Selected Legislative Proposals to Reform the Housing Finance System

Sean M. Hoskins
Analyst in Financial Economics

N. Eric Weiss
Specialist in Financial Economics

Katie Jones
Analyst in Housing Policy

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Summary

The 113th Congress has seen several developments in the effort to reform the housing finance system. In the House, the Protecting American Taxpayers and Homeowners Act of 2013 (PATH Act; H.R. 2767) proposes to wind down Fannie Mae and Freddie Mac (the government-sponsored enterprises, or GSEs) and to reform the Federal Housing Administration (FHA). H.R. 2767 was ordered to be reported out of the House Financial Services Committee on July 24, 2013. In the Senate, two bills have been the subject of much discussion. Republican and Democratic members of the Senate Committee on Banking, Housing, and Urban Affairs have sponsored the Housing Finance Reform and Taxpayer Protection Act of 2013 (S. 1217; commonly referred to as the Corker-Warner bill), which proposes to wind down Fannie Mae and Freddie Mac and to replace them with a new reinsurance plan. The FHA Solvency Act of 2013 (S. 1376; commonly referred to as the Johnson-Crapo bill), which would reform FHA, was reported out of the Senate Committee on Banking, Housing, and Urban Affairs on July 31, 2013.

The PATH Act proposes to wind down Fannie Mae and Freddie Mac over several years. In this context, wind down refers to dissolving Fannie Mae and Freddie Mac by removing their charters and placing certain assets and liabilities into a receivership entity. It would replace them with a National Mortgage Market Utility that would facilitate private market mortgage securitization but would not provide a government guarantee. The PATH Act would retain in a modified form the existing government guarantee programs, such as the FHA. The act would also eliminate or delay the implementation of certain existing regulations that some believe are inhibiting the recovery in the mortgage market. In addition, the PATH Act proposes to reform FHA by, among other things, making it an independent agency and taking steps to improve its finances.

The Corker-Warner bill proposes to wind down Fannie Mae and Freddie Mac and to replace the Federal Housing Finance Agency (FHFA) with a new Federal Mortgage Insurance Corporation (FMIC). The FMIC would be an independent agency charged with supporting the mortgage market and providing reinsurance on eligible mortgage-backed securities (MBS). These MBS would have an explicit full-faith-and-credit federal government guarantee. The FMIC would only pay out on its guarantee after a significant amount of private capital absorbed the first losses. In addition, the FMIC would regulate aspects of the mortgage market related to its guaranteed MBS.

The Johnson-Crapo bill proposes a number of changes to FHA aimed at ensuring that FHA's single-family programs are financially sound, including a number of provisions that have been sought by FHA.

This report will briefly explain the different approaches to housing finance reform proposed by these three bills, focusing on efforts to replace Fannie Mae and Freddie Mac and reform FHA. The report does not describe every provision of the proposals but discusses major concepts and themes.

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Introduction

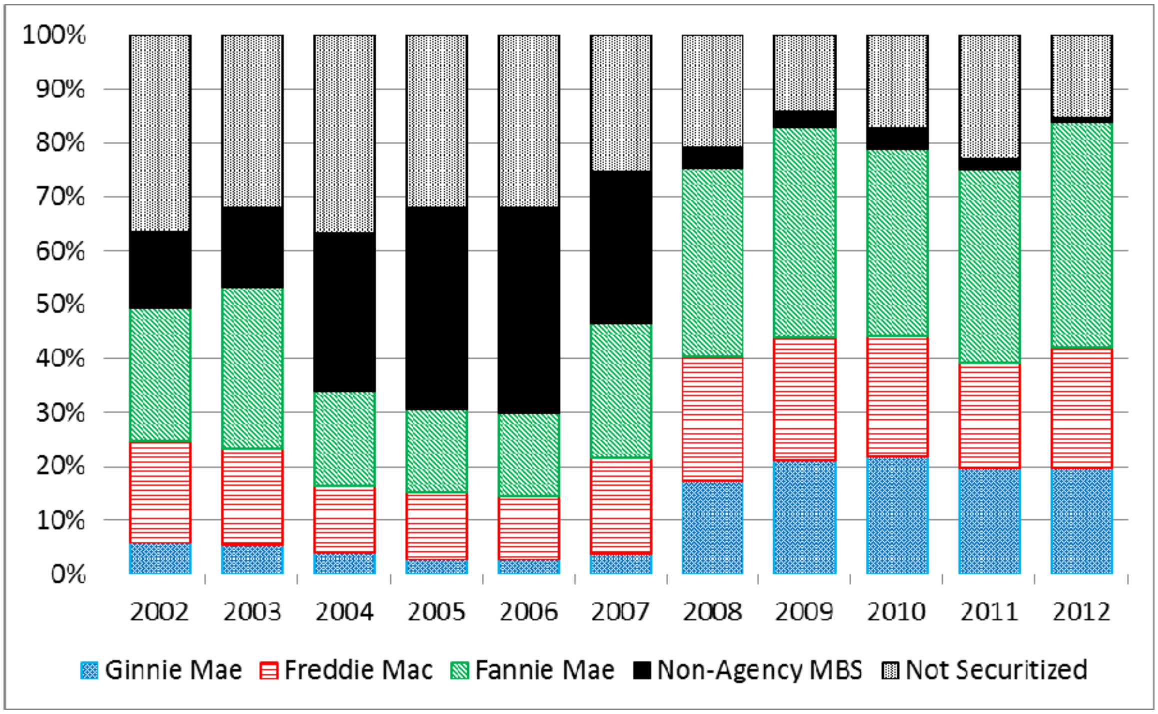
The bursting of the housing bubble in 2007 and the multi-year downturn in the housing and mortgage markets have led some to question whether the pre-crisis structure of the housing finance system is appropriate for the future. Many different housing finance reform plans have since been proposed, and from the debate several generally agreed upon principles have emerged. Among those principles is the belief that reform should

