NATIONAL ASSOCIATION OF REALTORS®

January 16, 2024

The Honorable Martin Gruenberg
Chair
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, D.C. 20429

The Honorable Michael Hsu
Acting Comptroller
Office of the Comptroller of the Currency
400 7th Street SW
Washington, D.C. 20219

The Honorable Jerome H. Powell
Chair
Board of Governors of the Federal Reserve System
20th Street and Constitution Ave. NW
Washington, D.C. 20551

Re: Notice of Proposed Rulemaking for Amendments to the Regulatory Capital Rule (Docket ID OCC–2023–0008, Docket No. R-1813)

Dear Chair Gruenberg, Acting Comptroller Hsu, and Chair Powell:

On behalf of the more than 1.5 million members of the National Association of REALTORS® (NAR), I would like to thank the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve, and the Federal Deposit Insurance Corporation (collectively, "the Agencies") for this opportunity to comment on proposed amendments to the bank capital standards, also known as the Basel III *Endgame* rulemaking (the "proposal").

As America's largest trade association, with a member base composed of residential and commercial brokers, salespeople, property managers, appraisers, counselors, and others engaged in the real estate industry, NAR knows the importance of having a strong, well-regulated, and well-capitalized banking system and a safe and secure housing and mortgage market.

Introduction

As the Agencies explore finalization of these new Basel Accords, NAR has strong concerns about the current proposal, especially as it relates to the risk-weighting of mortgages and the inevitable downstream effects to all borrowers, but especially first-time, minority borrowers, and low- and moderate-income borrowers.

The proposal makes drastic and sweeping changes to the capital requirements for single-family residential mortgages held in bank portfolios and especially impacts loans with high loan-to-value (LTV) ratios, loans made primarily to low- and moderate-income (LMI) borrowers and first-time buyers, many of those who are borrowers of color. In addition, the proposal alters the treatment of mortgage servicing rights (MSRs) and the cost of warehouse funding, which will affect a broader group of homebuyers.

The current approach from the Agencies to require increased capital for the largest banking participants may appear to only impact America's largest financial institutions. However, given the interconnectedness of the banking system, many community and local institutions, who rely on the largest participants for credit access, will suffer from a further restriction of credit in an already difficult time. Additionally, many communities will likely feel the impact of a drawback or elimination of programs that have been developed to help the same area where banks serve, such as the promotion[1] and rise of Special Purpose Credit Programs (SPCPs) and the recent revisions to the Community Reinvestment Act (CRA). The current proposal will only encourage a further drawback from the mortgage market by the largest banks but also smaller and mid-sized institutions as their cost of warehouse funding increases and the viability and profitability of MSRs decreases.

Without meaningful changes to the current proposal, NAR fears that consumers will face increased borrowing costs and a severe reduction in credit. The effects of this proposal will strike many potential borrowers, especially those in high-cost areas, but will hit underserved markets and those borrowers with low and moderate incomes the hardest, those whom the American Dream has already started to become nothing more than a hopeful wish.

NAR supports a housing finance system that is strong, resilient, well capitalized, well regulated, and offers broad access to qualified borrowers. We believe that the current proposal falls short in ensuring these goals and will add unnecessary pressure and cost onto a market that is already straining under the weight of historic underinvestment, high interest rates, and a lack of housing, especially affordable housing.

A New Housing Finance Ecosystem

Housing remains a significant portion of the country's gross domestic product and owning a home remains one of the most important steps to unlocking financial security. Following the passage of the Dodd-Frank Act, many new regulations were introduced to eliminate the risk factors that lead to the financial crisis in 2007 and 2008. Mortgage markets became highly regulated and were brought under additional oversight from the Consumer Financial Protection Bureau. Bank capital standards were also increased and overseen by a handful of regulators, including the finalization of the original Basel III Accords in 2013 and resolution planning requirements, to ensure that the institutions had the necessary cash on hand to weather storms, and if not, had clear resolution plans to unwind operations in a manner that would not create a shock to the financial markets and the overall economy.

Since then, financial markets have been strong and resilient. For years, regulators and lawmakers have pointed to the current financial system as one of the strongest and safest in the world[2]. This past spring saw a true test of this theory after the failure of three high-profile

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[1] Interagency Statement on Special Purpose Credit Programs Under the Equal Credit Opportunity Act and Regulation B." Federal Deposit Insurance Corporation, Financial Institution Letter, February 22, 2022. https://www.fdic.gov/news/financial-institution-letters/2022/fil22008.html

[2] "2023 Federal Reserve Stress Test Results." Board of Governors of the Federal Reserve System, June 2023. https://www.federalreserve.gov/publications/files/2023-dfast-results-20230628.pdf

regional banks: Silicon Valley Bank, Signature Bank, and First Republic Bank. Policymakers, economists, financial institutions, and consumers across the country followed the events closely for signs of systemic risk and the potential for downstream effects that could reveal further weakness in other financial institutions, both large and small, potentially leading to another economic downfall.

