From: Patrick Bates

Subject: Credit Risk Retention - Reg RR

Comments:

Docket No. R-1411

Regulatory Agencies Request Comment on Risk Retention Proposal
On March 31, The U.S. Department of Housing and Urban Development (HUD) along with the four bank regulators, the Securities and Exchange Commission and the Federal Housing Finance Agency released their risk retention proposal as required by the Dodd-Frank Reform Act. This proposal details the requirement that sponsors of asset-backed securities (ABS) retain at least five percent of the credit risk of the assets.

The proposal also defines qualified residential mortgages (QRM), which are loans that are exempt from the risk retention requirement, on the logic that they are very low risk. The underwriting standards for QRMs laid out in this proposal include 20% down payment, a maximum loan-to-value ratio of 80%, and borrower credit history restrictions including no 60-day delinquencies on any debt obligation within the previous 24 months. The proposal also request comments on an alternative approach that applies less conservative standards to QRMs including lower down payments.

The QRM and risk retention rules are the first major rule making efforts in what will be an extended reform of mortgage finance. Beyond their specific policy impact, they also begin to create momentum around the broader approach to mortgage finance.

Please consider my comments and respond when your schedule allows:

High down payment requirements do not necessarily correlate well with safe loans, but do prevent low- and moderate-income people from becoming homeowners. Quantity does NOT equal quality. Please explain how high down payment requirements do not necessarily correlate well with safe loans? The implication is that buyers who are able to submit high down payments are less financially stable or intend to over-leverage their finances. Please explain the logic behind this. More specifically, what percentage of high down payment loans ended up in default compared to loans with no or very small down payment, during the housing crisis? Further, has it occurred to Dodd, Frank, or anyone else that some people, like those who can't afford a down payment, shouldn't own real estate and have a mortgage? This legislation seems like nothing more than a different starting point to a new housing recession: QRM and Risk Retention Group federal law will abrogate all state law, force increased quantity of mortgage loans (while not caring about the quality of those loans or borrowers), those mortgage companies will write off their losses and, if necessary, get bailed out by politicians whose re-election campaigns they contributed the most to. Yes, this is a big problem.
Risk retention creates an economic incentive for originators and securitizers to maintain loan quality, but it may also affect the competitive landscape, because entities with larger balance sheets (such as major banks) will be better able to manage retained risk. Risk retention negatively affects the competitive landscape because entities with larger balance sheets (such as major banks who can contribute a lot more to re-election campaigns) will be

better able to manage retained risk. It is not a matter or "may."
Specifically, what in the legislation will help smaller banks compete with this federal encroachment on state's rights?
Defining safe mortgages may unintentionally limit the availability of mortgage credit. The stated intention of the QRM is to define a small subset of securitized mortgages, with securitization also occurring in the non-QRM space. However, there is a risk that QRM becomes a limit, rather a special category. Again, unintentionally limiting the availability of mortgage credit by defining safe mortgages is a good thing. Limiting the amount of credit extended to people who shouldn't have a mortgage is a good thing. Increasing FHA, HUD, FHFA, and other government entities role in the housing finance system is something the country is trying to lessen, not expand.

"Many factors contributed to the Great Recession of 2008, but its root cause was simple: In a two-decade-long bipartisan campaign to expand homeownership, especially among minority and lower-income communities, federal authorities cajoled, threatened and ultimately mandated that mortgage institutions put aside traditional, common-sense lending standards. A real estate bubble predictably followed as adjustable-rate mortgages, subprime loans requiring little or no down payment, and other lend-at-all-costs incentives combined with corporate greed to encourage an irrational exuberance about the value of real estate. Americans borrowed trillions of dollars to buy millions of homes at unjustifiably high prices, using the overvalued homes themselves as collateral, even as commercial banks packaged millions of these shaky mortgages into securities for investors looking for quick, easy profits. And standing behind it all stood government-backed Fannie Mae and Freddie Mac, implicitly guaranteeing everybody that nobody would lose their shirts.

The whole house of cards collapsed when people couldn't afford their mortgage payments. A flood of foreclosures followed, rendering all those subprime mortgage-backed securities worthless, causing panic on Wall Street and plunging the nation into a recession. Fannie and Freddie, having lost hundreds of billions of dollars to the folly of propping up the subprime mortgage market, are now under government conservatorship and bound by new, stringent lending standards. But one badly burned hand of government seems unaware that the other is thrusting itself right back into the fire. In a recent article for the American, housing expert Peter Wallison points out that the Federal Housing Administration is picking up where Fannie and Freddie left off by pursuing many of the same practices that led to the 2008 crisis.

The agency, which insures home loans with low or zero-down payments, is specifically exempted from the lending standards of the Dodd-Frank financial reform bill. By law, its programs are available to those with a credit score of at least 580, the bare minimum required to qualify for a mortgage. (A perfect credit score is 800 to 850, depending upon the rating agency). But FHA-participating institutions seeking to set the bar above 580 are being sued by radical community organizers. Incredibly, FHA plans to expand its portfolio, according to Wallison, to take on $1.34 trillion in additional mortgage debt by 2013.

Rather than subsidize the re-creation of the same dangerous culture of easy mortgages that got us into this mess, Congress should remedy the deficiency in

Dodd-Frank by mandating stronger lending standards for FHA-insured loans and then backing up lenders who apply them. Wallison is worth listening to because in 1999 he predicted disaster when Fannie Mae first began underwriting subprime loans. He told the New York Times: "If they fail, the government will have to step up and bail them out the way it stepped up and bailed out the thrift industry." Wallison has since been proven right in every aspect. If Congress fails to heed the warning this time, another great recession or worse will surely follow."[1]

Most Sincerely,

Patrick Bates