NAFCU

Testimony of

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On behalf of

The National Association of Federal Credit Unions

"Housing Finance Reform: Protecting Small Lender Access to the Secondary Mortgage Market"

Before the

United States Senate Committee on Banking, Housing, and Urban Affairs

November 5, 2013

Good morning, Chairman Johnson, Ranking Member Crapo and Members of the Committee. My name is John Harwell, and I am testifying today on behalf of the National Association of Federal Credit Unions (NAFCU). I appreciate the opportunity to share NAFCU's views with the committee on, "Housing Finance Reform: Protecting Small Lender Access to the Secondary Mortgage Market." NAFCU appreciates the bipartisan approach committee leadership and members have demonstrated on this critical issue. In addition to our testimony, NAFCU member credit unions look forward to continuing to work with you beyond today's hearing to ensure access to the secondary mortgage market for credit unions and their 96 million members.

Throughout my career in financial services I have had a deep focus on home loans and have an understanding of credit union mortgage lending from a number of perspectives. I currently serve as the Associate Vice President of Risk Management at Apple Federal Credit Union (Apple FCU) in Fairfax, Virginia. Before joining the management team at Apple FCU, I was with FedChoice FCU and served in a number of capacities culminating in Membership Services Manager. Over the years, I have been involved in the mortgage lending process as a loan officer, branch manager, compliance officer and risk manager. In addition to my responsibilities at Apple FCU, I currently serve on the Board of Directors of the Metropolitan Area Credit Union Managers Association dedicated to continuing education for credit union personnel from executives to board volunteers.

Headquartered in Fairfax, Virginia, Apple FCU serves more than 161,000 members with assets totaling over $1.8 billion. With 21 branches across northern Virginia, Apple FCU provides diversified financial services including mortgage origination and servicing. Financial education is very important to Apple FCU, and we are known for our student-run credit union branches in Fairfax County schools where we are able to reach young people and teach them the importance of personal finance.

As you know, NAFCU is the only national organization exclusively representing the interests of the nation's federally-chartered credit unions. NAFCU-member credit unions collectively account for approximately 68 percent of the assets of all federally chartered credit unions. NAFCU and the entire credit union community appreciate the opportunity to participate in this discussion regarding housing finance reform. My testimony today will explore the longstanding vital relationships credit unions have with the government sponsored enterprises (GSEs) and how important it is for any housing finance reform package to ensure credit union access to the secondary market under fair pricing conditions. Key issues in the housing finance reform debate for credit unions include:

- An explicit government guarantee on mortgage backed securities (MBS)
- Fair pricing and fee structures that reward loan quality
- Ensuring market feasibility of a mutual should such an entity be adopted in statute
- Flexible underwriting standards that will allow credit unions to best serve their members
- Adequate transition time to a new housing finance model

Background on Credit Unions and Credit Union Mortgage Lending

Historically, credit unions have served a unique function in the delivery of necessary financial services to Americans. Established by an act of Congress in 1934, the federal credit union system was created, and has been recognized, as a way to promote thrift and to make financial services available to all Americans, many of whom would otherwise have limited access to financial services. Congress established credit unions as an alternative to banks and to meet a precise public need—a niche credit unions fill today for over 96 million Americans. Every credit union is a cooperative institution organized "for the purpose of promoting thrift among its members and creating a source of credit for provident or productive purposes." (12 § USC 1752(1)). While nearly 80 years have passed since the *Federal Credit Union Act* (FCUA) was signed into law, two fundamental principles regarding the operation of credit unions remain every bit as important today as in 1934:

