



# **Housing Finance Reform Plan**

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# Executive Summary

## 1. Refocus FHA to its Core Mission

The financial crisis resulted in private capital receding from the housing finance system. As a result of the crisis and subsequent policy decisions of the previous Administration, the market share of the Federal Housing Administration's (FHA) increased dramatically from pre-crisis levels. As the United States Department of Housing and Urban Development (HUD) pursues reforms, FHA should refocus on its mission of providing housing finance support to low- and moderate-income families that cannot be fulfilled through traditional underwriting, including targeting first-time and lower-wealth creditworthy homebuyers who benefit from FHA's ability to provide affordable mortgage credit at fixed rates with lower down payments.

Since the financial crisis, the risk profile of FHA's portfolio has increased steadily, endangering FHA's ability to support access to affordable mortgage credit for first-time homebuyers (FTHBs). Credit scores of borrowers have fallen, while loan-to-value (LTV) and debt-to-income (DTI) ratios have increased. The use of downpayment assistance (DPA) programs also has grown significantly. Further, FHA's activities have strayed away from its core mission—through July of FY2019, 70 percent of FHA refinance endorsements are cash-out refinancing and FHA remains the largest insurer of reverse mortgage products through its Home Equity Conversion Mortgage (HECM) program. These activities create risks to the solvency of FHA and interfere with its core mission of helping low- and moderate-income borrowers with good credit – yet limited assets – afford a home and build wealth.

Through a formalized collaborative approach, FHA and the Federal Housing Finance Agency (FHFA) must work together to ensure that government-supported mortgage programs are not competing and do not crowd private capital out of the marketplace, both in their Single Family and Multifamily programs. Further, FHA must ensure that borrowers are creditworthy and that they have access to loans that meet their financial needs without creating undue risk. A mortgage product that is inappropriate for a borrower may lead to default and foreclosure, destroy credit, and exacerbate affordable housing need.

FHA must continue to have a strong enforcement regime that appropriately punishes bad actors and those who willingly defraud taxpayers. However, its enforcement regime should not deter reputable and well-regulated lenders from participating in FHA's programs. Accordingly, it must provide clarity and transparency in its regulatory expectations for participating lenders, including addressing lender and loan-level certification standards and the defect taxonomy. In collaboration with the Department of Justice (DOJ), FHA should continue to work to provide more clarity on how the agencies will consult on the appropriate use of the False Claims Act (FCA), which has driven away many lenders, including many depository institutions, from the FHA program. FHA must ensure it continues to appropriately use all enforcement remedies and mechanisms available. Doing so will provide lenders with transparency and a higher level of certainty and promote the participation of a more diverse lender base in FHA's programs.

## **2. Protect American Taxpayers**

With mortgage insurance on loans of over \$1.4 trillion in unpaid principal balance (UPB) and more than \$2.1 trillion in mortgage-backed securities (MBS) guaranteed by the full faith and credit of the United States, FHA and the Government National Mortgage Association (GNMA), respectively, must ensure their business and operational practices protect American taxpayers. Meeting this duty also is essential to FHA's and GNMA's respective missions and if either does not operate in a fiscally responsible manner, HUD's ability to provide affordable and sustainable mortgage credit for borrowers is severely jeopardized. FHA must maintain an appropriate level of capital reserves in the Mutual Mortgage Insurance Fund (MMIF). It is unacceptable for FHA to require a draw on taxpayer funds to sustain its book of business and so FHA should seek to build its capital ratio well above the statutory two percent minimum to ensure that it is able to weather stress events without requiring a taxpayer bailout.

FHA's risk management capabilities must be improved in order to prudently serve its core mission and to protect taxpayers. In particular, FHA must transform its data analytics and risk management capabilities. FHA also must continue to develop policies that ensure its reverse mortgage product – HECM, which has cost the MMIF billions of dollars in claims in recent years – is fiscally sustainable. To ensure that HUD and taxpayers are properly compensated for riskier loans, FHA should implement a “tiered pricing” framework to protect the MMIF.

FHA and GNMA must ensure that they can properly manage their counterparty risk exposure and strengthen surveillance practices. To achieve this strategic aim, FHA and GNMA should continue to work with FHFA and other federal entities to institute a framework that allows for ongoing coordination and evaluation of housing finance policies to ensure proper alignment across taxpayer-supported segments of the nation's housing finance system. GNMA must also evaluate its counterparties and their ability to withstand the stress inherent to changing conditions in the financial markets.

## **3. Provide FHA and GNMA the Tools to Appropriately Manage Risk**

FHA's and GNMA's respective footprints have increased significantly over the last decade—FHA has become the world's largest insurer of mortgages, insuring over \$1.4 trillion of mortgage loans on single-family homes, multifamily properties, and healthcare facilities. The experience of the financial crisis exposed the importance of improving the operational capabilities of FHA and GNMA and their critical need to have some autonomy and greater flexibility in hiring and procurement.

Today, FHA relies upon 40-year-old technology requirements that inhibit responsiveness to sudden market changes. To modernize FHA, Congress should re-charter it as an autonomous government corporation within HUD, which would provide the agency tools and resources necessary to make appropriate risk decisions to respond to changing markets. It is crucial FHA and GNMA have the appropriate tools to manage risk and both agencies must be given resources to hire and compensate talent with specialized expertise in the mortgage finance, risk management, and MBS markets. These reforms will help FHA prevent foreclosures and minimize risk of a taxpayer bailout in times of economic stress in the housing market.

#### **4. Provide Liquidity to the Housing Finance System**

GNMA securitization helps provide liquidity in the mortgage credit market to support the objectives of FHA, the United States Department of Agriculture (USDA), and the United States Department of Veterans Affairs (VA) mortgage insurance programs. During the last 10 years, the size of the GNMA guaranty program has increased in size from less than \$500 billion in 2008 to almost \$2.1 trillion today.

Currently, GNMA's technology platform is secure and robust. As outlined in the U.S. Department of the Treasury's housing finance reform plan, if Congress should authorize it, GNMA could provide an explicit, paid-for guaranty of the timely payment of principal and interest on qualifying MBS that are guaranteed by the GSEs and any potential competitor guarantors that might be chartered by FHFA. In recognition of its increased size and a potential expansion of its role, GNMA must also ensure that program participation requirements mitigate risk to the Federal Government. In support of this goal, GNMA must use its authorities to end lender practices, such as loan "churning," that increase the cost of mortgage credit for borrowers utilizing FHA, USDA, and VA mortgage insurance.

## Introduction

In the wake of the financial crisis, the dream of homeownership receded for many Americans. Today, however, lower taxes and the elimination of unnecessary government regulations have created an economic renaissance, making homeownership less of a dream and more of a possibility. As a direct result of the Trump Administration's pro-growth policies, unemployment is at a 50-year low,<sup>1</sup> and American families are earning higher incomes and enjoying more opportunities than seemed possible just a few years ago.

Yet, there is still one piece of unfinished business from the 2007-2008 financial crisis: housing finance reform. Due to government policies that encouraged risky lending and created moral hazard by building expectations that the Federal Government would bail out failing firms, the housing finance system was a central cause of the financial crisis. This system must be reformed and it is long overdue.

HUD plays a critical role in the nation's housing finance system—FHA provides credit enhancement and regulatory oversight for a portfolio exceeding \$1.4 trillion and GNMA guarantees more than \$2 trillion in MBS, with the full faith and credit of the United States of America. The symbiosis between the government-insured mortgage programs at FHA, the USDA, and the VA – with GNMA-guaranteed MBS – contributes to lower-cost mortgage credit and more affordable homeownership opportunities for creditworthy American borrowers.

As recognized in the March 27, 2019 Presidential Memorandum on Federal Housing Finance Reform (Presidential Memorandum), HUD plays an integral role in the nation's housing finance system. During the financial crisis, and after due to the policies of the previous Administration, FHA's and GNMA's balance sheets swelled, growing by approximately 350 percent and 400 percent, respectively, between FY2007 and FY2018. While FHA and GNMA are designed to be countercyclical, their balance sheets remain at substantially elevated levels and expose taxpayers to significant risks. In the event of a potential downturn in the housing market, FHA and GNMA may incur serious losses, inhibiting their ability to support the housing market and increasing the likelihood of a taxpayer-funded bailout. When the mortgage market contracts and private capital recedes, HUD must maintain stability in the nation's housing finance system by continuing to serve as a countercyclical buffer. When the economy is strong and markets are well-functioning, HUD must avoid competing with other government-supported programs and private capital, and take steps to provide housing finance support to low- and moderate-income families that cannot be fulfilled through traditional underwriting.

Accordingly, now is the time to refocus FHA and GNMA to their core missions and make sure they have the tools needed to manage their significant portfolios. Both organizations face challenges, including FHA's legacy information technology (IT) platforms and processes, the need for enhanced data analytics to support enhanced risk management, and perhaps most importantly, critical limitations on the ability to innovate and decisively react to changing market conditions to prevent taxpayer losses.

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<sup>1</sup> Bureau of Labor Statistics, *April 2019 Household Survey* (Apr. 2019), <https://www.bls.gov/news.release/pdf/empst.pdf>

Reform will reduce the Federal Government's outsized role in housing finance and prevent its activities from crowding out the private sector. Consistent with the goals set forth in the Presidential Memorandum, this plan presents a unique opportunity to define an appropriate role for HUD that refocuses FHA and GNMA on their core missions. By doing so, FHA and GNMA will be better positioned to help low- and moderate-income families become sustainable homeowners, build equity and wealth, and enable FHA and GNMA to act in a countercyclical manner in the event there is an economic downturn without the risk of a taxpayer-funded bailout.

## **A. FHA Background**

FHA's origin traces back to the Great Depression when Congress authorized its creation under the National Housing Act of 1934. The FHA of the 1930s served the same primary function as it does today: providing insurance coverage against losses on mortgages originated by FHA-approved lenders. Then, as in subsequent periods of market distress, FHA's mortgage insurance program has provided stability to the housing market and increased capital liquidity for home buying and construction.

FHA mortgage insurance eliminates the need for lenders to charge additional risk premiums. The reduction in risk allows lenders to offer affordable mortgage credit, expanding homeownership to low- and moderate-income families that cannot be fulfilled through traditional underwriting. FHA particularly benefits low- and moderate-income and FTHBs who may have good credit and income sufficient to support a mortgage, but not the assets to cover more than FHA's 3.5 percent minimum down payment requirement. In return for the benefits of mortgage insurance coverage, borrowers pay mortgage insurance premiums. FHA must generate enough premium revenue (and interest thereon) to cover expected losses and maintain the minimum capital reserve ratio of two percent required by statute.

During the financial crisis, FHA served as a countercyclical buffer in the nation's mortgage finance system by expanding to support the stability of the housing market during and after the financial crisis. When private capital largely withdrew from the housing finance system, FHA's share of mortgages for home purchase (as opposed to refinance mortgages) expanded to a peak of nearly 30 percent. FHA's single-family housing portfolio grew considerably in the wake of the financial crisis, reaching a high of 1,831,234 endorsements in FY2009 and remains at an elevated level. FHA endorsed 1,014,583 loans in FY2018. Today, FHA insures over 8.1 million forward and nearly 500,000 reverse single-family mortgages with more than \$1.2 trillion in UPB. When FHA's multifamily and healthcare programs are included, the total UPB is \$1.425 trillion.

