American Bankers Association
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To: Members of the Committee on Financial Services

From: James Ballentine, Executive Vice President, Congressional Relations and Political Affairs

Re: Markup of Protecting American Taxpayers and Homeowners Act of 2013 (PATH Act)

On Tuesday, July 23, 2013, the House Financial Services Committee is scheduled to consider the Protecting American Taxpayers and Homeowners Act of 2013 (PATH Act). I am writing on behalf of the members of the American Bankers Association to offer our views on this important housing reform legislation. We appreciate the leadership of Committee Chairman Jeb Hensarling and the efforts of the House Financial Services Committee to address the critical need for reform of the nation's housing finance system. It is essential that broad, bi-partisan housing-finance reform and regulatory relief for community-based banks be enacted this Congress, and we offer these views in the hopes that they assist in the further development and movement of this legislation.

We will divide our comments into five main areas: GSE Reform, FHA Reform, New Market Structure, Regulatory Relief, and Other Areas of Interest.

GSE REFORM

Section 103 of the PATH Act would wind down Fannie Mae and Freddie Mac within five years, and would not provide for any federal guarantee on any loan in their absence. Instead, this legislation would authorize the creation of a "public utility" which would oversee the creation and maintenance of a single platform for the sale of mortgages by originators to investors who would then securitize the mortgages. The public utility would be charged with ensuring equitable access to the secondary market for participants regardless of size or geographic location.

ABA agrees that the federal role in mortgage finance needs to be significantly reduced, but we believe that a fully priced and fully paid-for guarantee by the federal government for a class of well-underwritten loans within clearly defined and targeted loan limit boundaries is needed at this time to maintain a stable housing market. While we envision a transition to a marketplace with a large and perhaps predominant component that is not dependent on federal guarantees, a targeted federal role is essential to progress from the present reality toward that goal. It is important that all options be considered as the Committee debates this important issue. We would like to work with the Committee to determine the proper role of Fannie, Freddie, their successors, and the proposed public utility in housing reform.

There are many reforms incorporated into the bill's GSE Reform sections that deserve serious consideration. Specifically, ABA supports:

- Reducing the maximum mortgage amount eligible for sale to Fannie Mae and Freddie Mac included in Section 104 of the bill.

- Efforts to review and revise guarantee fees to ensure that the federal government is being adequately compensated for the risk it is taking when providing a guarantee included in Section 104 of the bill.

- Development of risk-sharing transactions, including first loss agreements with private-sector participants, included in Section 105 of the bill.

- Limiting GSE purchases to Qualified Mortgages included in Section 106 of the bill, but we note that further revisions to the Qualified Mortgage definition which are included in other sections of the bill, and which we also support, are necessary.

- Prohibiting the GSEs (or any successor) from purchasing or guaranteeing mortgages that are within a jurisdiction that has exercised eminent domain to seize a mortgage loan during the last 120 months as included in Section 107 of the bill.

FHA REFORM

The PATH Act would significantly alter the structure of the Federal Housing Administration (FHA), making it an independent entity outside of the Department of Housing and Urban Development. While ABA has not advocated for such a sweeping change, we do believe the idea has merit and should be explored further. Therefore, ABA does not take a specific position with regard to Sections 211 through 231, which would transform FHA into an independent agency, but we believe this approach is worthy of further discussion and consideration.

The bill would also re-target FHA to serve first-time homebuyers and low- and moderate-income borrowers – goals that ABA strongly supports. We also believe that the allowance for FHA to be employed in markets experiencing counter-cyclical mortgage conditions and Presidentially declared disaster areas is prudent. We support the intent of the draft legislation to revise the premium structure for FHA insurance and to create new risk-sharing pilot programs, and so therefore support Sections 232 and 233 of the bill, which detail these efforts.

We have concerns with Section 234 of the bill, which would reduce the mortgage insurance coverage provided by FHA to only 50 percent of the mortgage being insured. ABA continues to advocate for full coverage of the outstanding balances of loans insured under FHA. It is our view that with appropriate down payment amounts, more prudent underwriting standards, and reasonable premiums for the insurance being provided, there is no reason not to continue full insurance coverage of FHA loans. Further, given the re-targeted role envisioned by the bill for FHA to be targeted primarily to first-time and low- and moderate-income borrowers, it is appropriate for the program to provide full insurance coverage as a public policy matter to encourage lending to qualified borrowers in this market segment.

We support Section 235, setting a new premium structure for the FHA and establishing the authority to charge risk based premiums.

We also have concerns about Section 236, which would require a default and foreclosure statement to be provided by a lender to each FHA borrower at origination. This is an additional regulatory and paperwork burden that will only increase costs for lenders and borrowers. It provides little benefit to borrowers and may in fact be misleading.