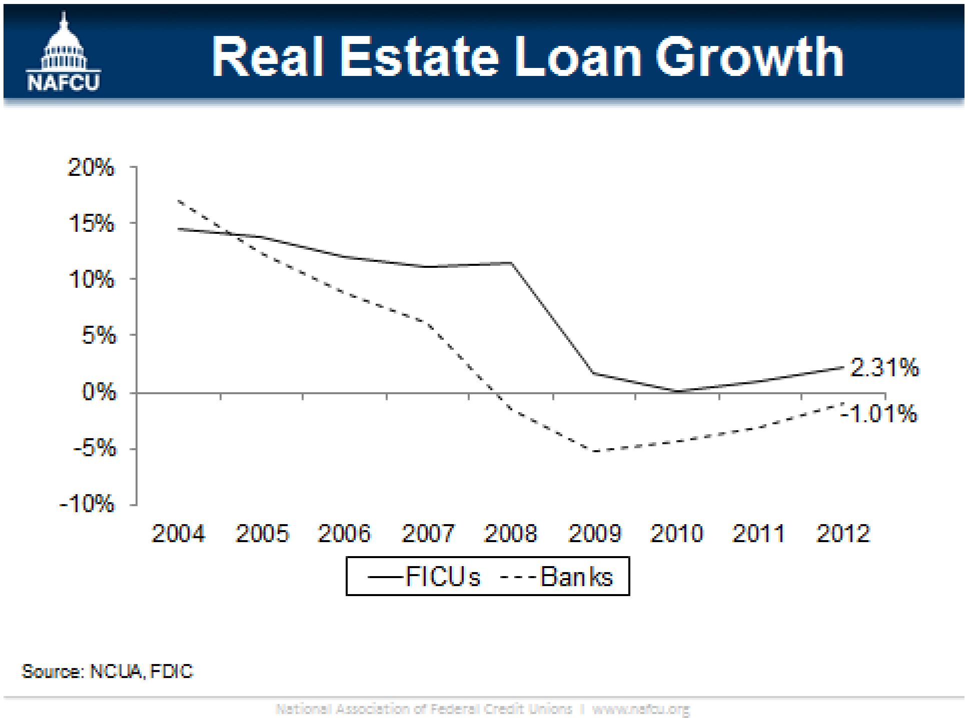
- credit unions remain totally committed to providing their members with efficient, low-cost, personal financial service; and,
- credit unions continue to emphasize traditional cooperative values such as democracy and volunteerism. Credit unions are not banks.

The nation's approximately 6,700 federally insured credit unions serve a different purpose and have a fundamentally different structure than banks. Credit unions exist solely for the purpose of providing financial services to their members, while banks aim to make a profit for a limited number of shareholders. As owners of cooperative financial institutions united by a common bond, all credit union members have an equal say in the operation of their credit union—"one member, one vote"—regardless of the dollar amount they have on account. These singular rights extend all the way from making basic operating decisions to electing the board of directors—something unheard of among for-profit, stock-owned banks. Unlike their counterparts at banks and thrifts, federal credit union directors generally serve without remuneration—a fact epitomizing the true "volunteer spirit" permeating the credit union community.

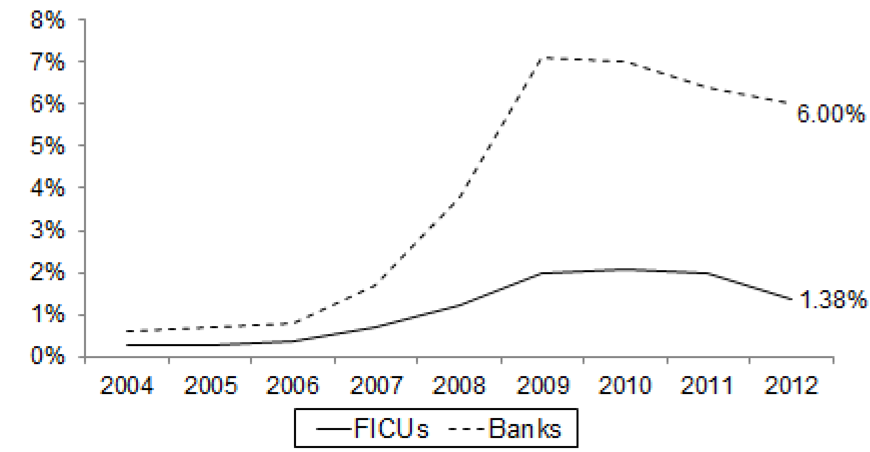
Credit unions continue to play a very important role in the lives of millions of Americans from all walks of life. As consolidation of the commercial banking sector has progressed, with the resulting depersonalization in the delivery of financial services by banks, the emphasis in consumers' minds has begun to shift not only to services provided, but also—more importantly—to quality and cost of those services. Credit unions are second-to-none in providing their members with quality personal financial services at the lowest possible cost.