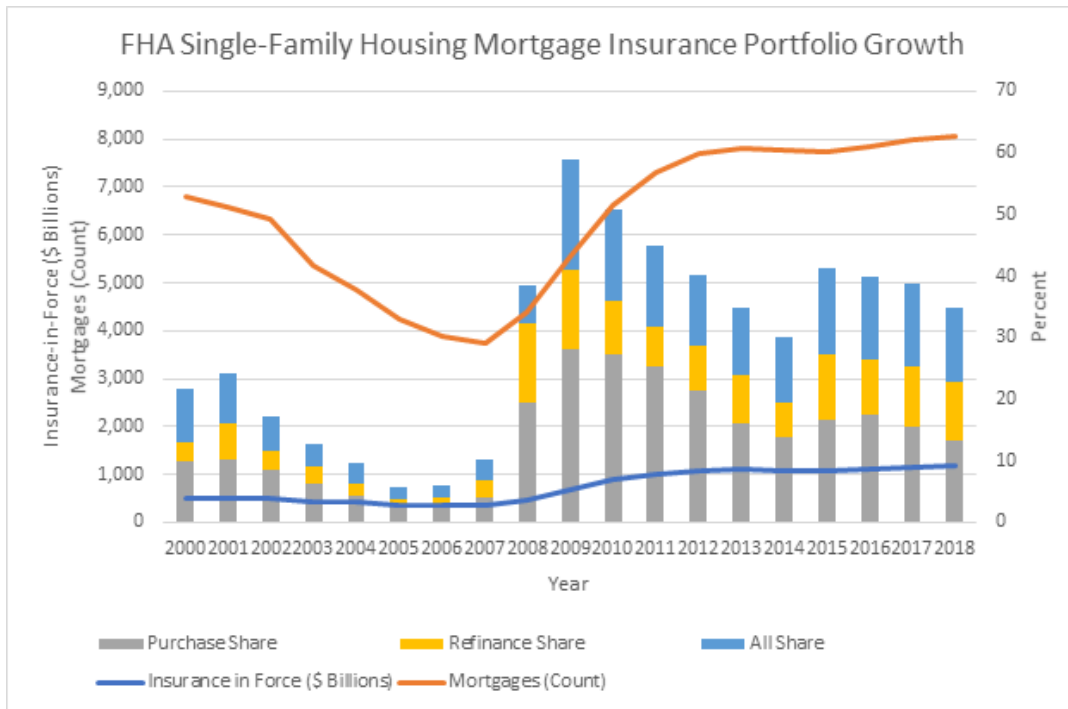


Figure 1

While FHA was created to counter the collapse of the housing finance market during the Great Depression, its mission now includes the promotion of affordable housing opportunities and homeownership, specifically for buyers not served by traditional underwriting. Then, as now, FHA facilitated access to credit for borrowers from lenders and also increased investor confidence to purchase mortgages.

## B. GNMA Background

Since 1968, when Congress authorized the creation of the agency, GNMA has played a central role in the development of the U.S. mortgage securitization system. Then, as now, GNMA effectuates its mission by providing a full faith and credit of the United States guaranty of the timely payment of principal and interest to security holders of MBS backed by pools of mortgages insured or guaranteed by federal agencies, including FHA, VA, and USDA. GNMA does not originate mortgages and does not issue MBS—it relies on issuers that are approved financial institutions to pool or securitize eligible mortgages, either originated or acquired by the issuers to issue GNMA-guaranteed MBS. The GNMA MBS guaranty program supports single-family forward residential mortgages, single-family reverse mortgages through the Home Equity Conversion Mortgage MBS (HMBS) program, and mortgages secured by multifamily and healthcare properties, and manufactured housing.

Following the financial crisis, GNMA’s outstanding MBS portfolio has increased nearly fourfold to over \$2.1 trillion concurrent with growth in the combined mortgage insurance and guaranty programs of FHA and VA. The market was able to absorb this substantial growth, which has been supported through investor demand for alternative full faith and credit instruments (i.e., U.S. Treasuries). The “last position” guaranty in mortgage securitization that GNMA covers in



its MBS guaranty program is an important element of potential reform of the broader housing finance system. As described in the U.S. Department of the Treasury's housing reform report also required pursuant to the Presidential Memorandum, GNMA could – if authorized by Congress – extend its explicit guaranty to MBS backed by conventional and multifamily mortgage loans, as it already has experience in marketing and administering MBS guaranty programs.

## **I. Refocus FHA to its Core Mission**

### **A. Targeting Programs to Borrowers Not Served by Traditional Underwriting**

Following the crisis, FHA's market share increased dramatically while its risk profile has degraded and activities beyond serving its mission borrowers expanded. FHA should refocus its single-family housing mortgage insurance program on low- and moderate-income families, including FTHBs, who cannot affordably access credit through traditional underwriting. Doing so will strengthen FHA's ability to help these borrowers build equity, avoid foreclosure, and protect taxpayers.

Generally, FHA facilitates earlier entry points into homeownership for FTHBs than conventional mortgage loans. This is FHA's most important contribution to the American housing market. The share of FHA-insured purchase mortgage activity for FTHBs has ranged between 75 percent in FY2011 and 83 percent in FY2018. Without FHA insurance, many of FHA's low- and moderate-income, minority, and FTHBs would lack access to affordable mortgage credit. The benchmark for success of FHA's programs should be ensuring that borrowers are receiving financing that is appropriate, sustainable, and optimized for long-term homeownership.

Despite the current strong economy, the credit risk profile of the average FHA FTHB has deteriorated in recent years. Additionally, the average original loan amount for an FHA borrower has increased steadily, from just over \$140,000 in FY2011 to over \$183,000 in FY2018, which has led to an increase in DTI ratios, as home prices generally have increased faster than wages. The average DTI for FHA purchase borrowers reached a post-crisis low in FY2013 of 40.02 percent, but has steadily increased, reaching 43.90 percent by FY2018. Moreover, nearly 24.80 percent of purchase loans in FY2018 had a DTI ratio greater than 50 percent, up from 13.54 percent in FY2013. In addition, average credit scores for FTHBs in the FHA program have deteriorated, decreasing from 687 in FY2010 to 664 in FY 2018. Collectively, these borrower attributes jeopardize the strength of FHA's single-family portfolio.

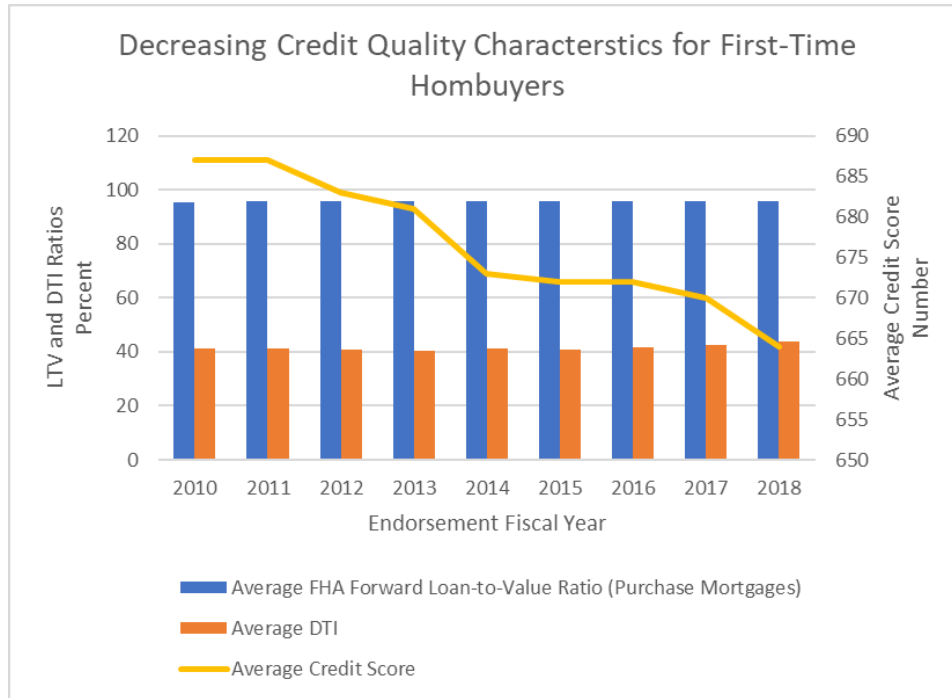


Figure 2

FHA has grown concerned as an increasing number of borrowers have used the FHA program to extract equity from their homes. Some portion of FHA-insured mortgage loans are to borrowers who currently have or previously had an FHA-insured mortgage loan. FHA should assess repeat FHA borrowers to ensure these mortgage loans are consistent with FHA’s mission. The FY2018 cash-out refinance volume of 150,883 loans was the highest reported since 2009.<sup>2</sup> In FY2018, cash-out refinance transactions represented 63.31 percent of all FHA refinance transactions, a substantial increase from the FY2017 level of 38.94 percent.

Particularly troubling is the number of FHA cash-out refinances of conventional loans. In FY2018, 35.05 percent of all FHA refinances were conventional to FHA cash-out refinances up from 23.38 percent in FY2017. On August 1, 2019, FHA took steps to curb the increase in cash-out refinancing within its single-family portfolio by limiting refinances to 80 percent LTV, matching the GSEs’ requirements. FHA should continue to monitor its cash-out refinance business closely to determine whether further action is necessary.

<sup>2</sup> U.S. Department of Housing and Urban Development (2018): Annual Report to Congress Regarding the Financial Status of the FHA Mutual Insurance Fund.