Despite these concerns, the financial system weathered the storm. In April, the Board of Governors of the Federal Reserve released a study investigating the cause of Silicon Valley Bank's failure and concluded that the bank failed primarily due to company mismanagement, a run spawned via social media, and failed regulatory oversight. One thing not mentioned within the accounting of the bank failure: risk connected to mortgage underwriting.[3]

The catastrophic financial collapse in 2008 is nothing to take lightly. Multiple factors led to the largest economic crisis the economy has seen since the Great Depression. Undercapitalized banking institutions played a significant part, as well as a lack of regulation. Since then, banks have been required to increase their level of capital and numerous additional checks have been added to the financial system, including the Basel III rules that brought America's institutions in line with those globally.[4] Risky consumers and mortgage products helped precipitate the financial crisis, but subsequent regulations have ameliorated both including the Ability to Repay rule and the TILA-RESPA Integrated Disclosures. With these changes, however, mortgage loans have increased in cost for both lenders and consumers.[5]

A Tough Market

For many Americans, the dream of homeownership is becoming just that—something that will only ever exist in dreams. High interest rates, especially compared to just two years ago, and a lack of housing stock have created a perfect storm of housing unaffordability. NAR has long advocated for removing barriers that are leading to higher costs in housing, including building more housing (especially affordable housing) removing unnecessary fees for mortgage programs (such as premiums at FHA and guarantee fees mandated by FHFA), and providing tax incentives to spur construction and encourage current owners to sell to other owner-occupants.

The U.S. faces a shortfall of over 5.5 million homes.[6] Given the current economic climate and the attempts by the Federal Reserve to reduce inflation by raising the federal funds rate,

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[3] "Review of the Federal Reserve's Supervision and Regulation of Silicon Valley Bank." Board of Governors of the Federal Reserve System, April 28, 2023. https://www.federalreserve.gov/publications/files/svb-review-20230428.pdf

[4] "Federal Reserve Board Approves Final Rule to Help Ensure Banks Maintain Strong Capital Positions." Board of Governors of the Federal Reserve System, July 2, 2023. https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130702a.htm

[5] "Cost to Originate Study: How Digital Offerings Impact Loan Production Costs." Freddie Mac, Single-Family, November 2021. https://sf.freddiemac.com/docs/pdf/report/cost-to-originate.pdf

[6] "Housing is Critical Infrastructure: Social and Economic Benefits of Building More Housing." Rosen Consulting Group, June 2021. https://cdn.nar.realtor//sites/default/files/documents/Housing-is-Critical-Infrastructure-Social-

consumers have faced skyrocketing interest rates around seven percent. These two factors, in addition to rising insurance rates across the country and especially in high-risk climate areas, mean that housing is often unattainable, unaffordable, and out of reach for many, especially lower-income and first-time buyers.

Evaluating the Proposal

As we evaluate changes to the financial, housing, and mortgage markets, we must take into account the current climate and landscape of the potential American homeowner. Regulators and Congress must evaluate all solutions to lower the costs of housing and remove barriers to homeownership. However, the current *Endgame* proposal from the Agencies will add another massive hurdle for consumers look for mortgage loan products. The specific changes to the risk-weighting for mortgages and servicing rights and the overall increase in capital across the board for the large banking institutions will inevitably mean that the cost of mortgages will increase, especially for lower-income consumers, those already struggling the most to obtain housing. Worse, the Agencies do not provide evidence of the risks to justify the enhanced proposal.

Traditionally, bank portfolio loans have filled the void for consumers who often don't fit into traditional credit boxes. This is particularly true concerning mortgages for borrowers who do not fit into the GSE, FHA, or VA credit boxes. The proposal significantly changes the amount of capital that needs to be held to support higher-LTV loans. According to the Urban Institute, the proposal adds 20 percent points across the board to the existing Basel III standards for all LTV categories, and especially impacts owner-occupied properties with higher-LTVs, presenting a 40% increase of reserved capital for loans with LTVs from 90-100 percent.[7] As for the true borrower impact, the Urban Institute estimates that for loans with LTV ratios from 80 to 90 percent, a borrower would need to pay around 12.5 basis points more per year for their mortgage, and for those with LTVs from 90 to 100 percent, the borrower would pay around 25 basis points more, equating to an extra $33 a month in payments for a $200,000 mortgage.