As has been noted by Members of Congress across the political spectrum, credit unions were not the cause of the recent economic crisis, and examination of their lending data indicates that credit union mortgage lending has outperformed bank mortgage lending during the recent downturn. This is due in part to the fact that credit unions were not the cause of the proliferation of sub-prime loans, instead focusing on placing their members in solid products they could afford.

While the housing market continues to recover from the financial crisis, and Congress works to put into place safeguards to ensure such a crisis never happens again, credit unions continue to be focused on providing their member-owners with the basic financial products they need and demand. The graphs below highlight how credit union real estate loan growth outpaced banks during the downturn, and how credit unions have fared better with respect to real estate delinquencies and real estate charge-offs. The fourth graph demonstrates how credit unions are holding more long-term real estate loans as a percentage of total real estate loans than banks. It is with this data in mind that NAFCU urges members of the Committee to recognize the historical performance and high quality of credit union loans as housing finance reform moves forward.



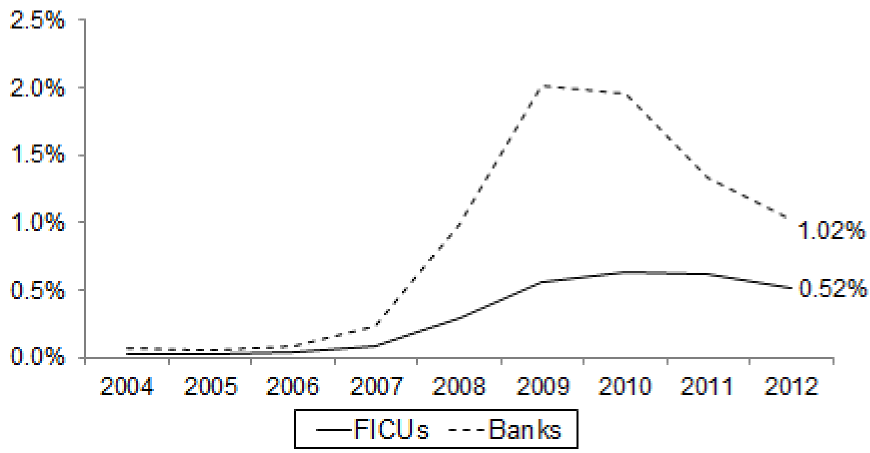
Real Estate Delinquencies*



FICU delinquencies are 60 days or more late; bank delinquencies are 90 days or more late