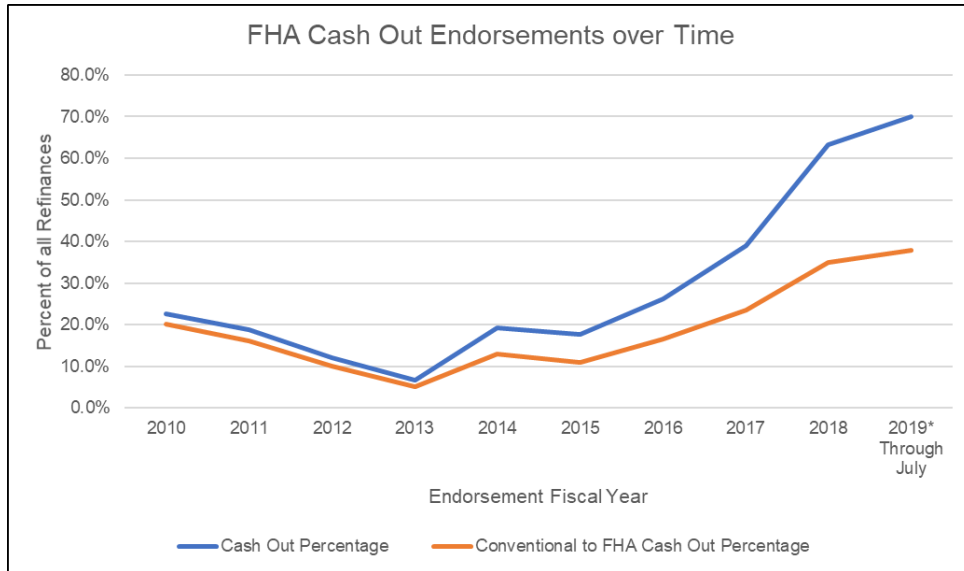
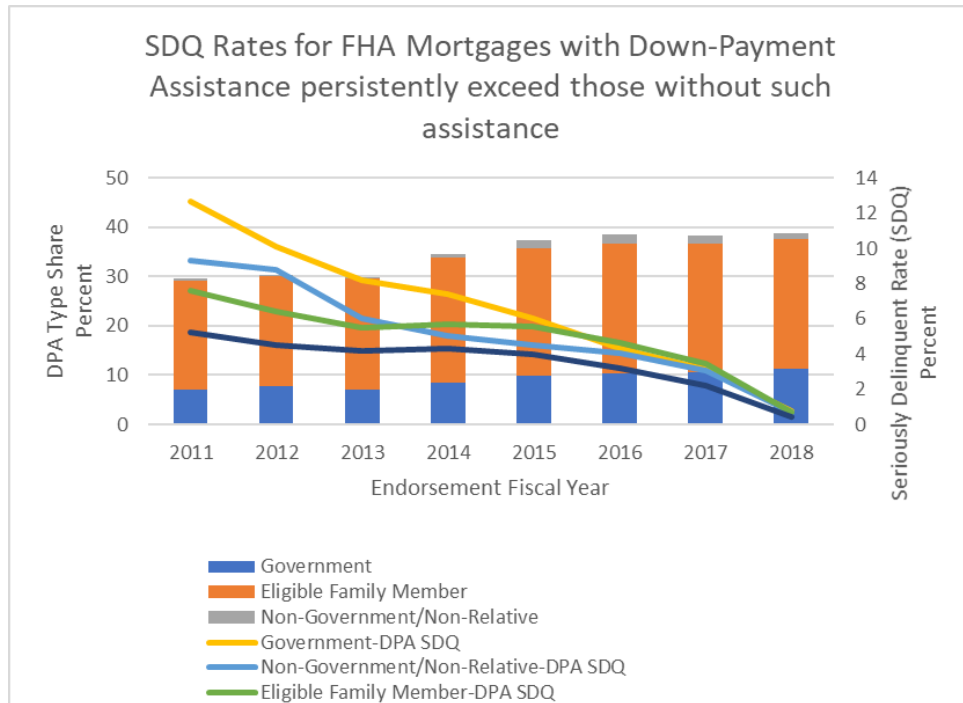


Figure 3

Also of significant concern is the increasing share of FTHBs relying on DPA to finance their purchases. In FY2018, approximately 43 percent of FTHBs relied on some form of DPA. This is the highest post-crisis share when only 34 percent in FY2010 used some form of DPA. Moreover, the average amount of DPA has increased over this period from \$6,667 in FY2010 to \$8,232 in FY2018.

FHA continues to monitor purchase mortgages with DPA given the additional risk in these loans. FHA loan performance data indicate that mortgages with DPA have higher early payment default (EPD) and serious delinquency (SDQ) rates than those without such assistance.<sup>3</sup> The SDQ rates for FY2018 endorsements with government-funded DPA were nearly double those without any form of DPA, and those with DPA covered either by a relative or other source performed only a few basis points better than the government-financed DPA loans. Given the higher EPD and SDQ rates associated with loans with government DPA, FHA will evaluate whether its current premium structure for these loans is commensurate with the risk taxpayers are taking on. It also is important that any DPA provided with respect to FHA loans complies with all legal requirements.

<sup>3</sup> Id. at 38.



*Figure 4*

FHA must consider reforms that maintain support of high initial LTV mortgages, as well as alternative options that incent increasing borrower savings dedicated for repayment support in addition to terms that accelerate equity accumulation, including 20-year mortgages. Faster accumulation of equity benefits borrowers and provides additional protection to the MMIF in the event of borrower default. Ultimately, homeownership must prove to be sustainable, which requires FHA to have the proper incentives in place to ensure a reasonable probability of success especially in the initial years of the loan when borrowers have accumulated limited equity.<sup>4</sup>

In December of 2017, FHA issued a Mortgagee Letter making clear that properties encumbered with Property Assessed Clean Energy (PACE) obligations will no longer be eligible for an FHA-insured mortgage. However, FHA remains concerned with PACE assessments that are placed on FHA loans after endorsement, and is monitoring this practice to determine if further action is warranted. Taxpayers should never have another lien “jump ahead” of FHA and encumber the collateral that makes FHA insurance viable and affordable.

Administrative Reforms:

- FHA should implement a Homebuyer Sustainability Scorecard to measure the performance of loans to low- and moderate-income and FTHBs. The Scorecard will track the percent of mission borrowers who default, return to renting, refinance out of an FHA loan, remain in an original FHA-financed home, and monitor the risk associated with

<sup>4</sup> American Enterprise Institute, *Wealth Building Home Loan*, American Enterprise Institute <https://www.aei.org/feature/wbhl/>.

secondary financing (i.e. DPA). FHA should use the Scorecard to evaluate additional underwriting criteria to ensure that new lending within its single-family portfolio is consistent with FHA's mission.

- FHA should conduct rulemaking to clarify the statutory prohibition on DPA providers that financially benefit from a transaction.
- FHA should examine incentives to make shorter-term mortgages that accelerate equity accumulation more attractive to FHA's mission borrowers.
- FHA should ensure its programs and policies are consistent with its core mission of serving families who cannot be served by traditional underwriting and that these programs and policies do not incent negative borrower behavior such as equity stripping via cash-out refinancing. FHA should continue to monitor its cash-out refinances closely to determine whether further action is necessary.
- FHA should examine the impact of repeat borrowers on the MMIF and ensure these loans are consistent with its mission.

#### Legislative Reforms:

- Congress should establish statutory limitations on FHA cash-out refinances, or at least ensure alignment (e.g., maximum allowed LTV levels) with such refinance transaction in the conventional market (manages borrower adverse selection across agencies).
- Congress should authorize the subordination of any state or local authorized PACE liens that jeopardizes the primary enforcement of FHA's superior lien for its mortgage insurance on existing loans.

### **B. Define Roles for Government-Supported Programs Through Better Coordination**

A central principle of the Administration's reform plan is that federal mortgage credit policies should be better coordinated in order to allow qualified borrowers to access responsible and affordable borrowing options and choices. Coordination ensures that there is not unhealthy and irresponsible competition between government-supported programs, which can lead to lower underwriting standards, increase risk to taxpayers, and threaten the long-term availability of credit to qualified borrowers. The GSEs should not be able to selectively choose from the FHA portfolio and leave taxpayers with the riskiest borrowers.

Due to the fundamental housing missions and mandates of both the GSEs and FHA, borrower choice in selecting the mortgage product that best fits their needs will result in some overlaps in the market. As discussed in this plan, the FHA program is primarily utilized by FTHBs who cannot be served through traditional underwriting, as it generally accepts more risk and provides low downpayment borrowers greater leverage than allowable in GSE programs while also offering government-subsidized pricing.

Uncoordinated policies create incentives that encourage entities to work at cross-purposes, resulting in little or no change in overall access to credit while increasing taxpayer exposure to uncompensated risk. In recent years, the market overlaps might have increased to the extent that the GSEs expanded credit guidelines to “stretch” into the FHA market. For example, DTIs on GSE loans expanded significantly in 2018. Efforts are already underway to address these risk trends and recent new originations indicate progress.

FHFA and FHA should coordinate to ensure that the GSEs and FHA serve defined roles within the marketplace. Ideally, coordinated policies would bring out the best that each has to offer. Consistent with their charters, each GSE’s role should be to perform “activities relating to mortgages on housing for low- and moderate-income families involving a reasonable economic return that may be less than the return earned on other activities.”<sup>5</sup> Similarly, and consistent with the Presidential Memorandum, FHA should focus on low- and moderate-income families that cannot be fulfilled through traditional underwriting.

#### Administrative Reforms:

- HUD and FHFA should develop and implement a specific understanding as to the appropriate roles and overlap between the GSEs and FHA, for example, with respect to the GSEs’ acquisitions of high-LTV and high-DTI loans and FHA’s underwriting of cash-out refinances, conventional-to-FHA refinances, and loans to FHA repeat borrowers.
- Critically important to these overlaps is care by FHA that its government-subsidized premiums, combined with the advantages of the GNMA full faith and credit MBS guaranty, do not undercut private sector pricing for large segments of mortgage loans that can be well served by private capital.

#### Legislative Reforms:

- Congress should establish FHA, VA, and USDA – the government-insured mortgage loan programs – as the sole source of low downpayment financing for borrowers not served by the conventional mortgage market.

### **C. Strengthening FHA Single-Family Default Servicing Processes**

A key part of FHA’s modernization effort is to significantly improve FHA’s outdated servicing policies, processes, and technology. FHA servicing must focus on the critical outcomes of ensuring sustainable homeownership and protecting taxpayers. Over the past decade, the costs associated with servicing both performing and non-performing mortgages throughout the industry have increased significantly. Between 2008 and 2014, the average cost of servicing performing loans increased from \$59 to \$158 per loan per year. Over the same period, the average cost of servicing non-performing loans increased from \$482 to \$1,949 per loan per year, peaking at \$2,357 in 2013.<sup>6</sup>

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<sup>5</sup> 12 U.S.C. § 1716(3).

<sup>6</sup> Laurie Goodman, *Servicing Is an Underappreciated Constraint on Credit Access*, URBAN INSTITUTE (Dec. 15, 2014), <https://www.urban.org/research/publication/servicing-underappreciated-constraint-credit-access>

While servicing costs have increased across the mortgage finance market since the financial crisis, independent estimates indicate that the FHA's servicing costs for non-performing loans are now multiples above the costs of servicing conventional mortgage loans.<sup>7</sup> A recent working paper by the Federal Reserve Board suggests that the cost of servicing FHA loans in foreclosure is 50 times the cost of servicing non-delinquent loans, whereas that ratio is 17 for the GSEs.<sup>8</sup>

The increase in the cost to service loans within FHA's mortgage insurance programs has likely translated into a higher cost of borrowing. FHA proposes the following recommendations to improve its servicing processes in order to promote sustainable homeownership and protect taxpayers.

#### Administrative Reforms:

- To better protect taxpayers, FHA should enhance its ability to better manage borrower defaults, have more flexibility to work out loans, and make timely changes that will reduce costs to the MMIF during stressed economic environments.
- FHA should clarify rules around conveyance and enhance consistency on what is considered "conveyance condition" while incentivizing timely conveyance of properties.
- FHA should enhance its ability to more effectively and efficiently utilize alternatives to conveyance using a "best execution model" that would reduce cost to the MMIF and improve outcomes.
- FHA should create more flexible loss mitigation processes, allowing for increased take-up in such programs, and eliminate unnecessary paperwork and process steps that will streamline borrower qualification in case of hardship.
- FHA should streamline its default milestone timeline that currently adds to management costs, providing greater flexibility to servicers and more appropriately incentivizing them to work toward more efficient resolutions, with consideration given to market conditions.
- FHA should reduce uncertainty and business risk of participation in FHA loan programs produced by penalties that do not match the severity of missed deadlines.
- FHA should establish a paperless data-driven claims process to replace the current inefficient and paper-intensive process. The new claims process will ensure that claims are validated before they are paid in order to better protect taxpayers.