- **Prevent taxpayers from having to provide assistance again in the future.** Fannie Mae and Freddie Mac—two government-sponsored enterprises or GSEs—experienced significant financial losses when house prices fell and foreclosure rates increased. The GSEs were placed in conservatorship by their regulator, the Federal Housing Finance Agency (FHFA), in September 2008.[1] Five years later, the GSEs remain in conservatorship and have received approximately $187 billion in assistance in the form of senior preferred stock purchased by the Department of the Treasury. Though the GSEs have made significant dividend payments to the Treasury since entering conservatorship, none of these payments count toward paying back the amount injected by Treasury. The dividends compensate Treasury for its assistance and the risk it has assumed. Furthermore, there are concerns that the Federal Housing Administration (FHA), an agency within the Department of Housing and Urban Development (HUD) that provides federal mortgage insurance, could soon need to draw on permanent and indefinite budget authority with Treasury to have enough funds to hold in reserve to pay for increases in expected future losses on the mortgages that it currently insures.[2]
- **Return private capital to the mortgage market.** The increased role of the federal government in the mortgage market since 2008 is shown in **Figure 1**. In addition to Fannie Mae and Freddie Mac, the government guarantees mortgage loans through FHA, the Department of Veterans Affairs (VA), and the U.S. Department of Agriculture (USDA). The government backs mortgage-backed securities (MBS) composed of FHA, VA, and USDA mortgages through Ginnie Mae, an agency within HUD. Since 2008, Ginnie Mae and the GSEs have collectively provided funding for approximately 75% to 85% of mortgage originations.

[1] For more on the financial status of the GSEs, see CRS Report R42760, *Fannie Mae's and Freddie Mac's Financial Status: Frequently Asked Questions*, by N. Eric Weiss.

[2] In general, FHA is supposed to earn enough money in fees to cover the costs of mortgages that default. However, like all federal credit programs, FHA has permanent and indefinite budget authority with Treasury to cover higher-than-expected future losses. For more on the financial status of FHA, see CRS Report R42875, *The FHA Single-Family Mortgage Insurance Program: Financial Status and Related Current Issues*, by Katie Jones.

Figure 1. Mortgage Categories



Source: Inside Mortgage Finance, *Mortgage Market Statistical Annual: 2013*, Volume II: The Secondary Market, p. 2 and 4, and CRS calculations.

Notes: The figure shows annual funding and origination sources. Note that not all mortgages that were securitized in a given year were actually originated in that year.

- **Ensure that mortgage credit is available and affordable to creditworthy borrowers.** During the housing downturn, underwriting criteria for mortgages generally tightened, requiring higher credit scores and higher downpayments.[3] Some borrowers had a more difficult time financing the purchase of a home. Reform proposals would attempt to make mortgage credit and certain mortgage products, such as the 30-year fixed-rate mortgage, both available and affordable to creditworthy borrowers.

Although different plans have similar goals, their different diagnoses of the market have led to divergent proposals. Some believe that private capital has been slow to return to the mortgage market because the government (through Fannie Mae, Freddie Mac, and FHA) is crowding out the private sector and because there are insufficient standards for the private sector to function appropriately. By shrinking the government's footprint and by establishing "rules of the road," the argument goes, the private sector will step up to fill the government's void. Others argue that while the government may need to reduce its role, the main impediment to the private sector returning is a lack of appetite for risk among private investors. They argue that the government must continue to provide some type of guarantee to ensure that the mortgage market will continue to provide credit at an affordable rate to creditworthy borrowers.

[3] For example, the average credit score of mortgages purchased by Freddie Mac has increased since 2006. See Freddie Mac, *Freddie Mac Update*, August 2013, at http://www.freddiemac.com/investors/pdffiles/investor-presentation.pdf.

The 113th Congress has seen several developments in the effort to reform the housing finance system. In the House, the Protecting American Taxpayers and Homeowners Act of 2013 (PATH Act; H.R. 2767), which proposes to wind down the GSEs and would reform FHA, was ordered to be reported out of the House Financial Services Committee on July 24, 2013. In the Senate, two bills have been the subject of much discussion. Republican and Democratic members of the Senate Committee on Banking, Housing, and Urban Affairs have sponsored the Housing Finance Reform and Taxpayer Protection Act of 2013 (S. 1217; popularly known as the Corker-Warner bill), which proposes to wind down Fannie Mae and Freddie Mac and to replace them with a new reinsurance plan. Unlike the PATH Act, the Corker-Warner bill does not address FHA. However, the Banking Committee has also ordered to be reported a separate FHA reform bill, the FHA Solvency Act of 2013 (S. 1376; popularly known as the Johnson-Crapo bill).[4]

This report will briefly explain the different approaches to housing finance reform proposed by these three bills, focusing on efforts to replace Fannie Mae and Freddie Mac and reform FHA. The report does not describe every provision of the proposals but discusses major concepts and themes. The next section will provide a brief overview of some of the major entities in the housing finance system to lay the foundation for the ensuing discussion of legislative proposals.

The Role of the GSEs and FHA in the Housing Finance System[5]

The housing finance system has two major components: a *primary market* and a *secondary market*. Lenders make new loans in the primary market, and loans are bought and sold in the secondary market. The federal government is involved in both markets. The government insures certain mortgages originated by lenders in the primary market through different government agencies, with FHA as the largest provider of government mortgage insurance. FHA is an agency within HUD that provides mortgage insurance on loans that meet its requirements (including a minimum down payment requirement and an initial principal balance below a certain threshold) in exchange for fees, or premiums, paid by borrowers. If a borrower defaults on an FHA-insured mortgage, FHA will repay the lender the entire remaining principal amount it is owed. In the secondary market, Ginnie Mae—also a government agency in HUD—guarantees MBS[6] composed of mortgages guaranteed by FHA and other government agencies. The combination of FHA and Ginnie Mae transfers the credit risk (the risk that some borrowers might default and not repay their mortgages) from the lender and investor to the government.