We oppose Section 264, which would require lenders to repurchase any FHA loan that defaults (60 days past due) in the first 24 months of the mortgage. If a lender appropriately underwrites a loan and follows all other FHA requirements, the lender should not bear the full burden of a defaulted loan.

We support Section 266, which prohibits the FHA from insuring loans that are within a jurisdiction that has exercised the power of eminent domain to seize a mortgage loan during the preceding 120 months.

NEW MARKET STRUCTURE

ABA supports the general intentions of Sections 301 through 316, which would establish a new “public utility.” In particular, ABA supports the creation of a utility or other entity as envisioned by the PATH Act to operate a new securitization platform (such as the one currently being developed by the Federal Housing Finance Agency). This utility would be tasked with operating the securitization platform in an open access manner and would ensure that eligible loan originators, aggregators, and issuers would have equitable access to the platform, regardless of size, geographic location, or market served. Open access is especially important for community banks and we encourage the Committee to make a special effort to ensure that access. We believe that such a utility or similar entity should be the vehicle to manage and regulate any federal guarantees that may be authorized.

ABA supports the creation of a covered bond market as one of several sources of liquidity for the mortgage market, as detailed in Sections 351 through 356 of the bill. Covered bonds might establish funding options that have certain characteristics similar to advances provided by the Federal Home Loan Banks, but they lack the cooperative Federal Home Loan Bank system’s unique characteristics that contribute to market liquidity and diversity. We encourage the Committee to make clear that in developing a covered bond market there should be no restrictions placed on use of either covered bonds or participation in Federal Home Loan Bank membership. Some have proposed limiting covered bonds to one segment of the market based upon asset size, while restricting Federal Home Loan Bank membership as well. We would strongly oppose any such restrictions and would oppose any legislation which included such restrictions.

REGULATORY RELIEF

Title IV of the PATH Act draft includes many provisions which ABA has long advocated and strongly supports. These provisions would help to rebalance the regulatory environment, particularly for community banks, from regulatory overreach that occurred in response to the financial crisis and would help to ensure a more vibrant, safe, and effective mortgage market. Specifically we support:

- Section 401 – the mandatory delay of Basel III implementation and study of Basel III impact.

- Section 402 – Basel III liquidity coverage ratio amendments.

- Section 403 – changes to the definition of points and fees under the Qualified Mortgage rule.

- Section 404 – the exclusion of asset-backed securities from the proposed definition of "covered funds" in which banks are restricted from investing.

- Section 405 – the suspension of the Security and Exchange Commission's Reg. AB rulemaking regarding asset-backed securities.

- Section 406 – the extension of the implementation date of Dodd-Frank Act mortgage regulations for one year.

- Section 407 – the repeal of the Qualified Residential Mortgage and the Premium Capture Cash Reserve Account rulemaking.

- Section 410 – the repeal of Sections 1413, 1431, and 1432 of the Dodd-Frank Act.

- Section 412 – establishing clear examination standards.

- Section 415 – exempting entities servicing 20,000 loans or fewer from Dodd-Frank Act servicing requirements.

The sections referenced above all provide significant needed relief, without which investments in the mortgage market and credit availability will be seriously constrained. With regard to Basel III, we continue to be concerned about the punitive restrictions that agencies have placed on bank mortgage servicing assets under the final Basel III capital rules. Such capital treatment of mortgage servicing will drive a wedge between mortgage borrowers and lenders, potentially pushing such activities into the non-bank sector. ABA pledges to work with the Committee on this and other capital issues arising from Basel III implementation that are expected to have adverse impacts on credit availability, and would be pleased to work with you on expanding these provisions in the bill.

Section 403 includes changes to the points and fees definitions for the Qualified Mortgage rule that also were included in H.R 1077, introduced by Representative Bill Huizinga. We strongly support these changes, which are of particular import to community banks who serve as mortgage brokers when serving their customers. Without the changes in this section, these banks will find it harder to make a Qualified Mortgage and to provide mortgage servicers to their local communities.

The extension of the implementation date of the Dodd-Frank Act mortgage regulations included in Section 406 is essential. These rules will dramatically refocus the entire lending process. Every participant in that process, from lenders to borrowers, service providers, appraisers, escrow agents, title agents, and all others will be impacted by the changes, and must come into compliance in the next six months. Between now and then banks must fully review all of the final rules, implement new systems, processes, and forms, train staff, and test changes for quality assurance, as well as work with all other providers to ensure that they too are compliant. That effort is made even more complicated when factoring in the fact that to manage year-end regulatory and tax reporting requirements, many institutions have an information-technology “freeze” between November and early January. Because it is not possible to test or revise the new mortgage compliance systems during the lock-down period, the compliance deadline is effectively November of 2013.