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<sup>7</sup> Karen Kaul, Laurie Goodman, Alanna McCargo, and Todd M. Hill-Jones, *Reforming the FHA's Foreclosure and Conveyance Processes*, URBAN INSTITUTE (Mar. 1, 2018)

<https://www.urban.org/research/publication/reforming-fhas-foreclosure-and-conveyance-processes>

<sup>8</sup> You Suk Kim, Steven M. Laufer, Karen Pence, Richard Stanton, and Nancy Wallace, *Liquidity Crises in the Mortgage Market*, WASHINGTON: BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM (2018), <https://doi.org/10.17016/FEDS.2018.016r1>.



- The Consumer Financial Protection Bureau (CFPB), FHA, and FHFA should jointly study how to reduce the costs of default mortgage servicing.

#### D. Ensure HUD’s Multifamily Programs are Appropriately Targeted

FHA’s multifamily mortgage insurance products play a critical role in ensuring that credit for multifamily development is available in many mid-size and smaller markets with a focus on low- and moderate-income families that are not traditionally served by private sector lenders. By financing affordable and market-rate housing, FHA’s multifamily program ensures access to safe and affordable housing for our nation’s workforce and vulnerable populations.

However, FHA’s multifamily lending policies should not discourage private capital from supporting preservation and development of affordable housing. Over the last decade, FHA’s multifamily program grew substantially, and its market share remains far above pre-crisis levels. FHA multifamily production volume peaked in 2013 with \$18.4 billion in new originations. In FY2018, FHA’s multifamily program closed 908 FHA-insured multifamily transactions worth \$15.2 billion with an asset management portfolio composed of 11,549 FHA-insured assets with a UPB of \$97 billion. In addition, FHA manages a portfolio of non-insured assets that support low-income housing through rental assistance subsidies.

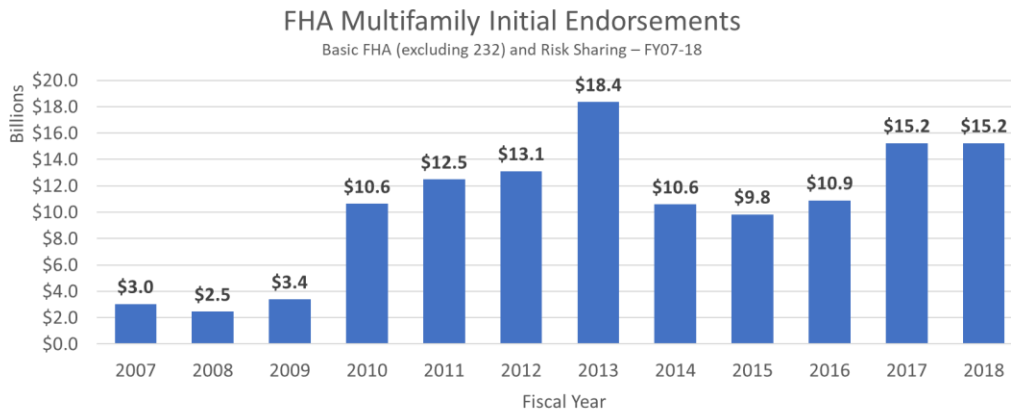


Figure 5

FHA maintains a successful program, the Rental Assistance Demonstration (RAD), allowing public housing agencies (PHAs) and owners to leverage the private market to make capital improvements and preserve the properties for long-term affordability. Using one of two components, RAD facilitates the conversion of properties to project-based Section 8 contracts by allowing public housing projects to convert to long-term Section 8 rental assistance contracts; or allowing properties currently operating under HUD’s legacy programs to convert tenant-based vouchers to project-based assistance. Launched in 2012, it has proven to be a successful model for preserving HUD-assisted affordable rental housing that might otherwise be lost to disrepair or neglect.

The following administrative and legislative reform recommendations are designed to reduce barriers to development of affordable rental housing for lower-income, workforce, and vulnerable populations in the nation's most underserved markets.

#### Administrative Reforms:

- Similar to the planned collaboration on single-family housing mortgage insurance programs, FHA and GNMA should establish proper coordination and information exchange processes with FHFA to ensure that government-supported multifamily programs do not overlap and compete with private capital.
- HUD should modify current noise regulations to permit development on property sites with noise levels above 75 decibels, which would likely encourage development in walkable, urban areas (including Opportunity Zones) close to transit and jobs and aligning with FHA's Multifamily Housing goals of more affordable housing.
- HUD should modify its current environmental review policy to increase the 200-unit threshold to 300 units which would allow for the completion of multifamily projects in more reasonable timelines, aligning with HUD's goals of more affordable rental housing to better meet the demand.

#### Legislative Reforms:

- Congress should eliminate the 455,000-unit statutory cap in the RAD program, which will expand its reach and impact.
- Congress should provide funding for investment in a strategic modernization plan which will holistically overhaul and integrate FHA's Multifamily IT systems. These systems will likely face unsustainable operating and management costs in the near future, and not leveraging the proposed IT road map, and retaining antiquated IT systems, is likely to make new future interconnections across HUD difficult, if not impossible.

### **E. Provide Regulatory Certainty to FHA Lenders**

FHA's lender base has shifted substantially in the last decade. Today, depository institutions represent less than 15 percent of lenders originating FHA-insured mortgages, down significantly from approximately 45 percent of the lender base in 2010.<sup>9</sup> Depositories have cited potential legal liability related to enforcement actions under the FCA as a leading reason for their limited participation, although increased regulatory burdens after 2010 have contributed to the decreasing share of depositories in mortgage lending, including participation with FHA.<sup>10</sup> Lenders have expressed concerns with the past discrepancy between the severity of the infraction and the potential penalties that were sought under the FCA—minor errors leading to exposure to severe financial penalties.

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<sup>9</sup> You Suk Kim, Steven M. Laufer, Karen Pence, Richard Stanton, and Nancy Wallace, *Liquidity Crises in the Mortgage Market*, BROOKINGS INSTITUTION (2018), <https://doi.org/10.17016/FEDS.2018.016r1>.

<sup>10</sup> Greg Buchak, Gregor Matvos, Tomasz Piskorski, Amit Seru, *Fintech, Regulatory Arbitrage, and the Rise of Shadow Banks*, JOURNAL OF FINANCIAL ECONOMICS 130 (3) (2018)

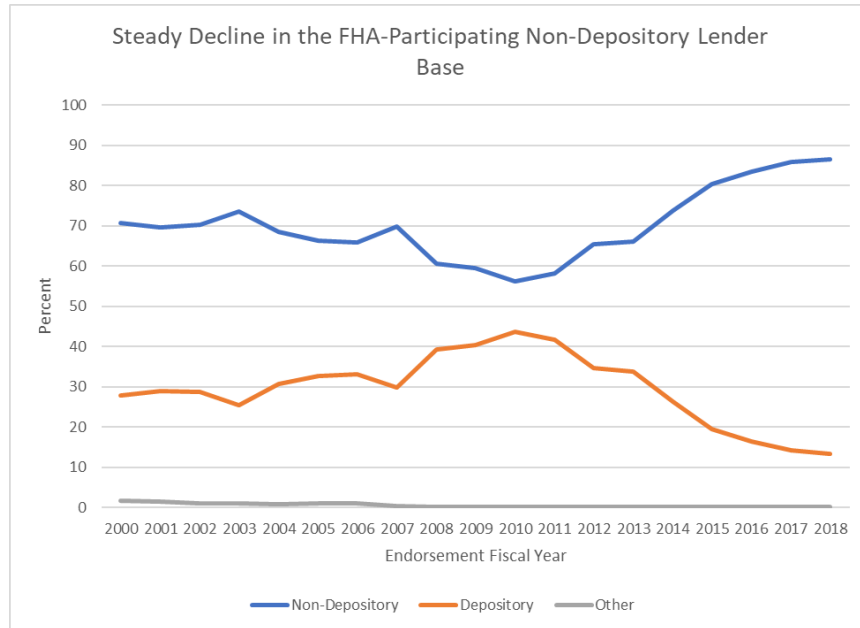


Figure 6

FHA strives to be clear in its guidance on compliance and legal enforcement matters and will not tolerate bad actors—those who seek to defraud borrowers and taxpayers, as well as those who make routine (and often material) errors that put strain on the agency’s resources. FHA makes it a top priority to adhere to the rule of law, and this means the agency’s view of materiality should be clearly communicated. FHA participants and advocacy groups have called for clarification of the process by which HUD and DOJ consider whether to pursue FCA remedies.

Administrative Reforms:

- FHA should continue to work with the DOJ to provide more clarity on how the agencies will consult on the appropriate use of the FCA.
- FHA should revise and expand its defect taxonomy in order to clearly align the severity of loan underwriting defects with proposed remedies.
- FHA should continue prioritizing the revision of certifications, which lenders attest for each FHA-insured loan, as well as lenders’ annual certifications. These revisions will provide lenders additional certainty and clarity on FHA’s requirements.

Legislative Reform:

- Congress should make a statutory change to permit shorter suspension periods and eliminate the annual cap on civil money penalties for program participants to provide FHA more flexibility when assessing penalties.

## **II. Protect American Taxpayers**

### **A. Strengthen FHA Risk Management Systems and Governance**

To ensure protection of the American taxpayer, a modernized FHA risk management organization is critical. As the size of FHA's portfolio has not returned to pre-crisis levels and taxpayers continue to bear increased risk, now is an appropriate time to develop and implement a framework that will better allow the agency to monitor current, emerging, and future countercyclical risks. The operational tools to build an exceptional risk management framework should include establishing appropriate risk tolerances and scorecards to monitor risk, updating risk model governance, and establishing credit risk transfer (CRT) program(s) which would introduce private sector investment, reducing risk to the overall FHA portfolio and the American taxpayer.

The lack of flexibility when addressing egregious underwriting errors or servicing breakdowns has become particularly detrimental as counterparty risk escalates throughout the mortgage system. For example, FHA is not allowed to force repurchases – as the GSEs are able – to enforce underwriting guidelines. FHA instead is limited to an indemnification alternative, essentially a “promise to pay,” to be applied regardless of the financial wherewithal of the offending counterparty. An ability to unwind the FHA insurance policy would insulate FHA from counterparty risk as it enforces its underwriting guidelines. Doing so will reduce the risk that the taxpayer will have to bear the cost of a counterparty's failure to perform.