[4] This report will describe H.R. 2767, S. 1217, and S. 1376. Additional pieces of legislation have been introduced in the 113th Congress to reform the housing finance system, but those proposals are beyond the scope of this report. For information on reform proposals in the 112th Congress, see CRS Report R41822, *Proposals to Reform Fannie Mae and Freddie Mac in the 112th Congress*, by N. Eric Weiss and CRS Report R42875, *The FHA Single-Family Mortgage Insurance Program: Financial Status and Related Current Issues*, by Katie Jones.

[5] For a more comprehensive overview of the housing finance system, see CRS Report R42995, *An Overview of the Housing Finance System in the United States*, by Sean M. Hoskins, Katie Jones, and N. Eric Weiss.

[6] An MBS is a bond that is collateralized by mortgages. The creation of an MBS typically involves a financial institution acquiring and pooling together many different mortgages and then issuing an MBS. An MBS could be divided up into different pieces, or tranches, that are sold to investors. The investors do not own the underlying mortgages but are buying the right to receive the future stream of payments that come from those mortgages.

Fannie Mae and Freddie Mac also operate in the secondary market. Until they were placed under government conservatorship in September 2008, Fannie Mae and Freddie Mac were stockholder-controlled companies with congressional charters that contain special privileges and certain special responsibilities to support affordable housing for low- and moderate-income households. The GSEs do not originate mortgages. Instead, the GSEs purchase conforming mortgages—mortgages that meet certain eligibility criteria based on size and creditworthiness—and either hold the mortgages in their own portfolios or pool the mortgages into MBS. The MBS are sold to investors or retained by the GSEs as investments. The GSEs guarantee that investors will receive timely payment of principal and interest on their MBS even if a borrower with a mortgage that is part of the MBS becomes delinquent. The GSE guarantee transfers the credit risk from the investors to the GSEs. To compensate the GSEs for their guarantee, the GSEs receive a guarantee fee.

When individuals discuss "bringing private capital back into the mortgage market," they often are referring to having private capital absorb credit risk rather than the government doing so through Fannie Mae and Freddie Mac or programs such as FHA. Private investors still bear other risks when they purchase MBS guaranteed by the GSEs or the government, such as risks related to the interest rate, but do not bear credit risk.

Reform Proposals

This section explains how the PATH Act and the Corker-Warner bill propose to wind down[7] the GSEs and would attempt to attract private capital back into the market. It also describes how the PATH Act and the Johnson-Crapo bill would reform FHA.

H.R. 2767, the Protecting American Taxpayers and Homeowners Act of 2013

The PATH Act (H.R. 2767)[8] proposes to wind down Fannie Mae and Freddie Mac over several years. It would replace them with a National Mortgage Market Utility that would facilitate mortgage securitization but would not provide a government guarantee. The act would also eliminate or delay the implementation of certain existing regulations that some believe are inhibiting the recovery in the mortgage market. In addition, the PATH Act would reform FHA, making it an independent agency and taking steps to improve its finances.

Phase Out of Fannie Mae and Freddie Mac

The phase out of Fannie Mae and Freddie Mac involves two stages, actions taken during the first five years before the GSEs' charters are repealed and actions subsequently taken.

First five years after enactment. The PATH Act proposes several steps to limit the GSEs' new business. The GSEs would only be allowed to purchase or guarantee mortgages that meet the

[7] In this context, wind down refers to dissolving Fannie Mae and Freddie Mac by removing their charters and placing certain assets and liabilities into a holding company, trusts, or receivership entity.

[8] This section describes the PATH Act as it was ordered to be reported out of the Financial Services Committee.

Qualified Mortgage (QM) standard.[9] Mortgages would also need to be below the conforming loan limit;[10] the limit in high-cost areas would decrease by $20,000 per year if the director of FHFA determines that market conditions allow it.[11] The GSEs would be prohibited from purchasing a mortgage for a home located in an area that used eminent domain to acquire a mortgage in the previous 10 years.[12]

In addition, the GSEs would have to set their guarantee fees for the mortgages that they guarantee at the level that the FHFA director determines is comparable to what a privately capitalized financial institution would charge. The GSEs' affordable housing goals and contributions to the Housing Trust Fund would be repealed.[13] Fannie Mae and Freddie Mac would also be required to have at least 10% of their annual business involve risk-sharing transactions that transferred credit risk to private investors.

Each GSE's mortgage portfolio would be required to decrease by 15% annually down to $250 billion. As of the end of the second quarter of 2013, Freddie Mac had a mortgage portfolio of $521 billion[14] and Fannie Mae had a mortgage portfolio of $565.2 billion.[15] The PATH Act would codify provisions that are currently in support agreements between Fannie Mae and Freddie Mac and the Treasury.[16]

Five years after enactment. Five years after enactment, the GSEs' charters would be repealed, unless the FHFA director determined that market conditions warranted a temporary extension.[17] After their charters are repealed, Fannie and Freddie would no longer have authority to conduct new business. FHFA, acting as receiver, would have the discretion to establish a receivership entity to assume the assets and liabilities of the GSEs after their charters are repealed. The federal government would explicitly guarantee the payment of certain outstanding liabilities.

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[9] Qualified mortgages are mortgages that meet certain underwriting standards and product feature requirements under a regulation promulgated by the Consumer Financial Protection Bureau. See CRS Report R43081, *The Ability-to-Repay Rule: Possible Effects of the Qualified Mortgage Definition on Credit Availability and Other Selected Issues*, by Sean M. Hoskins.

[10] The conforming loan limit establishes the maximum size mortgage that the GSEs can purchase. See CRS Report RS22172, *The Conforming Loan Limit*, by N. Eric Weiss and Sean M. Hoskins.

[11] To make the annual decision, the FHFA Director would determine whether the spread between comparable conforming and non-conforming mortgages (a measure of private sector willingness to provide credit) exceeds 80 basis points. If the spread exceeds 80 basis points, no annual increase would be made.