Regulatory implementation is further complicated by the fact that many banks commonly rely on vendors for software and system upgrades. Many banks report that their vendors are not yet ready to provide the necessary updates to the individual institutions, and some vendors may not do so until late summer or early fall. Given these time constraints, and the fact that the Consumer Financial Protection Bureau (CFPB) continues to issue modifications to the rules, it will be virtually impossible for most lenders to achieve full compliance by January 2014. That lack of confidence in the ability to comply likely will lead to a reduction of credit as lenders pull back from lending until such time as they have confidence in their ability to comply. It is a far better approach to delay implementation to ensure that the entire industry can comply than to meet an arbitrary deadline that will further disrupt the mortgage markets and harm credit availability.

In addition to the regulatory corrections made in the sections delineated above, we also strongly support Section 409, which exempts from the Dodd-Frank Act’s ability-to-repay requirements those residential mortgage loans originated by a creditor and held in portfolio. Those provisions of Dodd-Frank were intended to reform the securitization process to prevent lenders from originating loans without consequence and then passing the loans through the securitization chain. Portfolio lenders, willing to make a loan to a borrower who they view as a reasonable credit risk and willing to hold those loans on their own books, should not be required to meet the Dodd-Frank requirements. A portfolio lender’s own self-interest in maintaining a safe and sound portfolio, along with safety and soundness regulation and supervision, provide adequate regulation in this area. Further, the imposition of the Dodd-Frank requirements on portfolio lenders will make it impossible to serve some otherwise creditworthy customers and will significantly harm certain borrowers and populations which would otherwise be well served by portfolio lenders.

As referenced above, we support Section 410 of the bill, which would repeal three sections of the Dodd-Frank Act, including the defense to foreclosure provision. The defense to foreclosure provision has created a concern that prudential regulators will severely restrict the ability of banks to keep non-QM safe harbor loans in their portfolios. This would make QM the effective requirement for safety and soundness and risk mitigation purposes. Section 410 would help to ensure that lenders are able to offer mortgages to borrowers who do not meet all of the QM standards but who nevertheless have the ability to repay a mortgage loan.

ABA also strongly supports Section 412, which incorporates provisions of H.R. 1553, the Financial Institutions Examinations Fairness and Reform Act, bipartisan legislation introduced by Representatives Shelley Moore Capito and Carolyn Maloney. Our members are concerned that bank regulators are making decisions during the examination process that have effectively and unnecessarily reduced the amount of capital available for lending – particularly to small businesses. These decisions hinder banks’ ability to help local businesses grow and create jobs. The changes included in H.R. 1553 and incorporated into Section 412 of the PATH Act draft address this critical issue by establishing clear examination standards and creating an independent Examination Ombudsman to ensure the consistency of all examinations. These provisions also would ensure that financial institutions receive timely examination reports that include full documentation of the information the regulators used to make their determinations, and would create an expedited process for banks to appeal examination decisions without fear of reprisals.

OTHER AREAS OF INTEREST

There are provisions of the PATH Act which are of concern and which ABA cannot support in their current form. Specifically, we have concerns over Section 414, which would prohibit a mortgage servicer of a residential mortgage from holding an interest in any other security interest on the same dwelling. This provision would prohibit a lender who holds or services a mortgage loan from offering their customer a home equity loan or line of credit.

We also have concerns with Section 502, which incorporates provisions of H.R. 927, the Common Sense Economic Recovery Act. These provisions would permit certain current loans that would otherwise be treated as non-accrual loans as accrual loans. We are concerned about legislating changes in accounting standards, even if they are only intended to be for regulatory use. Banks are issuers of financial statements – upon which investors rely – as well as heavy users of financial statements of our borrowers. We need to make sure that all parties can rely on the accuracy of financial statements. We appreciate the motivation behind this provision and support requiring the Financial Stability Oversight Council (FSOC) to conduct a study of how best to prevent contradictory guidance from federal banking agencies, but the other aspects of this provision should be reconsidered. We also believe that Section 412 (which we support) provides a more effective and less disruptive means to address the objective of preventing classifications of performing loans.

CONCLUSION

The PATH Act is important and comprehensive legislation which begins the necessary process of reforming our nation's housing finance system. ABA supports many of the provisions of this legislation. We have concerns with other provisions and seek to work with Members in a bi-partisan manner to address those concerns and help to move this legislation forward in the legislative process.