#### Administrative Reforms:

- FHA should adopt a sound risk-based capital regime for the MMIF, well above the statutorily mandated two percent capital ratio, which will manage risk exposure to defined stress scenarios and ensure that FHA does not inappropriately compete with the GSEs or private capital.
- FHA should adopt a sound risk-based capital standard to manage exposure in the current insured portfolio for the General Insurance/Special Risk Insurance (GI/SRI) Fund and for future stress cycles and ensure that FHA does not inappropriately compete with the GSEs or private capital mortgage financing.
- FHA should pursue an inter-agency agreement with other government agencies (including GNMA and FHFA) involved in mortgage insurance and mortgage securitization on counterparty risks.
- FHA should pursue an inter-agency agreement on credit policy coordination with other government mortgage insurance agencies and FHFA which will help ensure a more efficient targeting and reducing overlap as FHA (and GNMA) achieve the policy goal of assuming primary responsibility for providing housing finance support to low- and moderate-income families that cannot be fulfilled through traditional underwriting.
- FHA should revise its risk-modeling governance, which will include a decreased reliance on contractors for technical and modeling expertise.

### Legislative Reforms:

- Congress should direct HUD to evaluate the options, feasibility, and economics of a CRT program similar to those recently implemented by the GSEs, with the purpose of exploring options to reduce the overall risk to taxpayers while still serving HUD's mission borrowers.
- Congress should direct FHA to more effectively manage lender counterparty risk in future books by authorizing such additional remedies as appropriate.

### **B. Improve Financial Viability of the Home Equity Conversion Mortgage Program**

At the end of FY2018, FHA's HECM portfolio had an economic net worth of negative \$13.63 billion and a standalone capital ratio of negative 18.83 percent. Changes made to the principal limit factors and insurance premiums in 2017, as well as the implementation of an appraisal inflation risk mitigation policy in 2018, have been directionally positive, but financial volatility within the HECM program remains a challenge for FHA.

The risks in the HECM portfolio have been shaped by the following features:

- HECMs accrue loan balances over time as opposed to forward mortgages where loans generally amortize as they mature.
- Unique mobility risks generally dependent on the longevity of borrowers (and eligible non-borrowing spouses that remain in homes secured by HECMs).<sup>11</sup>
- HECMs are non-recourse loans, meaning FHA has limited ability to recover financial losses on loan terminations beyond the value of the property.<sup>12</sup>
- HECMs can carry fixed or adjustable rates, although since FY2014, new HECM endorsements have predominantly been Adjustable Rate Mortgages (ARMs).
- HECMs remain subject to front-end appraisal bias risks and extreme fluctuations in home valuations. Several analyses have shown the prevalence of appraisal inflation in HECM transactions—reaching as high as 29 percent in 2009—which ultimately increased losses to the MMIF.
- Programmatic and capital/fund management challenges dealing with distantly-valued collateral (based on long-term forecasts of interest rates and home price changes).
- Mortgagee risks in having to fund borrower draws over time with loan balance repayment only demanded upon termination of HECMs. This puts cash-flow/liquidity risks on financial institutions originating and servicing HECMs that must fund borrower draws (that are not always neatly mapped out) prior to receiving any actual repayment from borrowers.

### Administrative Reforms:

- FHA should assess and revise its monitoring protocols of front- and back-end appraisal bias.

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<sup>11</sup> Adam W. Shao, Katja Hanewald, Michael Sherris, *Reverse Mortgage Pricing and Risk Analysis Allowing for Idiosyncratic House Price Risk and Longevity Risk*, INSURANCE: MATHEMATICS AND ECONOMICS Vol. 63

<sup>12</sup> Reverse mortgages, which tend to limit household mobility correlate to discounted property values over time.

- FHA should develop servicing standards for HECM products that will result in reduced operational and financial burdens on servicers and FHA.
- FHA should eliminate HECM-to-HECM refinancing, as these loan transactions result in greater appraisal inflation, increasing lending against properties that go up in value while being left with existing portfolio exposure on properties that have minimal (even decreasing) change in value. These transactions also negatively impact GNMA-guaranteed HMBS by influencing quick churn in pool participations.

#### Legislative Reforms:

- Similar to the forward mortgage product, Congress should revise the loan limit structure in the HECM program to reflect variation in local housing markets and regional economies across the United States instead of the current national limit set to the level of high-cost markets in the forward program. Currently, the HECM program utilizes one nationwide loan limit of \$726,525 (for 2019).
- Congress should set a separate HECM capital reserve ratio and remove HECMs as obligations to the MMIF. This would provide for more transparent accounting of program costs and decrease cross-subsidization that occurs with mission borrowers in the forward mortgage portfolio.

### **C. Implement Tiered Pricing to Protect the MMIF**

To ensure that FHA and taxpayers are properly compensated for riskier loans, FHA should implement a tiered pricing framework to protect the MMIF from excessive exposure to riskier loans, especially loans with higher risk DPA. Tiered pricing would allow FHA to diminish the drain of FHA's higher risk loans on the MMIF. It would not open new markets already served by private mortgage providers, since FHA would not lower premiums on its 30-year fixed rate product through this effort.

#### Administrative Reforms:

- FHA should develop and implement a tiered pricing system in order to protect the MMIF and ensure it is pricing appropriately for higher-risk loans.

### **D. Eliminating Regulatory Barriers to Affordable Housing Including Manufactured Housing**

For many American families, ownership of a single-family home represents a key facet of the American Dream. It is through single-family homeownership that many families put down roots, become active in their communities, and build wealth for future generations. However, overregulation of housing construction has been a key factor in supply failing to meet growing demand, particularly for entry-level housing in high-cost urban markets. As a result, even with low unemployment and strong wage and job growth, many creditworthy FTHBs are unable to afford the purchase of entry-level housing.

Research indicates that more than 24 percent of the cost of a new single-family home is the direct result of federal, state, and local regulations.<sup>13</sup> For multifamily, the figure is over 30 percent.<sup>14</sup> This has been a factor in the failure of new multifamily and single-family construction to keep pace with the formation of new households. Census Bureau data indicates that from 2010 to 2016, only seven homes were built for every ten households formed. This shortage in housing supply contributes to an unsustainably high financial burden borne by low- and middle-income Americans.

The Trump Administration is committed to reducing the red tape that is stifling housing choice for far too many American families. On June 25, the President continued his historic deregulation campaign by signing an Executive Order establishing the White House Council on Eliminating Regulatory Barriers to Affordable Housing. The Council, led by HUD Secretary Ben Carson, will build on the President's commitment to hardworking Americans by reducing overly burdensome regulations that artificially raise the cost of housing development that directly lead to the undersupply of affordable housing, and engaging with state, local, and tribal partners to help them do the same.

For many American families, entry-level housing options, including starter homes, condominiums and manufactured housing, serve as important steppingstones to achieving their ultimate dream of purchasing a single-family home in which to raise their children and build wealth for the long term. HUD plays a critical role in helping creditworthy first-time and low- and moderate-income borrowers achieve their goals, through FHA's insurance of entry-level housing, from which borrowers can successfully graduate to non-government-supported mortgages of future homes.

Manufactured housing<sup>15</sup> plays a vital role in meeting the nation's affordable housing needs, providing 9.5 percent of the total single-family housing stock. More than 22 million Americans reside in manufactured housing with a median annual household income of less than \$30,000. Manufactured homes are particularly important in rural communities, where they are approximately 16.2 percent of occupied housing units. The manufactured housing industry also plays an important part in the economy, accounting for approximately 40,000 jobs nationwide.<sup>16</sup> HUD regulation of manufactured housing fulfills a critical role of both protecting consumers and ensuring a fair and efficient market.

Policies that exclude or disincentivize the utilization of manufactured homes can exacerbate housing affordability challenges because manufactured housing potentially offers a more

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<sup>13</sup> Paul Emrath, Ph.D., Government Regulation in the Price of a New Home, HOUSINGECONOMICS.COM (May 2, 2016), <http://www.nahbclassic.org/generic.aspx?genericContentID=250611&channelID=311>

<sup>14</sup> Paul Emrath and Caitlin Walter, Regulation: Over 30 Percent of the Cost of a Multifamily Development, NATIONAL ASSOCIATION OF HOME BUILDERS (June 12, 2018), <http://www.nahbclassic.org/generic.aspx?genericContentID=262391>

<sup>15</sup> A manufactured home is built to the Manufactured Home Construction and Safety Standards (HUD Code) and displays a red certification label on the exterior of each transportable section. Manufactured homes are built in the controlled environment of a manufacturing plant and are transported in one or more sections on a permanent chassis.

<sup>16</sup> Manufactured Housing Institute, *2018 Manufactured Housing Facts: Industry Overview*, MANUFACTURED HOUSING INSTITUTE (June 2018), <https://www.manufacturedhousing.org/wp-content/uploads/2018/06/2018-MHI-Quick-Facts-updated-6-2018.pdf>

affordable alternative to traditional site-built housing without compromising building safety and quality. The failure to periodically update the Construction and Safety Standards, for example, has hindered the manufactured housing industry's ability to economize and leverage current construction techniques and materials that require special HUD approvals. In the previous Administration, updating the Construction and Safety Standards was not a priority, and the current requirements have not been updated in any significant way since 2009. HUD should take action to address barriers to the greater adoption of manufactured housing.

#### Administrative Reforms:

- Pursuant to the Executive Order of June 25, 2019, the HUD-led White House Council on Eliminating Regulatory Barriers to Affordable Housing will identify and recommend actions and policies to mitigate regulations that unnecessarily increase the cost of creating and preserving housing that is affordable and work with state, local, and tribal partners to do the same.
- FHA should consider innovative proposals to modify single-family housing mortgage finance underwriting to further encourage and promote additional supply of entry-level housing, particularly manufactured housing.
- To encourage innovation in manufactured housing, HUD should create a formal framework for identifying and evaluating new building, construction, and design developments and ensuring that HUD's regulations do not unnecessarily impede their adoption. This framework would help gather the evidence necessary to update HUD's regulations on a regular cadence, thereby better keeping up with evolving technology.
- HUD should devote resources to ensure the HUD-Code is modernized to incorporate the standards recommended by the MHCC, to minimize overly burdensome regulatory and compliance requirements, and to encourage innovation. Once revised, HUD should also move to a regular cadence of updating its code to ensure that it is keeping pace with evolving technologies and best practices.
- HUD should publish updated Title I standards that address regulatory burdens of participating in the program as part of its Single Family Housing Policy Handbook 4000.1 (SF Handbook), which is intended to serve as the consolidated, consistent, and comprehensive source of FHA Single Family Housing policy.
- HUD should elevate the Office of Manufactured Housing Programs within HUD and appoint a Deputy Assistant Secretary to lead it.



### **III. Provide FHA and GNMA the Tools to Appropriately Manage Risk**

#### **A. Establish FHA as an Autonomous Corporation within HUD**

FHA was established as an independent agency in 1934, but was incorporated into HUD when the Department was created in 1965. Unlike other offices within HUD, which generally support very low- and extremely low-income individuals and families, FHA offers mortgage insurance products to enhance access to homeownership, rental housing, and healthcare facilities. FHA needs autonomy within HUD to ensure it is able to keep pace with evolving portfolios and a dynamic, ever-changing marketplace. More independence would provide FHA greater control over staffing and procurement, including technology. It is vital that FHA be given increased authority to better address risk management functions that can suffer from being part of a larger organization.

##### Legislative Reform:

- Congress should enact legislation to restructure FHA as an autonomous government corporation within HUD.