[12] For information about proposals to acquire underwater mortgages through the use of eminent domain, see CRS Product WSLG187, *Legal Questions Abound Proposals to Use Eminent Domain to Acquire Underwater Mortgages*, by David H. Carpenter.

[13] Fannie Mae and Freddie Mac are required to meet certain affordable housing goals that are set by FHFA (for example, see FHFA, "2012-2014 Enterprise Housing Goals," 77 *Federal Register* 67535, November 13, 2012). The affordable housing goals target credit to low- and moderate-income households. For additional information on the Housing Trust Fund, see CRS Report R40781, *The Housing Trust Fund: Background and Issues*, by Katie Jones.

[14] Freddie Mac, *Freddie Mac Update,* at http://www.freddiemac.com/investors/pdffiles/investor-presentation.pdf.

[15] Fannie Mae, *Form 10-Q,* p. 34, at http://www.fanniemae.com/resources/file/ir/pdf/quarterly-annual-results/2013/q22013.pdf.

[16] For more information about the support agreements, see CRS Report R42760, *Fannie Mae's and Freddie Mac's Financial Status: Frequently Asked Questions*, by N. Eric Weiss.

[17] The FHFA director shall extend the conservatorship if the spread between comparable conforming and non-conforming mortgages (a measure of private sector demand to provide credit) exceeds 80 basis points.

Utility and Market Standards

The PATH Act would not create a new entity to guarantee MBS composed of conventional (non-government insured) mortgages. MBS composed of mortgages insured and guaranteed by the government, such as through FHA and VA, would still be eligible to be explicitly guaranteed by Ginnie Mae under the PATH Act.

Market Utility. The PATH Act would create a charter for a non-government, not-for-profit National Mortgage Market Utility (Utility) that would facilitate mortgage securitization. After a selection process, FHFA would assign the Utility charter to the chosen applicant. The Utility would not provide a government guarantee on MBS or originate mortgages. The Utility would establish market standards and guidelines for the other participants in the securitization process. It would operate the common securitization platform currently being developed by the FHFA and GSEs. The common securitization platform would be a voluntary securitization tool that could be used by private-sector actors to facilitate the back-office functions of securitization, such as providing disclosures to investors and tracking the assignment of mortgage notes.[18] The platform would potentially allow the mortgage market to benefit from economies of scale and from the efficiency generated by the standards that would be set through the platform. FHFA would regulate the Utility.

A MBS securitized through the platform and composed of mortgages that meet the underwriting and disclosure requirements of the Utility would be deemed a q*ualified security*. The Utility would establish multiple categories of Qualified Securities based on the underlying credit risk of the mortgages that compose the Qualified Security. The different categories of Qualified Securities would allow investors to determine which MBS is commensurate with the level of risk they wish to assume. Tailoring risk to the preferences of investors could facilitate demand for Qualified Securities and potentially lead to lower rates for borrowers in the primary market.

The Utility would be open-access, not charging fees that vary by the size of the participants. To facilitate the use of the platform by community banks and credit unions, the Federal Home Loan Banks[19] would be authorized to function as loan aggregators to pool loans from small institutions that could then be securitized through the platform.

Standards and Guidelines. The Utility would establish "rules of the road" for the securitization process. It would create standard securitization agreements to set the contractual terms between most of the major market participants (such as issuers, servicers, and investors). The Utility would also operate a National Mortgage Data Repository with publicly available mortgage data and mortgage-related documents.

Covered Bonds.[20] The PATH Act would direct financial regulators to implement regulations to create an oversight framework for covered bonds. Covered bonds are one method for financial

[18] Federal Housing Finance Agency, "Building a New Infrastructure for the Secondary Mortgage Market," October 4, 2012, http://www.fhfa.gov/webfiles/24572/fhfasecuritizationwhitepaper100412final.pdf.

[19] The Federal Home Loan Bank System is a government-sponsored enterprise that provides support to the mortgage market and to community development initiatives by lending to banks and other financial institutions that are members of the System. For more, see CRS Report RL32815, *Federal Home Loan Bank System: Policy Issues*, by Edward V. Murphy.

[20] This section was prepared using material from CRS Report R41322, *Covered Bonds: Background and Policy Issues*, by Edward V. Murphy.

institutions to raise funds from investors. They are rare in the United States, although variations of covered bonds have been used in Europe for centuries. A covered bond is a recourse debt obligation that is secured by a pool of assets, often mortgages. The holders of the bond are given additional protection in the event of bankruptcy or insolvency of the issuing lender. Covered bonds have some features, such as pooled mortgages, that resemble securitization, but the original lenders maintain a continuing interest in the performance of the loans. Although covered bonds are not a prohibited form of debt contract in the United States, some observers believe that legislation and agency rulemaking is required to facilitate the growth of a larger domestic covered bond market.[21]

FHA Reform

In recent years, increased default and foreclosure rates, as well as economic factors such as falling house prices, have contributed to increases in both the actual losses that FHA has incurred on insured loans and the anticipated losses that it expects to incur in the future. This increase in actual and expected losses has put pressure on FHA's insurance fund, and has led to concerns that FHA may need funds from Treasury to hold in reserve to pay for additional expected future losses.[22] According to the President's FY2014 budget, FHA may need to draw $943 million from Treasury in FY2013 for this purpose.[23] A final determination will be made by the end of FY2013.

Title II of the PATH Act includes many provisions intended to address FHA's financial condition by limiting the amount of risk it assumes, increasing the amount of capital that it is required to hold, and tightening certain mortgage standards. It also includes provisions to more narrowly target FHA's role in the mortgage market to certain types of homebuyers. In addition to making major changes to FHA's single-family insurance program, the PATH Act would also make some changes to other FHA insurance programs and, in some cases, mortgage programs for low-income households in rural areas that are administered by the U.S. Department of Agriculture (USDA).[24]

FHA Operations. FHA would become an independent agency outside of HUD, and FHFA would become the regulator for FHA and for the USDA's rural housing loan programs.

