



Reforming the housing finance market

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AS YOU KNOW, THE U.S. TREASURY HAS SUBMITTED A PLAN to Congress to reform our country's housing finance market. Treasury Secretary Tim Geithner has asserted that the government's role in housing should be limited to consumer protection, targeted assistance for low- and moderate-income borrowers and renters, and a targeted capacity to support market stability.

What does this mean for the credit union industry? In the short term, we will most likely see: the shrinking of conforming loan limits due to expire Oct. 1, 2011; a gradual increasing of guarantee pricing at Fannie Mae and Freddie Mac (toward the same capital standards as private institutions); an increase in the amount of private capital that risks loss ahead of taxpayers' funds through credit loss protections from private entities; and a gradual increase in down payment requirements.

The Treasury's plan

In the long term, the Treasury's plan lays out three potential ways to structure government support for reform. In each option, government support would be transparent, explicit and limited. Private markets would be the primary source of mortgage credit and the primary bearer of mortgage losses. FHA assistance and similar government initiatives that assist targeted groups, such as low and moderate income families, farmers and veterans, would be preserved. Following is a closer look at each option.

Option 1: The government's role would be limited almost exclusively to FHA assistance and similar targeted initiatives. The overwhelming majority of mortgages would be financed by lenders and investors, and they would not benefit from a government guarantee.

Option 2: Targeted assistance through FHA and other initiatives would be complemented by a government backstop designed only to promote stability and access to mortgage credit in times of mortgage stress. The government backstop would have a minimal presence in the market under normal economic conditions, but would scale up to help fund mortgages if private capital became unavailable in times of crisis.

Option 3: Access would be broadened for creditworthy

Americans and help ensure stability in times of market stress. Alongside the FHA and targeted assistance initiatives, the government would provide reinsurance for certain securities backed by high-quality mortgages. These securities would be guaranteed by closely regulated private companies under stringent capital standards and strict oversight, and reinsured by the government. The government would charge a premium to cover future claims and would not pay claims until private guarantors were eliminated.

Each of these options will require legislation, and they will be the course of significant debate as Congress tries to strike the right balance between providing Americans with broad access to mortgages, managing the risk to taxpayers and maintaining a stable, healthy mortgage market.

The future of Fannie and Freddie

Approximately 90 days after the Administration announced their plan to wind down Fannie Mae and Freddie Mac, House Republicans introduced their own plan. The plan calls for a hike in the fees charged to borrowers in two years, as well as other steps to shrink the companies' footprint in the housing market. The plan also calls on Fannie and Freddie to begin selling their massive portfolios of mortgage instruments (which keep rates low), and give up other advantages not available to banks and private sector forums.

Though the Administration generally agrees that it is necessary to increase costs of obtaining Fannie- and Freddie-backed mortgages to bring private sector firms back into the market, they also worry that withdrawing Fannie and Freddie's support for housing too quickly could further destabilize an already struggling housing market.

Life without Fannie and Freddie may be a vision shared by the Administration and House Republicans, but it is not likely to be realized any time soon. Congress must agree on a plan, which could take years, and then the market must be weaned slowly from dependence on the companies and the financial backing they provide. □

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