#### **B. Hire and Retain the Right Talent to Mitigate Risks to Taxpayers**

FHA and GNMA face challenges in hiring and retaining sufficient staff with expertise in mortgage finance and asset management. FHA and GNMA need the appropriate staff to manage their current large portfolios and ensure future books of business are appropriately mission-focused. Despite a significant increase in volume in both the forward and reverse mortgage programs, FHA's Office of Single Family Housing staff has decreased from 1,007 full-time employees (FTEs) in 2010 to 751 FTEs as of August 2019, a decline of 25 percent. Furthermore, 28.7 percent of the current workforce is eligible for retirement and 45.76 percent will be eligible within 5 years. By addressing these human capital challenges, FHA and GNMA can improve the management and oversight of their guaranteed loan and MBS portfolios.

##### Administrative Reforms:

- Like GNMA, FHA should explore the targeted use of pay flexibilities available under current law (e.g., Critical Pay) to improve hiring and retention of key positions requiring specialized technical skills related to the mortgage and securitization markets.

#### **C. Align Contracting and Procurement Processes with Business Needs**

FHA is limited in its ability to engage qualified and capable contractors in a timely manner because HUD's contracting process is burdensome and protracted. The material deficiencies in the agency's operational processes, risk management guidelines, and technologies have contributed to losses to the MMIF and a failure to capably protect HUD's security interests, respond to customer and borrower inquiries, monitor loans for program compliance, and process property disposition requests. GNMA has made broad use of its authority as a government corporation to contract for services as it conducts commercial activities. Its ability to do this

effectively has been a major contributor to its record of achieving its mission on a large scale with a notably smaller base of government staff.

#### Legislative Reform:

- To the extent administrative reforms are insufficient to address procurement challenges at FHA and GNMA, Congress should propose new statutory acquisition authorities for HUD, particularly to address instances where material underperformance of contracting vendors results in substantial quality deficiencies and costs.

#### **D. Modernize FHA Technology**

FHA has operated for decades on antiquated technology platforms that inhibit its ability to appropriately manage risk. FHA's over-reliance on outdated IT platforms ultimately increases the cost of mortgage credit by increasing business operating costs of originators and loan servicers. Currently, FHA's platform is built on a more than 40-year-old mainframe system that runs an obsolete programming language. The risk that this presents to FHA and, by extension, to the American taxpayer, is significant. Not only is FHA's current IT system outdated—it is unreliable. In FY2018 alone, there were 174 outages of Single Family's core systems.

To support the broad goal of greater standardization between FHA and industry business practices and processes, FHA has developed a detailed technology roadmap that will guide the development of a single platform and baseline architecture. The new IT system will cover all aspects of the mortgage process, from loan origination, through endorsement, servicing, claims, and, as required, disposition.

The investment in the new single platform structure will allow FHA to better adapt to changing industry, regulatory, and statutory requirements. The modernized systems will be data-driven, and ultimately allow FHA to fully digitize the mortgage process, opening doors to significantly more intensified risk analysis and management. The completion of this effort will permit FHA to increase compliance and reduce costly operational burdens, such as heavily paper-based processes currently in place. Importantly, it will also protect taxpayers from losses that result from fraud, in addition to reducing costs associated with maintaining and operating inefficient legacy systems and business processes.

By grounding the development of the new architecture in reducing operational risk, FHA can focus on delivering much-needed clarity and efficiency in its programs. This approach also lays the foundation for the incremental phase-out of FHA's legacy mainframe systems. By modernizing now, FHA has an opportunity to move generations ahead to a state-of-the-art system that leverages industry advancements including fast-feedback mortgage applications, upfront certainty, appraisal scoring, revised Mortgage Industry Standards Maintenance Organization (MISMO) data standards, integration of independent verification services, an application programming interface (API) driven ecosystem, and active loss mitigation guidance.

#### Administrative Reforms:

- FHA should explore agreements to share technology with GNMA and other government-supported mortgage programs when feasible.

- FHA should develop a mortgage origination risk tool integrating an automated underwriting system (AUS) platform, appraisal scorecard, risk assessment tool, and third-party verification services.

Legislative Reforms:

- Congress should appropriate sufficient funds for FHA to complete its multi-year single-family IT modernization effort.

**E. Realign Housing Assistance Programs into a New Office of Rental Subsidy and Asset Oversight within HUD**

The Federal Housing Commissioner oversees and administers mortgage insurance on FHA’s single-family forward and reverse, multifamily, and healthcare programs. Concurrently, that same person serves as the Assistant Secretary for Housing, overseeing and administering programs that provide rental assistance and subsidy to low-income, very low-income, and extremely low-income Americans including: Project-Based Rental Assistance (PBRA), Section 202 Housing for the Elderly, Section 811 Housing for the Disabled; the Rental Assistance Demonstration (RAD) program; federal regulation of manufactured housing, and housing counseling.

As it considers restructuring FHA as an autonomous corporation within HUD, Congress also should consolidate the PBRA, Public Housing, and Housing Choice Voucher subsidy programs (Sections 8 and 9), along with the RAD and Real Estate Assessment Center (REAC) functions, into a newly created Office of Rental Subsidy and Asset Oversight within HUD. In doing so, Congress should separate the dual roles of Federal Housing Commissioner and Assistant Secretary for Housing, as the Federal Housing Commissioner’s duties should focus solely on managing the FHA insurance programs. The realignment will achieve greater efficiencies, reduce regulatory and administrative burdens, increase self-sufficiency opportunities for residents receiving federal rental assistance or supportive services, and promote greater cost efficiency and asset management of the subsidized portfolio.

Administrative Reform:

- Absent legislation, the Department should pursue a reorganization that separates its mortgage insurance and rental assistance programs into separate offices.

Legislative Reforms:

- Congress should enact legislation to separate the position and responsibilities of the Federal Housing Commissioner from the position and responsibilities of the Assistant Secretary for Housing.
- Congress should enact legislation to create a new Office of Rental Subsidy and Asset Oversight overseen by the Assistant Secretary for Housing which would consolidate multifamily housing subsidy programs, Public Housing and Housing Choice Voucher programs, together with RAD and REAC.

- As part of this reorganization, Congress should establish the Office of Native American Programs as a separate office, led by a Presidentially-appointed, Senate-confirmed Assistant Secretary and separate the Native American programs from the other programs within HUD's Office of Public and Indian Housing.

## **IV. Provide Liquidity to the Housing Finance System**

Issuers participating in GNMA's MBS guaranty program pay the agency an on-going guaranty fee, as well as other incidental fees, predominantly for provision of the guaranty on pass-through income to securities investors. The guaranty fees charged by GNMA are fixed and set in statute. Interest income from borrowers in excess of the pass-through rate payable to security holders and GNMA's guaranty fee is retained by the issuer as mortgage servicing fees. GNMA's program requires the retention of certain minimum servicing fees to ensure servicing of the loans for the life of the GNMA MBS guaranty. Servicing fees, along with other cash flows associated with the on-going servicing of the mortgage loan (and net of the costs to service the mortgage loan), constitute an asset of the issuer called mortgage servicing rights (MSRs).

GNMA has prioritized risk management and the ongoing need for programmatic and organizational change to reduce the risk of issuer failures, thus minimizing the possibility of utilizing taxpayer funds in the operationalizing of the GNMA guaranty. In this regard, the agency faces a wide spectrum of risks stemming from the risk of a single large issuer failure (today, for example, nearly 40 percent of the securities outstanding are serviced by five non-banks) to multiple issuer failures, which would be operationally challenging to manage simultaneously (at present, one percent of the securities outstanding are serviced by 125 non-bank issuers). Overall, there are five key areas where GNMA will continue to focus its efforts and implement reforms:

- Strengthening the internal framework and operational structure to best manage counterparty risk by re-aligning internal responsibilities and creating new position and processes to monitor and address sources of risk that have increased as the housing financing industry has evolved.
- Increasing reliance on data and modeling to uncover and illuminate trends and risks that are not apparent from traditional compliance activities – a prime example is leading the industry toward widespread use of stress testing modeling.
- Increasing the enforcement, recovery and resolution capabilities in the event of issuer stress, with the objective that GNMA would be address adverse circumstances, including a large-scale issuer failure, without the occurrence of severe market or consumer disruption.
- Continuing focus on facilitating sufficient system liquidity (and liquidity management practices), given the now non-bank-dominated industry's increased reliance on steady flows of external capital.
- Continuing refinement of program standards and requirements relating to all of the above.

## **A. Advance GNMA Counterparty Risk Management and Securitization Platform Transformation**

GNMA should increase its counterparty risk management ability. GNMA continues to rely on existing staff resources, the ability to update policies and requirements through All Participants Memorandums (APMs), and the authority to take enforcement action if required. Critical to GNMA's success in such reform is support and coordination with those that oversee GNMA, such as HUD and OMB.

The following details the areas where GNMA should continue to strengthen and modernize its internal approach to risk, program guidelines and securitization platform transformation to better serve and protect borrowers, investors, issuers and taxpayers.

### Administrative Reforms:

- GNMA should transition the MBS platform from pool-level to loan-level functionality, including the ability to transfer servicing of individual loans within a pool. This reform will enhance the desirability and value of the MSR asset and reduce the cost of loans insured or guaranteed by Federal agencies relative to conventional loans.
- GNMA should continue to facilitate adequate liquidity in the housing finance system, including the implementation of reforms for the financing of and investment in MSRs, and oversight of the development of industry-level liquidity management methods, as outlined in the GNMA 2020 reform agenda.<sup>17</sup>
- GNMA should continue to maximize the value of its servicing portfolios, such as through establishing servicing fee standards and enhanced monitoring of servicing transfers to ensure that both parties maintain adequate MSR values.
- GNMA should enhance issuer standards through strengthened risk management requirements, including updated liquidity, leverage, and capital standards, with particular focus on very large issuers and sub-servicers.
- GNMA should strengthen its risk management analytics and predictive capabilities to mitigate risks, given the growing share of the agency's portfolio comprised of very large, non-bank counterparties. This should include GNMA's ongoing development of stress test modeling capability and the imposition of a stress testing regimen for non-bank institutions to evaluate performance under a range of economic scenarios.
- GNMA should implement enforcement, recovery and resolution reforms to protect taxpayers, which should include building the capability for the agency to move quickly, effectively and fairly to sanction firms who are failing to abide by program terms, and to address issuers who are vulnerable to failure, or otherwise threatens the sound administration of the MBS program.

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<sup>17</sup> [https://www.ginniemae.gov/newsroom/publications/Documents/ginniemae\\_2020\\_progress\\_update.pdf](https://www.ginniemae.gov/newsroom/publications/Documents/ginniemae_2020_progress_update.pdf)

- GNMA should fully modernize platform access, data standards, collection, and storage, which will transform the user interaction with the securitization and data analytical architecture into a highly secure, single gateway. This reform would increase GNMA’s ability to monitor its issuers, enforce its rules and requirements, and manage the overall safety and soundness of the program, as well as efficacy and validity of data collected and reported through the Mortgage Banker’s Financial Reporting Form.
- GNMA should develop and implement the policies, technology and operational capabilities necessary to accept digital promissory notes (eNotes) and other digitized loan files as acceptable collateral for its securities, which will enable issuers to enhance efficiency, risk management and customer experience by moving to digital collateral and a fully electronic “eClosing” process.