Eligible Borrowers. In general, FHA would only be allowed to insure mortgages for first-time homebuyers and low- and moderate-income borrowers. The required downpayment would be increased for all except first-time homebuyers to 5% from the current level of 3.5%. During

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[21] For information on previous actions by regulators to facilitate a covered bond market, see "Agency Actions on Covered Bonds" in CRS Report R41322, *Covered Bonds: Background and Policy Issues*, by Edward V. Murphy.

[22] FHA's single-family mortgage insurance program is supposed to bring in enough money through the fees, or premiums, that it charges for insurance to pay for the costs of any mortgage defaults. However, like all federal credit programs, FHA has permanent and indefinite budget authority to receive funds to pay for higher-than-expected future losses. The insurance fund for FHA's single-family programs is the Mutual Mortgage Insurance Fund (MMI Fund). Other types of mortgages, such as multifamily mortgages, are insured under other insurance funds. For more detailed information on the financial status of the MMI Fund, see CRS Report R42875, *The FHA Single-Family Mortgage Insurance Program: Financial Status and Related Current Issues*, by Katie Jones.

[23] *The Appendix, Budget of the United States Government, Fiscal Year 2014*, p. 574, at http://www.whitehouse.gov/sites/default/files/omb/budget/fy2014/assets/hud.pdf.

[24] In addition to insuring single-family mortgages, FHA also insures certain mortgages for multifamily buildings and healthcare facilities, as well as insuring reverse mortgages for senior citizens. The USDA's Rural Housing Services makes or guarantees certain types of mortgages under programs established under Title V of the Housing Act of 1949.

periods of market stress and in areas affected by disasters, FHA would be permitted to guarantee more types of mortgages, potentially allowing FHA to step in to insure more mortgages when mortgage credit is otherwise not easily available.

Maximum Mortgage Amounts and Insurance Coverage. Under the PATH Act, the dollar limit on the original principal balance of a mortgage that FHA can insure would be decreased in certain areas. Furthermore, the percentage of the mortgage that FHA could insure would decrease to 50% of the original principal balance, from 100%, over five years.

Premiums. The PATH Act would establish a minimum annual premium of 0.55%, and FHA would be required to set its premiums high enough to cover its administrative costs and salaries as well as the cost of insurance and the capital that FHA has to hold in reserve. FHA would be allowed to set premiums that vary based on the risk characteristics of the mortgage.

Capital Requirements. FHA's financial reports would have to be prepared using private-sector accounting standards. The capital ratio—the amount of additional capital that FHA must hold in reserve to pay for any additional, unanticipated future losses, beyond what it holds to pay for expected losses—would be increased to 4% of its outstanding insurance obligations. (Under current law, the required capital ratio is 2%.) FHA would be subject to certain restrictions if the capital ratio fell below certain thresholds.

Lender Oversight. Lenders could be required to reimburse FHA for defaulted mortgages that did not meet its standards in certain circumstances. Lenders would also need to agree to repurchase mortgages that default soon after the mortgage was originated. FHA would be required to publish a consolidated handbook, updated annually, with all of its requirements for lenders and servicers.

Other FHA Programs. The PATH Act would restrict occupancy of multifamily buildings with FHA-insured multifamily mortgages to low- or moderate-income households.[25] FHA would be required to set capital ratios for its other insurance funds.[26] FHA would be required to set certain limits and standards related to its Section 242 hospital insurance program, and FHA's reverse mortgage insurance program (the Home Equity Conversion Mortgage, or HECM) would be eliminated.

Other Provisions. After two years, 10% of new FHA single-family mortgage insurance, by dollar volume, would be required to be insured under risk-sharing agreements, whereby FHA would share the credit risk on the mortgage with other entities. FHA and USDA would be prohibited from backing mortgages in which seller concessions exceeded 3% and in areas that used eminent domain to obtain mortgages in the previous 10 years.

[25] For the purposes of FHA's mortgage insurance programs, multifamily properties are generally considered to be properties with five or more units, while single-family properties are properties with one to four units.

[26] FHA-insured single-family mortgages, including reverse mortgages, are insured under the MMI Fund, whereas other types of FHA-insured mortgages, such as multifamily mortgages, are insured under other insurance funds. Under current law, the MMI Fund is the only one of FHA's insurance funds required to maintain a minimum capital ratio.

Other Provisions

The PATH Act would, among other things, modify recent financial reforms that some believe are preventing private institutions from providing mortgage credit.[27] For example, implementation of certain Basel III[28] bank regulation rules would be delayed so that regulators could study their effects on smaller institutions. Mortgages securitized through the platform would be exempt from certain Dodd-Frank Act provisions, such the Ability-to-Repay rule.[29] In addition, the effective dates for some of the Dodd-Frank mortgage market rulemakings would be delayed by at least a year to allow institutions more time to comply, and Dodd-Frank's credit risk retention requirement[30] would be repealed.

S. 1217, the Housing Finance Reform and Taxpayer Protection Act of 2013

The Corker-Warner bill (S. 1217) proposes to wind down Fannie Mae and Freddie Mac and to replace FHFA with a new entity to be called the Federal Mortgage Insurance Corporation (FMIC). The FMIC would be an independent agency charged with supporting the mortgage market and providing reinsurance on eligible MBS. These MBS would have an explicit full-faith-and-credit federal government guarantee, and the FMIC would regulate aspects of the mortgage market related to these MBS.

Phase Out of Fannie Mae and Freddie Mac

Fannie Mae and Freddie Mac Wind Down. Upon enactment, FHFA would begin to wind down Fannie Mae and Freddie Mac over no more than five years. A holding company and trusts would be established for Fannie Mae's and Freddie Mac's outstanding debt obligations and mortgages. The federal government would guarantee the repayment of these obligations. Remaining funds would go first to the holder of their senior preferred stock (the Department of the Treasury), then to other preferred stockholders, and finally to common stockholders.

