August 25, 2000

The Honorable Richard H. Baker, Chairman
House Subcommittee on Capital Markets, Securities
and Government Sponsored Enterprises
434 Cannon House Office Building
Washington, D.C. 20515

Dear Chairman Baker:

AARP appreciates this opportunity to submit an initial set of comments regarding, HR 3703, the "Housing Finance Regulatory Improvement Act of 2000", introduced by Chairman Leach and you on February 29, 2000. The proposed legislation represents the culmination of an extensive round of Subcommittee oversight hearings on the roles of Fannie Mae (formerly the Federal National Mortgage Association), Freddie Mac (the Federal Home Loan Mortgage Association), and the Federal Home Loan Bank System in the nation's credit and housing markets. The goals of HR 3703 are to:

- reduce an implicit GSE default liability for American taxpayers – a liability attributed to their federal charters, and
- increase competition within the general mortgage credit market in an effort to further reduce the cost of buying a home.

As government sponsored enterprises, Fannie Mae and Freddie Mac are privately owned, but federally chartered companies created by Congress to overcome market barriers to the flow of credit necessary to meet the nation's housing needs. Fannie Mae and Freddie Mac are publicly traded companies. The Federal Home Loan Banks (FHLBs) are cooperatives owned by their member banks and thrifts. [Because the structure and issues associated in HR 3703 with FHLBs are different from those of Fannie Mae and Freddie Mac, the Association will defer commenting on FHLBs at this time.]

For over 50 years it has been an explicit national goal to provide "a decent home and a suitable living environment for every American family". For AARP members as well as for the wider community of mid-life and older Americans that the Association serves, the availability and affordability of suitable housing are key components of the continuing American Dream – whether that housing is owned or rented. Research sponsored by AARP in 1995 indicated that 4-out-of-5 homeowners age 65 and older owned their home free and clear. This is not only a measure of success of the existing housing finance system, but also a measure of the enduring value and dedication that most Americans have toward owning a home. This year the Census Bureau reports that aggregate American homeownership is at a historical high of 67.1 percent.

Major demographic transformations continue to change the shape of the nation's housing needs and problems. For example, despite the progress made in improving housing conditions, many older Americans continue to experience serious housing problems because of substandard conditions, affordability, and inappropriateness for "aging in place". Rapid growth of our older population accentuates the need for housing options that can accommodate their diverse needs. Projections by the Census Bureau indicate that by 2020, the older population (age 65 and older) will have grown to 53 million, a 55 percent increase from 34 million in 1998.

Fannie Mae and Freddie Mac have made important financial innovations and investment contributions over the last 30 years which must be sustained, which have helped to produce a remarkable growth in homeownership in the United States. At the same time, the financial prominence and public mission of Fannie Mae and Freddie Mac warrant continuous oversight, analysis and assessment. A similar scrutiny, risk analysis and constructive criticism should be employed in comparing and evaluating the premises and promises implied by proposals for reform of the system. AARP maintains that the best test of housing GSEs performance, or proposals to change their role, is how well the <u>full range</u> of housing needs of the nation will be met.

It is worth noting that the basic structure of our housing finance system has adapted well to changing needs and demands. In 1989, as part of the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA), Congress <u>restated</u> Fannie Mae's and Freddie Mac's charters, directing that these two GSEs "provide stability" and "ongoing assistance to the secondary mortgage markets." Subsequently, the Federal Housing Enterprise Financial Safety Act of 1992 (FHEFSA) provides that the GSEs "have important public missions that are reflected in the statutes and charter acts establishing the [Federal Home Loan] Banks and the enterprises." The present charters and supporting statutes governing Fannie Mae and Freddie Mac charge them with:

- providing stability in the secondary market for residential mortgages;
- remaining in and promoting access to the mortgage credit market throughout the nation by operating in all 50 states in all economic climates; and
- meeting specific and binding affordable housing goals designed to improve the flow of mortgage funds to low and moderate-income families.

As the Subcommittee's hearings and recent agency, academic and research forums attest, much has been accomplished. For example, Fannie Mae and Freddie Mac have negotiated agreements with HUD to significantly increase their purchase of low and moderate residential mortgages. But more needs to done in this market as well as in the purchase of multifamily mortgages. Progress has been made in engaging Fannie Mae and Freddie Mac in efforts to reduce the prevalence of predatory lending practices through tightening of their underwriting guidelines. Efforts have been launched to make more information available to potential home buyers regarding the calculation and meaning of personal credit scores. Here again more can be done.

Mr. Chairman, HR 3703 seeks to further enhance the performance of the nation's mortgage credit markets by:

- consolidating the regulation of Fannie Mae and Freddie Mac into one, new independent regulatory board, replacing the independent Office of Federal Housing Enterprises Oversight (OFHEO) with its current responsibility for safety and soundness compliance, as well as the responsibility shouldered by the U.S. Department of Housing and Urban Development (HUD) for compliance in meeting obligations for low and moderate income housing goals;
- granting the new regulatory board with the authority to approve new activities as well as ongoing charter compliance;
- eliminate Fannie Mae's and Freddie Mac's lines of credit to the U.S. Treasury;
- requiring annual enterprise credit ratings; and
- requiring a study of a GSE failure effects on deposit institutions.

AARP appreciates the merit of assessing the GSEs during a period of prosperity rather than crisis. However, the Association has a number of concerns regarding the potential for counterproductive side effects from implementation of HR 3703:

- As the market in U.S. Treasury securities is reduced, will the change to and effect of the proposed regulatory regime be as smooth as theorized, or will the transition destabilize the value of existing GSE financial instruments, including those with GSE guarantees, held not only by federally-insured deposit insurance institutions and the FHLBs, but also life insurance companies and finance companies, mutual funds and private investors, and public as well as private pension funds;
- Will the bill's provisions to increase GSE transparency by further tightening mandatory review for existing as well as new products and services by a new board have the unanticipated side effect of choking off the GSE's ability to innovate, and transferring competitive advantage to strictly private sector firms whose proprietary interests will be shielded from public review;
- Does this proposal then raise the prospect that Fannie Mae and Freddie Mac may seek to reduce their commitments to affordable housing goals, choking off an increasingly productive public-private sector collaborative role, without obtaining any comparable commitments from strictly private sector firms. Historically, low and moderate income individuals and housing developments have been neglected without such institutional commitments; and
- Given the progress that has been made in capacity-building by OFHEO and the pending risk-based capital rules for assessing the safety and soundness of Fannie Mae and Freddie Mac, is now the time to be substituting another new and uncertain regulatory regime -- particularly following on the heals of last year's enactment of financial modernization legislation, and the consolidation and change now underway in the financial services industry?

In summary, the Association's concern with HR 3703 is that too little consideration has been given to the aggregate impact of the proposed changes on achievement of low and moderate income housing goals, and its potential for destabilizing financial markets it seeks to enhance.

AARP stands ready to work with you, the Subcommittee and the residential mortgage industry -- including Fannie Mae and Freddie Mac -- on the full range of challenges facing our nation's housing finance. system. Specifically, the Association is committed to maintaining a stable system, with improved credit risk management, but that preserves and hopefully enhances the nation's efforts, and to lowering the cost of mortgage credit, and to include products and services from which low and moderate income families can benefit. If you have any questions, please do not hesitate to call me or ask your staff to contact Roy Green of AARP's Department of Federal Affairs at (202) 434-3800.

Sincerely,

Martin A. Corry
Director
Federal Affairs