## **B. Guaranty Fee-setting Flexibility**

GNMA’s single-family guaranty fee of six basis points (bps) was set by statute 1987. This guaranty fee provides the funds from which losses would be paid if GNMA needed to step in to remit funds to security-holders as the result of an issuer’s failure to do so. This six bps guaranty fee is also the source of funds for payments relating to loans that were in pools seized in the past by GNMA in cases of issuer failure.

GNMA believes that the authority to administratively adjust its guaranty fee within a narrow, permissible range, would ensure that such fees are adequate for the risks in the program and sufficient for GNMA to meet its statutory obligations under extreme circumstances. Under this proposal, GNMA would be required to justify and seek approval for any proposed adjustments from the HUD Secretary, but the change would require no further passage of law.

GNMA currently possesses a level of reserves the agency deems adequate to meet foreseeable needs to exercise and fulfill its guaranty. Thus, GNMA is not at this time proposing a specific increase in the fee. GNMA’s financial requirements have increased, however, and are likely to continue to do so, notably due to the increasing share of non-bank responsibility for residential mortgage servicing which has increased both the likelihood and the potential size of a call on GNMA’s guaranty. This reform recommendation is not be intended to change the purpose of the guaranty fee, which is to provide funds for financial obligations resulting from GNMA having exercised the guaranty. Rather, the reform would provide flexibility to the agency to seek adjustments needed to ensure efficiency and operational effectiveness as the secondary mortgage market continues to evolve, and ultimately ensure its MBS guaranty program maintains fiscal soundness.<sup>18</sup>

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<sup>18</sup> For reference, this item was highlighted in Government Accountability Office’s (GAO) May 2019 audit, “*GNMA: Risk Management and Staffing-Related Challenges Need to be Addressed.*” Specifically, GAO recommended that “The Chief Risk Officer of GNMA should periodically conduct an actuarial or similar analysis that includes a stress test to evaluate the extent to which the current level of the guaranty fee for single-family MBS provides GNMA with sufficient reserves to cover potential losses under different economic scenarios.”

#### Legislative Reform:

- Congress should pass legislation granting GNMA the authority to administratively adjust its guaranty fee within a narrow, permissible range.

### **C. Reforms to Maintain the Integrity of GNMA Securities**

Over the past two years, GNMA has identified unsound loan origination and servicing practices, broadly referenced as churning, that has elevated risks to the integrity of the MBS security as investors attempt to account for such prepayment risks. This churning can increase the cost of mortgage credit for borrowers utilizing FHA, USDA, and VA mortgage insurance.

Starting in 2016, GNMA instituted a six-month “seasoning” requirement for VA streamline loans, and then in 2017 the agency extended the requirement to include cash-out refinances. Additionally, in May 2018, federal legislation was enacted that placed additional requirements for VA streamline loans and, in accordance with the law, the VA published a final rule placing certain requirements for cash-out refinances, which have ultimately helped to protect Veteran borrowers as well as restore confidence in the GNMA MBS among the agency’s investor base.

To date, nonetheless, prepayment speeds in the GNMA security continue to remain elevated relative to historic norms and current interest rates. Therefore, GNMA is continuing its efforts to reduce loan churning in all programs.

#### Administrative Reforms:

- GNMA should continue to coordinate with appropriate federal mortgage insurance programs, take action where (and when) necessary to the integrity of the GNMA MBS guaranty, and advance efforts to provide further data transparency to address higher-than-necessary note rate mortgages.
- GNMA should work with other federal parties to implement sound “Net Tangible Benefit” tests by all federal mortgage insurance programs.



## **Conclusion**

FHA and GNMA play a critical role in the nation's housing finance system and any fundamental reforms must account for this. Better coordination among certain institutions – principally FHA, GNMA, and FHFA – is important to ensure that government-supported programs are not crowding out private capital, and instead focus on policies that serve borrowers, including potential first-time and low- and moderate-income homebuyers, that may not have access to appropriate mortgage credit through traditional underwriting without government support.

FHA and GNMA should focus on helping these borrowers become sustainable homeowners while minimizing risk to the taxpayer to the greatest extent possible and providing a path for borrowers to graduate from government-supported programs. For too long FHA and GNMA have operated somewhat isolated from the rest of the housing finance system – often without the proper resources, technology, and authority to fulfill their responsibilities to borrowers, industry partners, and the American taxpayers. The Presidential Memorandum provides an opportunity for this Administration to ensure FHA and GNMA can continue to serve their important missions effectively, responsibly, and sustainably.

**Appendix A**  
**Legislative and Administrative Recommendations**

	<b>Recommendation</b>	<b>Type</b>	<b>Timeline</b>
<b>I. Refocus FHA to its Core Mission</b>			
<i>A. Targeting Programs to Borrowers Not Served by Traditional Underwriting</i>			
1.	FHA should implement a Homebuyer Sustainability Scorecard to measure the performance of loans to low- and moderate-income and FTHBs. The Scorecard will track the percent of mission borrowers who default, return to renting, refinance out of an FHA loan, remain in an original FHA-financed home, and monitor the risk associated with secondary financing (i.e. DPA). FHA should use the Scorecard to evaluate additional underwriting criteria to ensure that new lending within its single-family portfolio is consistent with FHA’s mission.	Administrative	As promptly as practicable
2.	FHA should conduct rulemaking to clarify the statutory prohibition on DPA providers that financially benefit from a transaction.	Administrative	As promptly as practicable
3.	FHA should examine incentives to make shorter-term mortgages that accelerate equity accumulation more attractive to FHA’s mission borrowers.	Administrative	As promptly as practicable
4.	FHA should ensure its programs and policies are consistent with its core mission of serving families who cannot be served by traditional underwriting and that these programs and policies do not incent negative borrower behavior such as equity stripping via cash-out refinancing. FHA should continue to monitor its cash-out refinances closely to determine whether further action is necessary.	Administrative	N/A
5.	FHA should examine the impact of repeat borrowers on the MMIF and ensure these loans are consistent with its mission.	Administrative	As promptly as practicable
6.	Congress should establish statutory limitations on FHA cash-out refinances, or at least ensure alignment (e.g., maximum allowed LTV levels) with such refinance transaction in the conventional market (manages borrower adverse selection across agencies).	Legislative	N/A
7.	Congress should authorize the subordination of any state or local authorized PACE liens that jeopardizes the primary enforcement of FHA’s superior lien for its mortgage insurance on existing loans.	Legislative	N/A

	<b>Recommendation</b>	<b>Type</b>	<b>Timeline</b>
<i>B. Define Roles for Government-Supported Programs Through Better Coordination</i>			
8.	HUD and FHFA should develop and implement a specific understanding as to the appropriate roles and overlap between the GSEs and FHA, for example with respect to the GSEs’ acquisitions of high-LTV and high-DTI loans and FHA’s underwriting of cash-out refinances, conventional-to-FHA refinances, and loans to FHA repeat borrowers.	Administrative	As promptly as practicable
9.	Critically important to these overlaps is care by FHA that its government-subsidized premiums, combined with the advantages of the GNMA full faith and credit MBS guaranty, do not undercut private sector pricing for large segments of mortgage loans that can be well served by private capital.	Administrative	As promptly as practicable
10.	Congress should establish FHA, VA, and USDA – the government-insured mortgage loan programs – as the sole source of low downpayment financing for borrowers not served by the conventional mortgage market.	Legislative	N/A
<i>C. Strengthening FHA Single-Family Default Servicing Processes</i>			
11.	To better protect taxpayers, FHA should enhance its ability to better manage borrower defaults, have more flexibility to work out loans, and make timely changes that will reduce costs to the MMIF during stressed economic environments.	Administrative	As promptly as practicable
12.	FHA should clarify rules around conveyance and enhance consistency on what is considered “conveyance condition” while incentivizing timely conveyance of properties.	Administrative	As promptly as practicable
13.	FHA should enhance its ability to more effectively and efficiently utilize alternatives to conveyance using a “best execution model” that would reduce cost to the MMIF and improve outcomes.	Administrative	As promptly as practicable
14.	FHA should create more flexible loss mitigation processes, allowing for increased take-up in such programs and eliminate unnecessary paperwork and process steps that will streamline borrower qualification in case of hardship.	Administrative	As promptly as practicable
15.	FHA should streamline its default milestone timeline that currently adds to management costs, providing greater flexibility to servicers and more appropriately incentivizing them to work toward more efficient resolutions, with consideration given to market conditions.	Administrative	As promptly as practicable

	<b>Recommendation</b>	<b>Type</b>	<b>Timeline</b>
16.	FHA should reduce uncertainty and business risk of participation in FHA loan programs produced by penalties that do not match the severity of missed deadlines.	Administrative	As promptly as practicable
17.	FHA should establish a paperless data-driven claims process to replace the current inefficient and paper-intensive process. The new claims process will ensure that claims are validated before they are paid in order to better protect taxpayers.	Administrative	As promptly as practicable
18.	The CFPB, FHA, and FHFA should jointly study how to reduce the costs of default mortgage servicing.	Administrative	As promptly as practicable
<i>D. Ensure HUD's Multifamily Programs are Appropriately Targeted</i>			
19.	Similar to the planned collaboration on single-family housing mortgage insurance programs, FHA and GNMA should establish proper coordination and information exchange processes with FHFA to ensure that government-supported multifamily programs do not overlap and compete with private capital.	Administrative	As promptly as practicable
20.	HUD should modify current noise regulations to permit development on property sites with noise levels above 75 decibels, which would likely encourage development in walkable, urban areas (including Opportunity Zones) close to transit and jobs and aligning with FHA's Multifamily Housing goals of more affordable housing.	Administrative	As promptly as practicable
21.	HUD should modify its current environmental review policy to increase the 200-unit threshold to 300 units which would allow for the completion of multifamily projects in more reasonable timelines, aligning with HUD's goals of more affordable rental housing to better meet the demand.	Administrative	As promptly as practicable
22.	Congress should eliminate the 455,000-unit statutory cap in the RAD program, which will expand its reach and impact.	Legislative	N/A
23.	Congress should provide funding for investment in a strategic modernization plan which will holistically overhaul and integrate FHA's Multifamily IT systems. These systems will likely face unsustainable operating and management costs in the near future, and not leveraging the proposed IT road map, and retaining antiquated IT systems, is likely to make new future interconnections across HUD difficult, if not impossible.	Legislative	N/A
<i>E. Provide Regulatory Certainty to FHA Lenders</i>			