Conforming Loan Limit. Under the Corker-Warner bill, the nationwide conforming loan limit (the maximum amount of a mortgage that Fannie Mae and Freddie Mac can purchase), which is currently $417,000 except for certain high-cost areas where it cannot exceed $625,500, could increase based on increasing home prices. In high-cost areas the limit would decrease over five years by an amount determined through a formula set in the bill.

Affordable Housing. The existing mandatory housing goals would be repealed upon enactment. Fannie Mae's and Freddie Mac's contributions to the Housing Trust Fund and Capital Magnet

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[27] The PATH Act would modify existing regulation beyond what is described in this section. This section provides several illustrative examples of regulations what would be modified or repealed.

[28] For additional information about Basel III bank regulation, see CRS Report R42744, *U.S. Implementation of the Basel Capital Regulatory Framework*, by Darryl E. Getter.

[29] For more information on the ability-to-repay rule, see CRS Report R43081, *The Ability-to-Repay Rule: Possible Effects of the Qualified Mortgage Definition on Credit Availability and Other Selected Issues*, by Sean M. Hoskins.

[30] For additional information, see CRS Report R42056, *Ability to Repay, Risk-Retention Standards, and Mortgage Credit Access*, by Darryl E. Getter.

Fund would be repealed and replaced with contributions to those funds from the proceeds of a fee on covered MBS.

Mortgage Portfolios. Each GSE's mortgage portfolio would be allowed a maximum mortgage portfolio of $552.5 billion as of December 31, 2013, and this would decrease by 15% annually.[31] This reduction is currently required by the support agreements that Treasury entered into with Fannie Mae and Freddie Mac.[32] The legislation would take provisions that currently are in those contracts and make them law.

FHFA Wind Down. Regulation of Fannie Mae, Freddie Mac, and the Federal Home Loan Banks would be transferred to the FMIC from FHFA. FHFA staff and assets would be transferred to the FMIC. There would be a period of time of overlap.

Phase In of the FMIC

Guarantee. The FMIC would provide an explicit full-faith-and-credit guarantee as a backstop to private-sector capital on MBS that are issued by approved issuers and are composed of mortgages that meet its standards. To be eligible for a security guaranteed by the FMIC (part of a "*Covered Security*"), the mortgage loan amount would need to be below the conforming loan limits set by the bill and the mortgage would need to meet the underwriting criteria established by the Ability-to-Repay and Qualified Mortgage (QM) rule.[33] An eligible mortgage would also need to meet certain requirements related to downpayment, private mortgage insurance, maximum amount, and other conditions as determined by the FMIC. In unusual and exigent market conditions,[34] mortgages that do not meet the eligibility criteria may receive a guarantee for a limited time. Only FMIC-approved issuers could issue guaranteed MBS.[35]

Lenders would be allowed to make and to securitize mortgages that do not meet the FMIC eligibility criteria, but these nonconforming mortgages could not be included in an FMIC-guaranteed MBS. Likewise, mortgages that meet the FMIC criteria would not have to be guaranteed by FMIC.

MBS Capital. To be eligible for the FMIC guarantee, an MBS would require a private market holder to be in a first-loss position with sufficient capital to withstand losses associated with a significant economic downturn, which is defined as being able to cover at least a 10% decline in the face value of the security. The FMIC could approve different risk-sharing mechanisms, which could provide for approved issuers, approved bond guarantors, or investors, to share the losses.

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[31] As of the end of the second quarter of 2013, Freddie Mac had a mortgage portfolio of $521 billion and Fannie Mae had a mortgage portfolio of $565.2 billion.

[32] See CRS Report R42760, *Fannie Mae's and Freddie Mac's Financial Status: Frequently Asked Questions*, by N. Eric Weiss.

[33] For more information on the ability-to-repay rule, see CRS Report R43081, *The Ability-to-Repay Rule: Possible Effects of the Qualified Mortgage Definition on Credit Availability and Other Selected Issues*, by Sean M. Hoskins.

[34] A determination of exigent and unusual circumstance may be made by the FMIC upon the written agreement of the Chairman of the Board of Governors of the Federal Reserve System and the Secretary of the Treasury and in consultation with the Secretary of Housing and Urban Development.

[35] Issuing MBS involves pooling eligible mortgages, securitizing them, and selling the security to investors.

Losses. The FMIC would cover losses in excess of the private market holders' capital from the reserves held in a newly established Mortgage Insurance Fund (MIF). The MIF would be maintained and administered by the FMIC, and it would be financed primarily by MBS guarantee fees. The guarantee fees would be determined by the FMIC and set at levels necessary for the MIF to maintain its reserve balance. The MIF would be required to reach a reserve balance of 1.25% of the amount of securities insured within 5 years and 2.50% within 10 years.

Market Standards. The FMIC would support the mortgage market by establishing standards and "rules of the road" for the part of the market that it would oversee. For example, the FMIC would develop standard securitization agreements to establish the contractual terms between most of the major market participants (such as issuers, servicers, and investors). The FMIC would continue FHFA's current efforts to develop a common securitization platform and a new common technology platform for back-office functions.[36] The FMIC may impose monetary penalties and revoke or suspend the approved status of participants that violate its standards or other requirements.

Affordable Housing. The legislation would replace Fannie's and Freddie's affordable housing goals with a fee on the covered MBS.[37] The HUD's Housing Trust Fund would receive 80% of the funds, and the other 20% would go to the Treasury's Capital Magnet Fund.[38]

Organization. The FMIC would be an independent government agency headed by a director, appointed by the President with the advice and consent the Senate, who shall serve a five-year term. There would be a Board of Directors with five members and the director serving as chairperson. The four additional board members would also be appointed by the President with the advice and consent of the Senate to serve five-year terms. The FMIC would be structured with several offices, including an Office of Underwriting, an Office of Securitization, an Office of Federal Home Loan Bank Supervision, and an Office of the Inspector General.

Other Provisions

The legislation would, among other things, transfer Fannie Mae's and Freddie Mac's multifamily mortgage operations to the FMIC, require the Government Accountability Office (GAO) to submit a report on the feasibility of a fully private secondary market within eight years of enactment, and provide equal access for small lenders to the secondary market through a new entity, the FMIC Mutual Securitization Company, and by other actions.

