JOHNSON/CRAPO GSE REFORM PROPOSAL: ABA SHORT SUMMARY

Senate Banking Committee Chairman Tim Johnson (D-SD) and Ranking Member Mike Crapo (R-ID) have drafted legislation to eliminate Fannie Mae and Freddie Mac and replace them with a new system providing for a targeted market of mortgage loans which could be guaranteed by the federal government.

Under the new system the Federal Mortgage Insurance Corporation would replace Fannie and Freddie as the guarantor and regulator of a new system. The FMIC, patterned after the Federal Deposit Insurance Corporation, would be explicitly backed by the full faith and credit of the United States, and would only guarantee mortgage securities in which the private market holds at least a ten percent first loss position.

The FMIC would also regulate the private market providers that would be chartered to provide necessary services under the new system. Participants in the new system would include:

- Originators: lenders who underwrite mortgages for homebuyers and sell eligible loans into the secondary market.
- Aggregators: entities who pool mortgages (which they may have originated or purchased); obtain a guarantee from a private guarantor or a credit enhancement through a capital markets execution (typically through mortgage insurance), and deliver the pool to a Securitization Platform to be issued with a FMIC - backed government guarantee.
- Guarantor: Guarantors hold 10% capital and provide a guarantee on mortgage-backed securities. This guarantee stands in front of the government guarantee which would only apply if the guarantor fails.
- Capital Markets Execution: Investors hold fully funded first loss positions of at least 10% of the mortgage backed securities value, putting private capital in front of the government guarantee. The FMIC must approve capital markets mechanisms to be used in providing a credit enhancement.

Mutual Entity: Smaller lenders (defined as those with up to $500 billion in assets) would be able to join a mutual entity which could purchase and aggregate loans and sell them (for cash) through the Securitization Platform. Federal Home Loan Banks would also be eligible to join the Mutual.

The Securitization Platform would be cooperatively owned by those entities eligible to sell loans into the FMIC System and would provide standard forms and contracts for securitization. The Platform could also be used to provide securitization forms and contracts for non-FMIC guaranteed transactions as well.

Multifamily housing finance will also be governed and guaranteed by the FMIC. Guarantors will be approved by FMIC and will guarantee a first loss position as well as issue securities on which they provide guarantees. Approved multifamily guarantors will have a 10% capital requirement. Existing Fannie Mae and Freddie Mac multifamily programs will be continued and allowed to be used by future guarantors.

Affordable Housing: The draft specifically repeals Affordable Housing Goals and replaces them with a market based incentive system whereby an average 10 basis points is charged on each loan guaranteed through the new system to support affordable housing. The fee can be adjusted up or down based upon an institution's demonstration of its record of meeting community needs.

Underwriting Standards: FMIC will set underwriting standards for loans eligible for the guarantee. Standards must mirror the QM (Qualified Mortgage) standard established by the CFPB and must include a 5% minimum down payment requirement (or a 3.5% requirement for first time homebuyers).

Governance: The FMIC will be governed by an independent, bi-partisan 5 member board appointed by the President and approved by the Senate.

Regulatory Authority: The FMIC is given authority to approve, supervise and examine the entities involved in the provision of the FMIC guarantee. These authorities include:

- Approval and supervision of guarantors who back FMIC securities;
- Approval and supervision of aggregators who deliver mortgages to the Securitization Platform for FMIC insured securities;
- Approval and supervision of private mortgage insurers who provide credit enhancements for FMIC guaranteed securitizations;
- Approval and examination for servicers of eligible mortgage loans (and FMIC must ensure that small servicers are not disadvantaged).

ABA Position: ABA views the Johnson/Crapo bill as an important step forward in addressing the unsustainable conservatorship of Fannie Mae and Freddie Mac. We note that the draft includes many key provisions urged by ABA including equitable access to the secondary market for lenders of all sizes. ABA staff and leadership continue to engage with Senate and Administration representatives to discuss further refinements and concerns. Concerns include the creation of a new regulatory entity (FMIC) and ensuring that it does not unnecessarily add to the regulatory burden of insured depositories; and the impact of the market based approach to affordable housing and that protections are provided to ensure that affordable housing efforts remain facially neutral and not subject to political coercion. ABA is also working to examine the capitalization and first loss positions required under the draft, as well as the various fee structures proposed. For the new system to work, capital requirements and fee structures must be economically feasible and appropriately prudential for all participants in the secondary market system.

For further information: See the links below for further information.

For the text of the draft legislation:
http://www.banking.senate.gov/public/index.cfm?FuseAction=Files.View&FileStore_id=512757b1-e595-4b85-8321-30d91e368849

For a Section by Section of the legislation prepared by Senate Banking staff:
http://www.banking.senate.gov/public/index.cfm?FuseAction=Files.View&FileStore_id=b8ab780d-0486-41be-9579-eac40dd09ce8

For a detailed summary of the legislation:
http://www.banking.senate.gov/public/_files/SummaryoftheBipartisanHousingFinanceReformDraft_update.pdf

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