Source: NCUA, FDIC

Real Estate Charge-offs



Source: NCUA, FDIC

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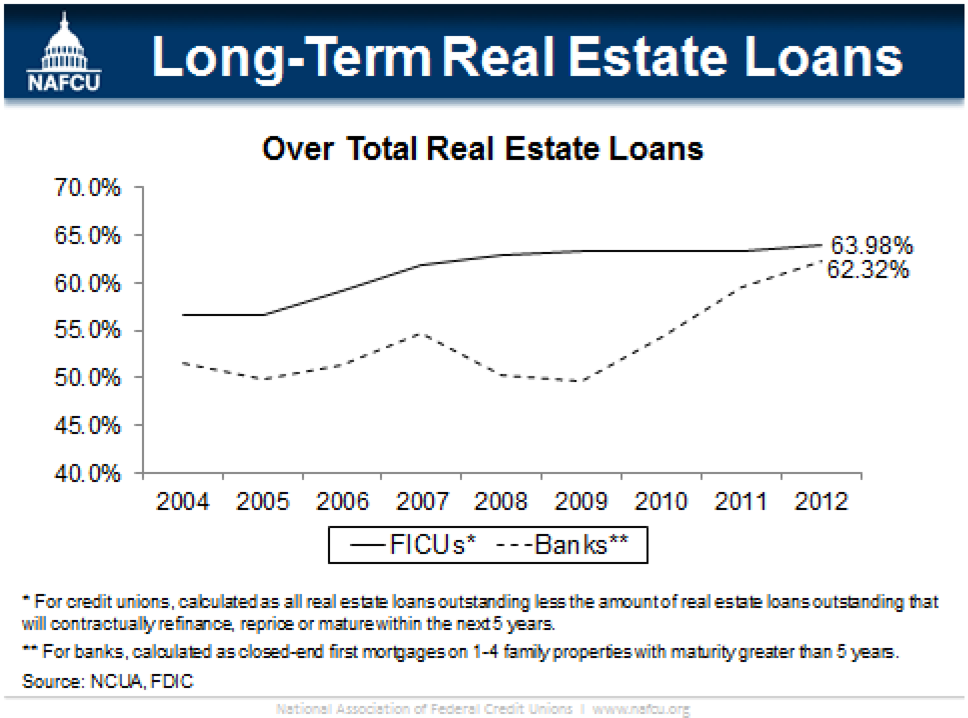
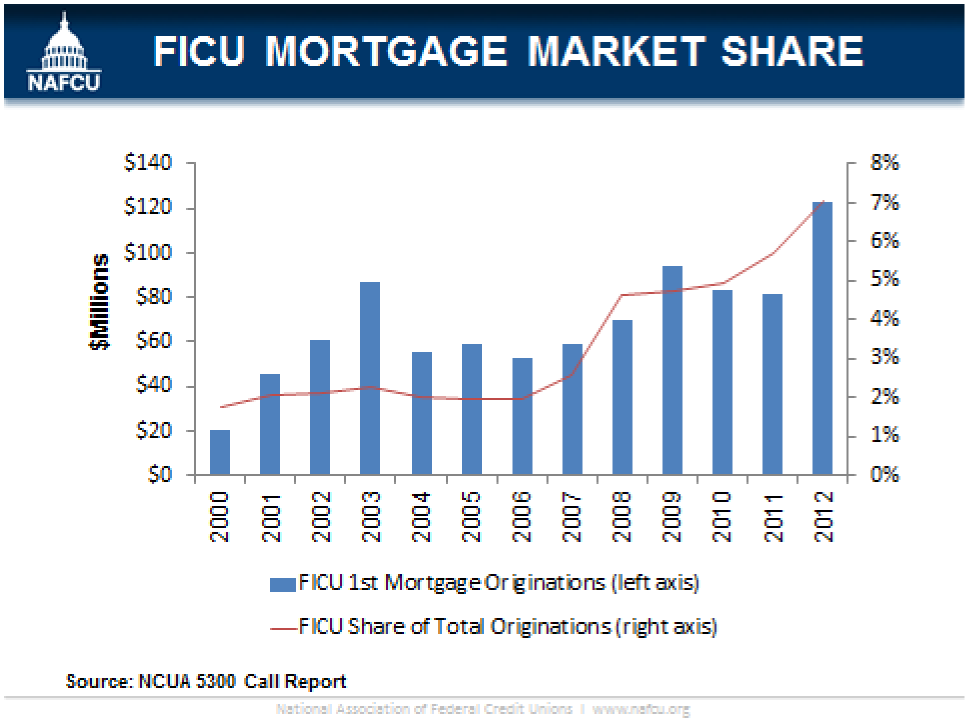
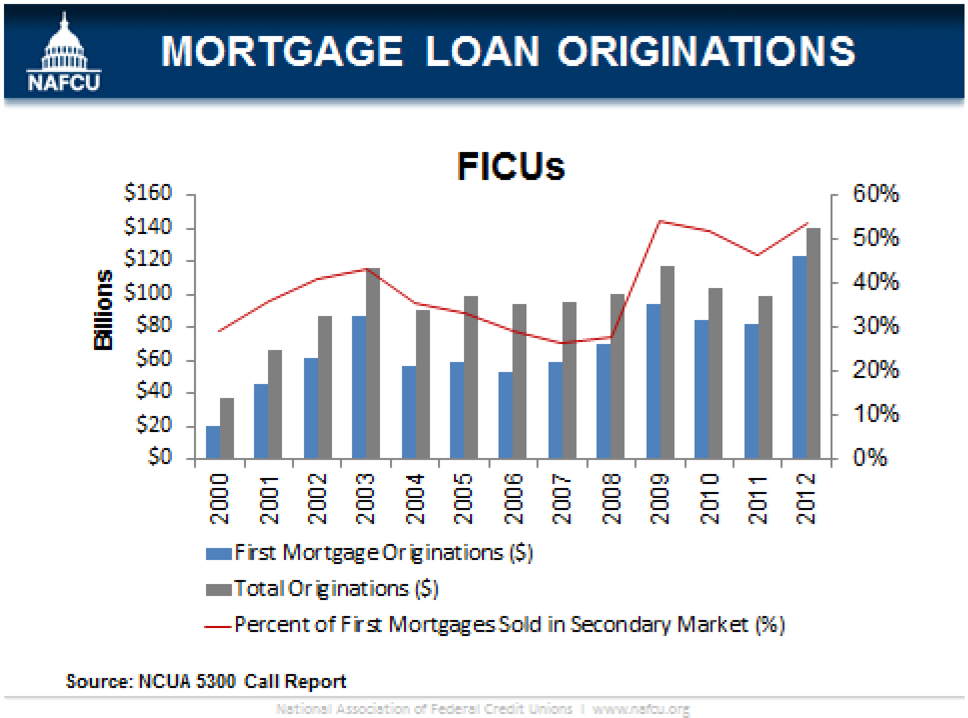