While these numbers may not sound like a lot to some, the on-the-ground impact is much more visible. High-LTV mortgages are most important to LMI borrowers. The Urban Institute notes that 28 percent of high-LTV borrowers were LMI borrowers, accounting for 67,000 bank loans each year. Additionally, 23 percent of high-LTV borrowers are considered middle-income, receiving 55,000 loans. Many of these loans are encouraged due to the CRA, further helping communities that banks serve, and the research shows that more than 21,000 loans per year were made to Black borrowers and a further 31,000 to Hispanic borrowers.[8] Additionally, borrowers within high-cost areas will bare the brunt of the changes even harder.

and-Economic-Benefits-of-Building-More-Housing-6-15-2021.pdf?_gl=1*1yxqjjy*_gcl_au*NzA5ODQyOTg3LjE2OTcwNDg5MjY.

[7] "Bank Capital Notice of Proposed Rulemaking: A Look at the Provisions Affecting Mortgage Loans in Bank Portfolios." Laurie Goodman and Jun Zhu, the Urban Institute, September 2023. https://www.urban.org/sites/default/files/2023-09/Bank%20Capital%20Notice%20of%20Proposed%20Rulemaking.pdf

[8] *Id.*

Furthermore, one missing consideration from the LTV risk-weight changes is the existence of private mortgage insurance (PMI). PMI acts as an efficient insulation against losses, for both the loan originator and the Government Sponsored Enterprises (GSEs), which have done extensive work to shore up the capital requirements and business practices of their PMI counterparties. It also allows consumers to qualify for loans with low down payments. Without the acknowledgement of the role of PMI and its potential to avoid losses, banks are further incentivized to avoid providing high-LTV loans, often to the market segments that need it most. Likewise, Credit Risk Transfer in both its reinsurance and structured forms have played a key role in supporting the GSEs' ability to reduce their risk, while supporting homeownership. These programs are widely touted as a success and supported by Congress.

REALTORS® believe these proposed changes run astray from the goals of President Biden to bring affordability and equity to the housing markets and exist in a vacuum, not taking into account the current strength of the banking system, the protections put into place in the Dodd-Frank Act and post-financial crisis, nor mortgage insurance. The proposed changes will inevitably affect the decision making of banks, including which products and services they choose to support and those they choose to shy away from or eliminate completely. Already, we are seeing a retreat from mortgage lending in 2023, especially compared to the recent activity of the last five years.[9] Further impediments will only encourage additional draw-back and more consolidation, harming consumer choice and driving up costs.

The effects will not solely be experienced by America's largest banks—there are significant downstream effects that will impact independent mortgage banks (IMBs) of all sizes. Two unintended consequences of the proposal will be a reduction in warehouse lines of credit to small- and medium-sized institutions, those who often serve rural and underserved communities, and a reduction in mortgage servicing rights (MSR) financing.

Regarding warehouse lines, the risk weighting does not correlate with the actual risk of the loans being offered by IMBs.[10] The higher capital requirements for large banks will inevitably raise the cost of borrowing for smaller entities or eliminate their source of funding altogether, leading to further consolidation in a market where IMBs are hemorrhaging money on the loans they make.[11] What is more, encouraging the elimination of more competition will inevitably lead to higher costs for borrowers.

As for MSRs, banks already face a particularly high risk-weighting. The proposal reinstitutes a 10 percent cap on MSRs. This lower cap can lead to a host of problems, including a further retreat from banks in originating loans and holding the servicing rights, lower MSR values across the board, and raising interest rates even further as the appetite for servicing is reduced and the MSR value drops. IMBs will also be expected to further absorb the changes, and while this has proven reliable in the short-term post-financial crisis, regulators have

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[9] "Mortgage Originations Continue to Contract, Analysts Say." National Mortgage Professional, July 27, 2023. https://nationalmortgageprofessional.com/news/mortgage-originations-continue-contract-analysts-say

[10] "Testimony of the Mortgage Bankers Association Before the House Financial Services Subcommittee on Financial Institutions and Monetary Policy -- Implementing Basel III: What's the Fed's Endgame?" September 14, 2023. https://docs.house.gov/meetings/BA/BA20/20230914/116339/HHRG-118-BA20-Wstate-BroeksmitR-20230914.pdf

[11] "Independent Mortgage Banks Reported Nearly $3k Loss on New Originations." MReport, March 17, 2023. https://themreport.com/news/data/03-17-2023/independent-mortgage-banks

continued to voice concern about the systemic risk and potential undercapitalization of some large nonbank servicing entities.[12] Pushing the economics of mortgage servicing further away from depositories only heightens risk to the system.