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[36] Federal Housing Finance Agency, "Building a New Infrastructure for the Secondary Mortgage Market," October 4, 2012, http://www.fhfa.gov/webfiles/24572/fhfasecuritizationwhitepaper100412final.pdf.

[37] Section 506. For more information about the affordable housing goals, see CRS Report R42760, *Fannie Mae's and Freddie Mac's Financial Status: Frequently Asked Questions*, by N. Eric Weiss.

[38] For information on the Housing Trust Fund, see CRS Report R40781, *The Housing Trust Fund: Background and Issues*, by Katie Jones. The Capital Magnet Fund "provide[s] competitively awarded grants to [Community Development Financial Institutions] and qualified nonprofit housing organizations. CMF awards can be used to finance affordable housing activities as well as related economic development activities and community service facilities." See Community Development Financial Institutions Fund, at http://www.cdfifund.gov/what_we_do/programs_id.asp?programID=11.

S. 1376, the FHA Solvency Act of 2013

The Johnson-Crapo bill (S. 1376) was reported out of the Senate Banking Committee on July 31, 2013. It proposes to make a number of changes to FHA aimed at strengthening its financial position. Most of these changes are aimed at ensuring that FHA's programs are financially sound, but do not focus on limiting FHA's market role or shifting risk to the private sector to the degree that the PATH Act does. For example, S. 1376 would not restrict FHA insurance to only first-time or low- and moderate-income homebuyers. It also would not make FHA an independent agency or reduce the percentage of the mortgage that FHA can insure.

Eligible Borrowers. FHA would be required to evaluate and revise its underwriting standards for mortgages using certain criteria, similar to the criteria for qualified mortgages.

Maximum Mortgage Amounts. GAO would be required to submit a study on the appropriate dollar limit on the maximum mortgage amount that FHA can insure.

Premiums. FHA would require a minimum annual premium of 0.55% and increase the maximum premiums that FHA can charge. FHA would be required to re-evaluate its premiums annually to ensure that they are adequate to maintain the capital ratio.

Capital Requirements. The capital ratio would be raised to 3% within 10 years. (Under current law, the required capital ratio is 2%.) If the capital ratio failed to meet certain thresholds, FHA would be required to take certain steps, including implementing premium surcharges for new borrowers and reporting to Congress on steps it was taking to restore the capital ratio. FHA would be required to undergo stress-testing based on the stress test model developed by the Federal Reserve for banks and report the results in its annual actuarial review. Congress would have to be notified within 48 hours if FHA used its authority for funding from Treasury for the single-family insurance fund.

Lender Oversight. Lenders could be required to reimburse FHA for defaulted mortgages that did not meet its standards in certain circumstances. FHA would be authorized to terminate lenders' approval on a nationwide basis, as well as in specific areas. FHA would be required to publish a consolidated guide with all of its requirements for lenders and servicers.

Other FHA Programs. The bill would require certain changes to FHA's reverse mortgage program, the Home Equity Conversion Mortgage (HECM) program, and would authorize FHA to make certain changes to the HECM program through administrative guidance documents for a period of time under certain conditions.

Other Provisions. FHA would be allowed to transfer mortgage servicing rights to specialty servicers under certain circumstances. FHA would be required to finalize its rules on seller concessions.[39]

[39] In July 2010, FHA issued a proposed rule to limit seller concessions to 3% of the lesser of the home's sale price or appraised value. In February 2012, it issued a revised proposed rule and asked for comments on the revisions. See Department of Housing and Urban Development, "Federal Housing Administration (FHA) Risk Management Initiatives: Revised Seller Concessions," 77 *Federal Register* 10695-10707, February 23, 2012.

Comparison of Major Provisions

Table 1 compares non-FHA related provisions in the PATH Act and the Corker-Warner bill. **Table 2** compares the FHA reforms in the PATH Act and the Johnson-Crapo FHA bill.

Table 1. Comparison of Non-FHA Provisions in H.R. 2767 and S. 1217

Topic	PATH Act (H.R. 2767)	Corker-Warner (S. 1217)
Fannie and Freddie Wind Down	The PATH Act would limit the GSEs' new mortgage purchases to those that meet the QM standard and would require the GSEs to share credit risk with the private sector. It would require the GSEs to continue to reduce their mortgage portfolio.	The Corker-Warner bill would require the GSEs to continue to reduce their mortgage portfolio immediately.
	Within five to seven years of enactment, FHFA would place the GSEs into receivership and repeal their charters. Certain outstanding GSE obligations would be guaranteed by the government.	Within five years, the bill would repeal the GSEs' charters. Certain outstanding GSE obligations would be guaranteed by the government.
Newly Established Entity	The PATH Act would establish the National Mortgage Market Utility, a non-government, non-profit entity that is privately managed. The Utility would operate the common securitization platform and would set standards and guidelines for the securitization process.	The Corker-Warner bill would establish the Federal Mortgage Insurance Corporation (FMIC) as an independent government agency. The FMIC would provide insurance for certain MBS, would oversee the common securitization platform, and would set standards and guidelines for the securitization process.
Government Guarantee	The PATH Act would not create a new government guarantee on mortgages or MBS. It would keep in a narrowed form the existing government guarantee programs, i.e., FHA, VA, USDA Rural Housing, and Ginnie Mae.	The FMIC would provide a government guarantee on MBS that meet its requirements. The FMIC would only pay out on its guarantee after private capital (at least 10% of the value of the security) absorbed the first losses.
FHFA	The PATH Act would have FHFA operate as the regulator of the Utility.	The Corker-Warner bill would eliminate FHFA after the GSEs have been wound down. Much of FHFA's remaining responsibilities and personnel would be transferred to FMIC.
Securities Eligible for the Securitization Platform	Under the PATH Act, MBS that meet the Utility's guidelines would be Qualified Securities. Qualified Securities would not have a government guarantee.	Under the Corker-Warner bill, MBS that meet FMIC's criteria are eligible for the FMIC guarantee and would be Covered Securities. Covered Securities and non-covered securities could be issued through the common securitization platform.
Market Standards	The PATH Act would require the Utility to develop standard securitization agreements that would establish the contractual terms between most of the major market participants.	The Corker-Warner bill creates an Office of Securitization in the FMIC. The Office would develop standard securitization agreements that would establish the contractual terms between most of the major market participants.
Affordable Housing	The PATH Act would repeal the GSEs' affordable housing goals and the Housing Trust Fund.	The Corker-Warner bill would replace Fannie's and Freddie's affordable housing goals with an additional fee on covered securities that would be allocated to the Housing Trust Fund and to the Capital Magnet Fund.