As Committee discussions on this topic continue, a primary concern of credit unions is continued unfettered access to the secondary mortgage market including adequate transition time to a new system should lawmakers see such a change necessary. A second concern, equally as important, is recognizing the quality of credit union loans through a fair pricing structure. Because credit unions originate a relatively few number of loans compared to others in the marketplace – federally insured credit unions had about 7 percent of the first mortgage originations in 2012 (see chart below) – they cannot support a pricing structure based on loan volume, institution asset size, or any other geopolitical issue that will lend itself to discrimination and disadvantage their member-owners.



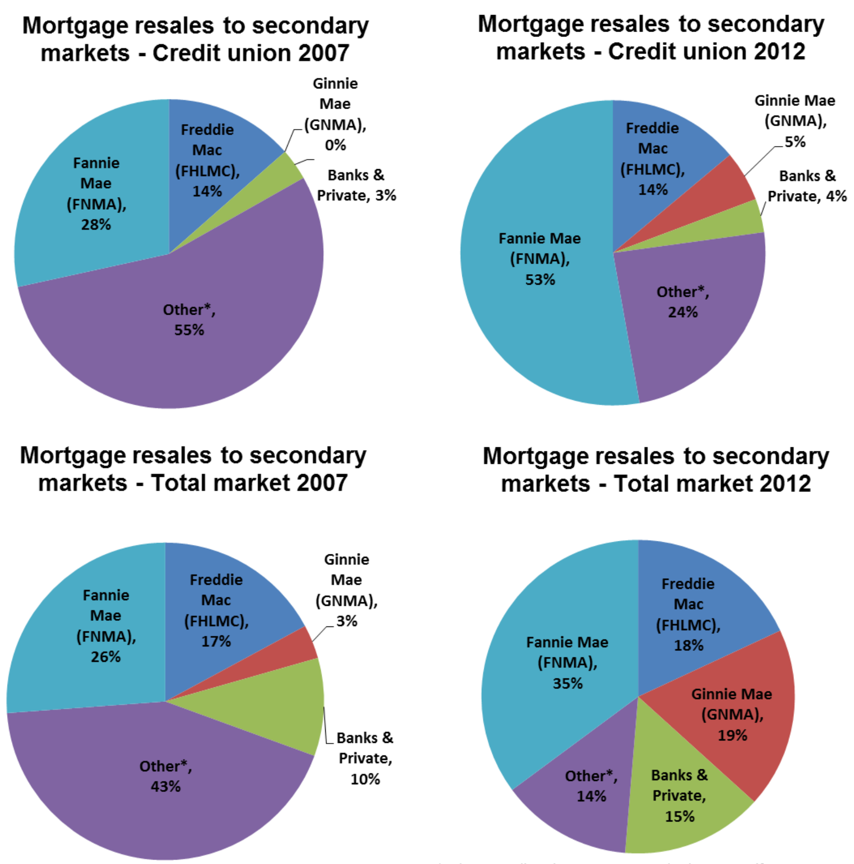
Recent trends in asset portfolios, coupled with the current interest rate environment, present a unique challenge to credit union management. In the past few years, interest rates have fallen to record lows, credit unions have experienced vigorous share growth and credit union participation in the mortgage lending arena has increased to historic heights. Credit union mortgage originations more than doubled between 2007 and 2013, and the credit union share of first mortgage originations expanded from 2.5 to about 7 percent. The portion of first mortgage originations sold into the secondary market also more than doubled over that same period, from 25.7 percent in 2007 to 53.6 percent in 2012, according to National Credit Union Administration (NCUA) call report data (see chart below).



While credit unions hedge against interest rate risk in a number of ways, selling products for securitization on the secondary market remains a key component of safety and soundness. Lenders must have continued and unfettered access to secondary market sources including Fannie Mae, Freddie Mac, Ginnie Mae and the Federal Home Loan Banks (FHLBs) as they are valuable partners for credit unions who seek to hedge interest rate risks by selling their fixed-rate mortgages to them on the secondary market. Not only does this allow credit unions to better manage risk, but they are also able to reinvest those funds into their membership by offering new loan products or additional forms of financial services. A 2012 NAFCU real estate survey highlights the growing use of GSEs among credit unions. More than three-quarters of respondents indicated that credit union board policy restricted the percentage of real estate loans that could be held on their balance sheet, with a median limitation of 35 percent. Without these critical relationships credit unions would be unable to provide the services and financial products their memberships demand and expect.

Home Mortgage Disclosure Act data shows how heavily credit unions have come to rely on the GSEs. Between 2007 and 2012, the portion of credit union first mortgages that were sold to

Fannie Mae grew from 28 percent to 53 percent. The portion sold to Freddie Mac remained a constant 14 percent over the same period. Credit unions sold a total of 67 percent of their first mortgages to the GSEs in 2012. The total market for mortgage resales is also heavily dependent on the GSEs. The portion sold to Fannie Mae and Freddie Mac in 2007 was 43 percent in 2007 and 53 percent in 2012.



*Other = Credit Union, Mortgage Bank, Finance or Life Ins. company

Finally, it should also be noted that the government plays an important role in helping to set standards and bring conformity to the housing market. Changing standards to eliminate or make conformity difficult could make it harder for credit unions to sell loans onto the secondary market as they do not have the economies of scale larger market participants enjoy.

Key Credit Union Concerns in Housing Finance Reform Efforts

In 2010, as the future of housing finance became a focal point in Congress, with the Administration, and among the regulatory agencies, the NAFCU Board of Directors established a set of principles that the association would like to see reflected in any reform efforts. The aim of these principles (listed below) is to help ensure that credit unions are treated fairly during any housing finance reform process.