As mentioned earlier, the housing market faces a deficit of more than 5.5 million homes. We are pleased that the risk-weighting has not been changed for multifamily mortgages. However, the additional impediments for owner-occupied mortgages will likely lower interest in construction for owner-occupied housing. Reducing certainty and increasing borrowing costs across the board, thus pushing even more Americans from the chance of owning a home, will discourage investment and production in new and rehabbed housing at precisely the wrong time.

The impact will also be felt by communities that the Agencies have recently taken actions on. SPCPs are a novel way for lenders and community partners to increase credit access for historically disadvantaged communities. Many large institutions have offered programs similar to SPCPs, and the recent announcement by the joint agencies further encouraged and gave legal certainty for others to create and execute new programs. Market dynamics, such as high interest rates and the lack of affordable housing, has meant that SPCPs have only recently started to smolder. The proposal would require banks to retain additional capital against such loans, raising their cost and undermining the very intent of the program. Unfortunately, the current proposal adds yet another barrier to the process of creating vibrant and successful SPCPs.

Additionally, it remains unclear how the proposal will interact with the recently finalized CRA rule.[13] The CRA was enacted more than 50 years ago to encourage banks to meet the credit needs of the communities in which they serve, especially in low- and moderate-income neighborhoods. Incentives have been given to banking institutions to extend credit and provide opportunities in a safe and regulated manner, often to communities who have been underserved. Unfortunately, the recent proposal from the Agencies acts as a deterrent from offering services, especially mortgages, to the communities that CRA was specifically designed to help. The beneficial updates to CRA, expansion of included activities, and additional tracking of results and impact could be entirely forgotten in favor of banks holding extra, unnecessary capital.

NAR finds it prudent that the Agencies keep the agreed upon Basel III standards and avoid adding additional capital requirements at a particularly challenging time for the U.S. housing market and economy. We believe a reconsideration of the proposals is necessary unless the Agencies offer strong, supporting evidence that the additional capital is required to protect consumers and the economy. REALTORS® do not see the necessity of the current proposal, and the repercussions as a result will only make housing a goal that is simply unattainable for anyone but the wealthiest Americans, many of whom have reaped the results of generations of an unequitable housing system that still reverberates through minority and low-income communities today.

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[12] "Remarks by FDIC Chairman Martin J. Gruenberg at the Exchequer Club on the Financial Stability Risks of Nonbank Financial Institutions." September 20, 2023. https://www.fdic.gov/news/speeches/2023/spsept2023.html

[13] "Agencies Issue Final Rule to Strengthen and Modernize Community Reinvestment Act Regulations." Joint Agencies, October 24, 2023. https://www.federalreserve.gov/newsevents/pressreleases/bcreg20231024a.htm

Conclusion

We thank the Agencies for the opportunity to comment on this major proposal. It's important to remember all that is at stake here. Raising costs and interest rates on borrowers during a very difficult housing market serves no one. The proposed changes will unfairly impact all borrowers but will especially be costly for those who least are able to absorb the higher costs and higher fees associated with a future home loan. Many of the proposed changes undercut other important efforts from the housing finance agencies and the Administration to close the wealth gap and promote an affordable and equitable housing finance system.

In addition, there are real risks to the housing market and the economy by increasing the capital standards without a strong justification. The housing economy and underwriting standards remain exceptionally strong, and other surrounding weaknesses in the financial markets have not trickled down to mortgages or mortgage-backed securities. That does not mean that lending has become easier, which we are seeing borne out by higher costs to originate and the consolidation and closure of lenders. The proposal unfortunately does not do anything to encourage large banks to re-enter the mortgage market and instead will unfairly put a squeeze on the IMBs that have helped fill the hole left by the largest players in the wake of the financial crisis.

REALTORS® support a strong and resilient mortgage market that offers opportunities to qualified individuals and allows competition and profitability for mortgage providers. Unfortunately, NAR feels that this proposal has missed the mark. We stand ready to work with the Agencies to improve the proposals so that the communities that our members serve have opportunities to achieve the American Dream. Should you have any questions or comments, please feel free to reach out to Matthew Emery, Senior Policy Representative, at memery@nar.realtor.

Sincerely,

Kevin M Sears

Kevin Sears
2024-2025 President, National Association of REALTORS®