Topic	PATH Act (H.R. 2767)	Corker-Warner (S. 1217)
Mortgage-Related Financial Reform Regulations	The PATH Act would modify or repeal certain recent mortgage-related financial reforms.	Not addressed.

Source: Created by the Congressional Research Service (CRS) using information obtained from the Legislative Information System (LIS) available at http://www.congress.gov.

Table 2. Comparison of FHA Provisions in H.R. 2767 and S. 1376

Topic	PATH Act (H.R. 2767)	FHA Solvency Act (S. 1376)
FHA Structure	FHA would become an independent agency. FHFA would regulate FHA and the USDA rural housing programs. FHA's financial reports would have to use accounting methods used in the private sector.	No similar provisions; FHA would remain part of HUD.
Eligibility and Underwriting Standards	FHA insurance would be limited to first-time or low- and moderate-income homebuyers, and the downpayment would be increased to 5% for all but first-time homebuyers. FHA would be permitted to guarantee more types of mortgages during periods of market stress and in areas affected by disasters.	FHA would be required to evaluate and revise its underwriting standards for mortgages using certain criteria.
Maximum Mortgage Amount	The maximum dollar amount of a mortgage that FHA can insure would be decreased in some areas.	GAO would be required to submit a study on the appropriate dollar level for the maximum mortgage amounts.
Insurance Coverage	The share of a mortgage that FHA can insure would be reduced to 50% over five years.	No similar provision; the share of a mortgage that FHA can insure would remain at 100%.
Premiums	The PATH Act would set a minimum annual premium of 0.55% and allow FHA to set premiums that vary based on the credit risk of the mortgage. FHA would have to ensure that its premiums are high enough to cover administrative and personnel costs as well as the costs of insurance and maintaining the capital ratio.	The FHA Solvency Act would set a minimum annual premium of 0.55% and increase the maximum annual premiums that FHA can charge. FHA would have to re-evaluate its premiums annually to ensure that they are adequate to cover the costs of insurance and maintain the capital ratio.
Capital Requirements	The capital ratio would be increased to 4% of outstanding insurance-in-force. If the ratio fell below certain thresholds, FHA would be subject to certain restrictions on the mortgages it could insure. FHA would also be required to set capital ratios for its other insurance funds.	The capital ratio would be increased to 3% of outstanding insurance-in-force within ten years. If the ratio fell below certain thresholds, FHA would have to take certain actions, such as premium surcharges for new borrowers. FHA would be subject to stress tests based on the Federal Reserve's stress test model. Congress would have to be notified within 48 hours if FHA used its authority to draw funds from Treasury.

Topic	PATH Act (H.R. 2767)	FHA Solvency Act (S. 1376)
Lender Oversight	Under certain circumstances, lenders could be required to reimburse FHA for defaulted mortgages that did not meet its standards.	Under certain circumstances, lenders could be required to reimburse FHA for defaulted mortgages that did not meet its standards.
	Lenders would have to agree to repurchase certain mortgages that experience early defaults.	FHA could terminate lenders' approval on a nationwide basis, as well as in specific areas.
	FHA would be required to annually publish a manual, handbook, or guide that consolidates all of its origination and underwriting requirements for lenders and servicers.	FHA would be required to publish a single resource guide that consolidates all of its policies, processes, and procedures for lenders and servicers.
Other FHA Programs	Repeals the HECM program that provides FHA insurance on reverse mortgages.	Requires certain changes to the HECM program, and allows FHA to implement some changes administratively for a period of time.
	Occupancy of buildings with FHA-insured multifamily mortgages would be restricted to low- or moderate income households.	
	FHA would be required to set certain limits and standards related to its mortgage insurance program for hospitals.	
Other	Seller concessions would be limited to 3% for FHA and USDA mortgages.	FHA would be required to finalize its rules on seller concessions (proposed rules limit seller concessions to 3%).
	After two years, 10% of FHA's new business would have to be insured pursuant to risk-sharing agreements with other entities.	FHA would be allowed to transfer mortgage servicing rights to specialty servicers under certain circumstances.
	FHA and USDA would be prohibited from backing mortgages in areas that used eminent domain to obtain mortgages in the past 10 years.	

Source: Created by CRS using information obtained from the Legislative Information System (LIS) available at http://www.congress.gov.

Author Contact Information

Sean M. Hoskins
Analyst in Financial Economics
shoskins@crs.loc.gov, 7-8958

Katie Jones
Analyst in Housing Policy
kmjones@crs.loc.gov, 7-4162

N. Eric Weiss
Specialist in Financial Economics
eweiss@crs.loc.gov, 7-6209

Key Policy Staff

Area of Expertise	Name	Phone	E-mail
Dodd-Frank mortgage-market rulemakings, Fannie Mae, Freddie Mac, FHFA, and the secondary mortgage market	N. Eric Weiss	7-6209	eweiss@crs.loc.gov
Dodd-Frank mortgage-market rulemakings, Fannie Mae, Freddie Mac, and the secondary mortgage market	Sean Hoskins	7-8958	shoskins@crs.loc.gov
FHA, Ginnie Mae, and mortgage-market government-guarantee programs	Katie Jones	7-4162	kmjones@crs.loc.gov