule.

We note that legislation has been considered which would exclude from the definition "all title charges, regardless of whether they are charged by an affiliated company, provided they are bona fide and reasonable." Defining points and fees in this way will maintain a competitive marketplace, prevent over-pricing or limited choice in low-moderate income areas and allow consumers to enjoy the existing benefit of working through one entity for their new mortgage or refinance. A statutory revision would make this definition clearer and stronger than the CFPB's amended rule.

We hope the Committee will also consider including language in the housing finance reform bill to repeal the credit risk retention requirement in the "qualified residential mortgage" rule, and to allow the consumer to waive the requirement that mortgage disclosures be provided to the consumer three business days before closing.

Finally, we encourage the Committee to consider language to repeal the defense to foreclosure provision of the Dodd-Frank Act. The litigation risk created by the defense to foreclosure provision has caused many credit unions to worry that prudential examiners will severely restrict the ability of credit unions to keep non-QM loans that do not enjoy the QM rule's safe harbor in their portfolio after the rule goes into effect. This would make QM the effective requirement for safety and soundness and risk mitigation purposes. These changes would do a great deal to alleviate the very real concern of credit unions that they will not be able to offer mortgages to their members who do not meet all of the QM standards but who nevertheless have the ability to repay a mortgage loan. These changes will also help facilitate the kind of creative products that are possible through portfolio lending that individualize the process of getting a mortgage based on the individual circumstances of each member.

Conclusion

We are encouraged that the Committee has engaged in a process to consider comprehensive housing finance reform. Unquestionably, the housing finance system is in need of repair. A conservatorship is not meant to last nearly a decade. It is critical that Congress get reform legislation right as it impacts the overall economy and perhaps more importantly, the housing needs of Americans. We appreciate that the Committee has sought our views on this legislation and look forward to providing continued assistance as the legislation moves through the process. On behalf of America's credit unions and their 110 million members, thank you for your consideration of our views.