	<b>Recommendation</b>	<b>Type</b>	<b>Timeline</b>
24.	FHA should continue to work with the DOJ to provide more clarity on how the agencies will consult on the appropriate use of the FCA.	Administrative	As promptly as practicable
25.	FHA should revise and expand its defect taxonomy in order clearly align the severity of loan underwriting defects with proposed remedies.	Administrative	As promptly as practicable
26.	FHA should continue prioritizing the revision of certifications which lenders attest for each FHA-insured loan as well as lenders' annual certifications. These revisions will provide lenders additional certainty and clarity on FHA's requirements.	Administrative	As promptly as practicable
27.	Congress should make a statutory change to permit shorter suspension periods and eliminate the annual cap on civil money penalties for program participants to provide FHA more flexibility when assessing penalties.	Legislative	N/A
<b>II.</b>			
<b>Protect American Taxpayers</b>			
<i>A. Strengthen FHA Risk Management Systems and Governance</i>			
28.	FHA should adopt a sound risk-based capital regime for the MMIF, well above the statutorily mandated two percent capital ratio, which will manage risk exposure to defined stress scenarios and ensure that FHA does not inappropriately compete with the GSEs or private capital.	Administrative	As promptly as practicable
29.	FHA should adopt a sound risk-based capital standard to manage exposure in the current insured portfolio for the GI/SRI Fund and for future stress cycles and ensure that FHA does not inappropriately compete with the GSEs or private capital mortgage financing.	Administrative	As promptly as practicable
30.	FHA should pursue an inter-agency agreement with other government agencies (including GNMA and FHFA) involved in mortgage insurance and mortgage securitization on counterparty risks.	Administrative	As promptly as practicable
31.	FHA should pursue an inter-agency agreement on credit policy coordination with other government mortgage insurance agencies and FHFA which will help ensure a more efficient targeting and reducing overlap as FHA (and GNMA) achieve the policy goal of assuming primary responsibility for providing housing finance support to low- and moderate-income families that cannot be fulfilled through traditional underwriting.	Administrative	As promptly as practicable

	<b>Recommendation</b>	<b>Type</b>	<b>Timeline</b>
32.	FHA should revise its risk-modeling governance, which will include a decreased reliance on contractors for technical and modeling expertise.	Administrative	As promptly as practicable
33.	Congress should direct HUD to evaluate the options, feasibility, and economics of a CRT program(s) similar to those recently implemented by the GSEs with the purpose of exploring options to reduce the overall risk to taxpayers while still serving HUD’s mission and homeownership objectives.	Legislative	N/A
34.	Congress should direct FHA to more effectively manage lender counterparty risk in future books by authorizing such additional remedies as appropriate.	Legislative	N/A
<i>B. Improve Financial Viability of the Home Equity Conversion Mortgage Program</i>			
35.	FHA should assess and revise its monitoring protocols of front- and back-end appraisal bias.	Administrative	As promptly as practicable
36.	FHA should develop servicing standards for HECM products that will result in reduced operational and financial burdens on servicers and FHA.	Administrative	As promptly as practicable
37.	FHA should eliminate HECM-to-HECM refinancing, as these loan transactions result in greater appraisal inflation, increasing lending against properties that go up in value while being left with existing portfolio exposure on properties that have minimal (even decreasing) change in value. These transactions also negatively impact GNMA-guaranteed HMBS by influencing quick churn in pool participations.	Administrative	As promptly as practicable
38.	Similar to the forward mortgage product, Congress should revise the loan limit structure in the HECM program to reflect variation in local housing markets and regional economies across the United States instead of the current national limit set to the level of high-cost markets in the forward program. Currently, the HECM program utilizes one nationwide loan limit of \$726,525 (for 2019).	Legislative	N/A
39.	Congress should set a separate HECM capital reserve ratio and remove HECMs as obligations to the MMIF. This would provide for more transparent accounting of program costs and decrease cross-subsidization that occurs with mission borrowers in the forward mortgage portfolio.	Legislative	N/A
<i>C. Implement Tiered Pricing to Protect the MMIF</i>			

	<b>Recommendation</b>	<b>Type</b>	<b>Timeline</b>
40.	FHA should develop and implement a tiered pricing system in order to protect the MMIF and ensure it is pricing appropriately for higher-risk loans.	Administrative	As promptly as practicable
<i>D. Eliminating Regulatory Barriers to Affordable Housing Including Manufactured Housing</i>			
41.	Pursuant to the Executive Order of June 25, 2019, the HUD-led White House Council on Eliminating Regulatory Barriers to Affordable Housing will identify and recommend actions and policies to mitigate regulations that unnecessarily increase the cost of creating and preserving housing that is affordable and work with state, local, and tribal partners to do the same.	Administrative	As promptly as practicable
42.	To encourage innovation, in manufactured housing, HUD should create a formal framework for identifying and evaluating new building, construction, and design developments and ensuring that HUD's regulations do not unnecessarily impede their adoption. This framework would help gather the evidence necessary to update HUD's regulations on a regular cadence, thereby better keeping up with evolving technology.	Administrative	As promptly as practicable
43.	FHA should consider innovative proposals to modify single-family housing mortgage finance underwriting to further encourage and promote additional supply of entry-level housing, particularly manufactured housing.	Administrative	As promptly as practicable
44.	HUD should devote resources to ensure the HUD-Code is modernized to incorporate the standards recommended by the MHCC, to minimize overly burdensome regulatory and compliance requirements, and to encourage innovation. Once revised, HUD should also move to a regular cadence of updating its code to ensure that it is keeping pace with evolving technologies and best practices.	Administrative	As promptly as practicable
45.	HUD should publish updated Title I standards that address regulatory burdens of participating in the program as part of its Single Family Housing Policy Handbook 4000.1 (SF Handbook), which is intended to serve as the consolidated, consistent, and comprehensive source of FHA Single Family Housing policy.	Administrative	As promptly as practicable
46.	HUD should elevate the Office of Manufactured and Innovative Housing Programs within HUD and appoint a Deputy Assistant Secretary to lead it.	Administrative	As promptly as practicable

	<b>Recommendation</b>	<b>Type</b>	<b>Timeline</b>
<b>III. Provide FHA and GNMA the Tools to Appropriately Manage Risk</b>			
<i>A. Establish FHA as an Autonomous Corporation within HUD</i>			
47.	Congress should enact legislation to restructure FHA as an autonomous government corporation within HUD.	Legislative	N/A
<i>B. Hire and Retain the Right Talent to Mitigate Risks to Taxpayers</i>			
48.	Like GNMA, FHA should explore the targeted use of pay flexibilities available under current law (e.g., Critical Pay) to improve hiring and retention of key positions requiring specialized technical skills related to the mortgage and securitization markets.	Administrative	As promptly as practicable
<i>C. Align Contracting and Procurement Processes with Business Needs</i>			
49.	To the extent administrative reforms are insufficient to address procurement challenges at FHA and GNMA, Congress should propose new statutory acquisition authorities for HUD, particularly to address instances where material underperformance of contracting vendors results in substantial quality deficiencies and costs.	Legislative	N/A
<i>D. Modernize FHA Technology</i>			
50.	FHA should explore agreements to share technology with GNMA and other government-supported mortgage programs when feasible.	Administrative	As promptly as practicable
51.	FHA should develop a mortgage origination risk tool integrating an automated underwriting system (AUS) platform, appraisal scorecard, risk assessment tool and third-party verification services.	Administrative	As promptly as practicable
52.	Congress should appropriate sufficient funds for FHA to complete its multi-year single-family IT modernization effort.	Legislative	N/A
<i>E. Realign Housing Assistance Programs into a New Office of Rental Subsidy and Asset Oversight within HUD</i>			
53.	Absent legislation, the Department should pursue a reorganization that separates its mortgage insurance and rental assistance programs into separate offices.	Administrative	As promptly as practicable



	<b>Recommendation</b>	<b>Type</b>	<b>Timeline</b>
54.	Congress should enact legislation to separate the position and responsibilities of the Federal Housing Commissioner from the position and responsibilities of the Assistant Secretary for Housing.	Legislative	N/A
55.	Congress should enact legislation to create a new Office of Rental Subsidy and Asset Oversight overseen by the Assistant Secretary for Housing which would consolidate multifamily housing subsidy programs, Public Housing and Housing Choice Voucher programs, together with RAD and REAC.	Legislative	N/A
56.	As part of this reorganization, Congress should establish the Office of Native American Programs as a separate office, led by a Presidentially-appointed, Senate-confirmed Assistant Secretary and separate the Native American programs from the other programs within HUD's Office of Public and Indian Housing.	Legislative	N/A
<b>IV. Provide Liquidity to the Housing Finance System</b>			
<i>A. Advance GNMA Counterparty Risk Management and Securitization Platform Transformation</i>			
57.	GNMA should transition the MBS platform from pool-level to loan-level functionality, including the ability to transfer servicing of individual loans within a pool. This reform will enhance the desirability and value of the MSR asset and reduce the cost of loans insured or guaranteed by Federal agencies relative to conventional loans.	Administrative	As promptly as practicable
58.	GNMA should continue to facilitate adequate liquidity in the housing finance system, including the implementation of reforms for the financing of and investment in MSRs, and oversight of the development of industry-level liquidity management methods, as outlined in the GNMA 2020 reform agenda.	Administrative	As promptly as practicable
59.	GNMA should continue to maximize the value of its servicing portfolios, such as through establishing servicing fee standards and enhanced monitoring of servicing transfers to ensure that both parties maintain adequate MSR values.	Administrative	As promptly as practicable
60.	GNMA should enhance issuer standards through strengthened risk management requirements, including updated liquidity, leverage, and capital standards, with particular focus on very large issuers and sub-servicers.	Administrative	As promptly as practicable

	<b>Recommendation</b>	<b>Type</b>	<b>Timeline</b>
61.	GNMA should strengthen its risk management analytics and predictive capabilities to mitigate risks, given the growing share of the agency’s portfolio comprised of very large, non-bank counterparties. This should include GNMA’s ongoing development of stress test modeling capability and the imposition of a stress testing regimen for non-bank institutions to evaluate performance under a range of economic scenarios.	Administrative	As promptly as practicable
62.	GNMA should implement enforcement, recovery and resolution reforms to protect taxpayers, which should include building the capability for the agency to move quickly, effectively and fairly to sanction firms who are failing to abide by program terms, and to address issuers who are vulnerable to failure, or otherwise threatens the sound administration of the MBS program.	Administrative	As promptly as practicable
63.	GNMA should fully modernize platform access, data standards, collection, and storage, which will transform the user interaction with the securitization and data analytical architecture into a highly secure, single gateway. This reform will increase GNMA’s ability to monitor its issuers, enforce its rules and requirements, and manage the overall safety and soundness of the program, as well as efficacy and validity of data collected and reported through the Mortgage Banker’s Financial Reporting Form.	Administrative	As promptly as practicable
64.	GNMA should develop and implement the policies, technology and operational capabilities necessary to accept digital promissory notes (eNotes) and other digitized loan files as acceptable collateral for its securities, which will enable issuers to enhance efficiency, risk management and customer experience by moving to digital collateral and a fully electronic “eClosing” process.	Administrative	As promptly as practicable
<i>B. Guaranty Fee-setting Flexibility</i>			
65.	Congress should pass legislation granting GNMA the authority to administratively adjust its guaranty fee within a narrow, permissible range.	Legislative	N/A

	<b>Recommendation</b>	<b>Type</b>	<b>Timeline</b>
<i>C. Reforms to Maintain the Integrity of GNMA Securities</i>			
66.	GNMA should continue to coordinate with appropriate federal mortgage insurance programs, take action where (and when) necessary to the integrity of the GNMA MBS guaranty, and advance efforts to provide further data transparency to address higher-than-necessary note rate mortgages.	Administrative	As promptly as practicable
67.	GNMA should work with other federal parties to implement sound “Net Tangible Benefit” tests by all federal mortgage insurance programs.	Administrative	As promptly as practicable