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July 28, 2011

Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

Alfred M. Pollard
General Counsel
Federal Housing Finance Agency
Fourth Floor, 1700 G Street, NW
Washington, DC 20552.

RE: Credit Risk Retention: Docket No. R-1411 (Federal Reserve Board); RIN 2590-AA43 (Federal Housing Finance Agency)

Dear Ms. Johnson and Mr. Pollard:

On behalf of the National Association of Federal Credit Unions (NAFCU), the only trade association that exclusively represents the nation's federal credit unions, I am writing to provide NAFCU's comments on the proposed rule regarding qualified residential mortgages (QRMs). The proposal does not directly impact credit unions. However, as participants in the mortgage market, credit unions will obviously feel the effects of the final rule as it will have a significant impact on the entire mortgage lending market. The agencies are being asked to strike a delicate balance: On the one hand, the rule must ensure lenders and borrowers have a meaningful economic interest in the loans being underwritten; on the other hand, the rule should not place homeownership beyond the reach of middle- and low-income Americans. NAFCU strongly objects to the 20 percent down payment requirement as proposed.

The proposed rule would generally require lenders to retain at least five percent of the risk for home mortgages underwritten by the lender. The proposed rule would eliminate this requirement for mortgages that meet certain underwriting standards and that thus qualify as QRMs. Among other things, the QRM exception requires a down payment of 20 percent. While credit unions are exempt from the rule, we share the same concerns with other interested parties regarding the impact of the QRM rule. First, the rule will inevitably decrease the availability of mortgage financing for moderate- and low-income borrowers. Second, the QRM rule could have serious repercussions for the secondary mortgage market, which would, in turn, dramatically impact small and moderate sized mortgage lenders.

The proposed 20 percent down payment requirements will negatively impact many borrowers while providing little – if any – benefit to any other participant in the mortgage market. First, requiring a 20 percent down payment will necessarily limit the pool of borrowers eligible for a QRM, and dramatically decrease the number of low- and middle-income Americans who can realize the benefits homeownership. According to the National Association of Realtors' (NAR), a family making the median average income would need to save for sixteen years in order to put a 20 percent down payment on a home (based on the average annual median sale price of $172,900 for 2010). Furthermore, economic realities dictate that lenders must charge more for loans that do not qualify as QRMs as they cannot be as easily securitized. The most likely end result is that the down payment requirement will decrease the availability of mortgage financing overall and increase the cost of credit for all borrowers. At the same time, there is evidence to suggest a 20 percent down payment has only a marginal impact on limiting foreclosures. Certainly the down payment is one of several important underwriting factors. However, the down payment is not the only important factor, and other elements, such as debt-to-income ratio (DTI) and creditworthiness are likely better indicators of the likelihood of default. It is with this in mind that NAFCU recommends modifying the 20 percent down payment proposal.

The agencies should permit loans with a lower down payment to qualify provided other underwriting parameters are met. First, NAFCU would suggest the agencies simply decrease the down payment requirement. Alternatively, the agencies could enhance the QRM requirements by decreasing the down payment when other factors such as the DTI or the borrower's creditworthiness sufficiently mitigate credit risk. Regardless of which path the agencies choose, it is imperative that the down payment requirement be re-examined. A 20 percent down payment requirement will reduce the pool of eligible borrowers, drive up prices for borrowers who remain eligible and, at the same time delay a much needed recovery in the housing market.

NAFCU is also concerned with the consequences the rule will have on the secondary mortgage market. Credit unions sell the vast majority of their home mortgages on the secondary market. NAFCU appreciates the exemption included for loans held by the government sponsored enterprises (GSEs). Nonetheless, there is obviously uncertainty regarding the long-term structure and viability of the GSEs. Without a robust secondary market, credit union mortgage lending will by necessity grind to a halt. Obviously, there is a possibility that the QRM will become the industry standard for loans that are to be sold on the secondary market. This is even more likely to be true for smaller institutions that will not possess the bargaining power derived from a large volume of ineligible mortgage originations. Credit unions simply could not continue as a reliable source of mortgage funds if their only two alternatives are to either require a 20 percent down payment or to hold all mortgage originations on the balance sheet. Certainly, credit unions could retain some mortgages, but given the capital constraints inherent to the credit union charter, holding mortgage loans in portfolio would unacceptably deplete net worth ratios.

In conclusion, NAFCU does not support the 20 percent down payment requirement. The provision would make it near impossible for millions of Americans to purchase a home. Millions more would still be eligible for a mortgage, but at a much higher price. At the same time, it is less than certain that substantial down payments do much to limit foreclosures. The broad repercussions in the secondary mortgage market should be examined more closely, especially in the context of the impact on the overall availability of credit. As proposed, this rule will only hamper an already slow recovery in the housing market, and the overall economy, while providing little in the way of tangible benefits.

NAFCU understands that irresponsible underwriting was one of several contributing factors to the recent economic turmoil. Further, we agree that the down payment is one of several important factors to consider when underwriting a mortgage loan. Nonetheless, the proposed down payment requirement is simply too large. The agencies should reconsider the QRM requirements, and provide for flexibility in the down payment amount when other important underwriting criteria are present to mitigate credit risk. NAFCU appreciates the opportunity to comment on the proposed rule. Should you have any questions or require additional information please call me at (703) 842-2212.

Sincerely,

Dillon Shea
Associate Director of Regulatory Affairs