- NAFCU believes a healthy, sustainable and viable secondary mortgage market must be maintained. Credit unions must have unfettered, legislatively-guaranteed access to such a market. In addition, in order to achieve a healthy, sustainable and viable secondary market, NAFCU believes there must be healthy competition among and between market participants in every aspect of the secondary market. Market participants should include, at a minimum, multiple Government Sponsored Enterprises (GSEs), Federal Home Loan Banks, Ginnie Mae (as insurer of FHA, VA, and other government-backed loans), and private entities.

- The U.S. government should issue explicit guarantees on the payment of principal and interest on MBSs. The explicit guarantee will provide certainty to the market, especially for investors who will need to be enticed to invest in the MBSs and facilitate the flow of liquidity.

- During any transition to a new system (whether or not current GSEs are to be part of it) credit unions must have uninterrupted access to the GSEs, and in turn, the secondary market.

- Credit unions could support a model for the GSEs that is consistent with a cooperative or a mutual entities model. Each GSE would have an elected Board of Directors, be regulated by the Federal Housing Finance Agency, and be required to meet strong capital standards.

- A board of advisors made up of representatives from the mortgage lending industry should be formed to advise the FHFA regarding GSEs. Credit unions should be represented in such a body.

- While a central role for the U.S. government in the secondary mortgage market is pivotal, the GSEs should be self-funded, without any dedicated government appropriations. GSE’s fee structures should, in addition to size and volume, place increased emphasis on quality of loans and risk-based pricing for loan purchases should reflect that quality difference. Credit union loans provide the high quality necessary to improve the salability of many agency securities.

- Fannie Mae and Freddie Mac should continue to function, whether in or out of conservatorship, and honor the guarantees of the agencies at least until such time as necessary to repay their current government debts.

- NAFCU does not support full privatization of the GSEs at this time because of serious concerns that small community-based financial institutions could be shut-out from the secondary market.

- The Federal Home Loan Banks (FHLBs) serve an important function in the mortgage market as they provide their credit union members with a reliable source of funding and liquidity. Reform of the nation's housing finance system must take into account the consequence of any legislation on the health and reliability of the FHLBs.

Mortgage Lending at Apple FCU

Apple FCU currently has over 3,150 loans and $720 million in total mortgage loan originations outstanding. About a third of our loans are sold on the secondary market to Freddie Mac. Apple FCU has maintained the servicing on those loans, as it is important to us to keep that interaction with our members. The 30-year fixed rate mortgage is an important product to our membership and is a close second to the 15-year fixed rate in being our most common type of first trust. We currently hold over 600 30-year fixed rate mortgages in portfolio. Any change to housing finance should be done in a way that helps preserve this product for credit union members in the marketplace.

NAFCU's Perspective on Emerging Senate Debate

NAFCU applauds Chairman Tim Johnson and Ranking Member Mike Crapo for their work in addressing solvency of the Federal Housing Administration earlier this year, and their continued bipartisan attention to housing policy as the Banking Committee agenda aggressively pursues housing finance reform ideas from the perspective of all stakeholders. We would also like to recognize the work of Senators Mark Warner and Bob Corker, and the members of this Committee who have cosponsored their legislation, for laying the foundation for housing finance reform with the introduction of the "Housing Finance Reform and Taxpayer Protection Act of 2013" (S.1217). As you know, this legislation has the support of several committee members and provides for an explicit government guarantee on qualifying mortgage backed securities in a reformed secondary market.

The Importance of Maintaining a Government Guarantee

NAFCU and its member credit unions have examined various proposals for reform of the housing finance system and have reached the conclusion that we cannot support any approach that does not maintain an explicit government guarantee of payment of principal and interests on mortgage backed securities (MBS). The explicit guarantee will provide certainty to the market, especially for investors who will need to be enticed to invest in the MBS and facilitate the flow of liquidity in times of economic uncertainty. We think the approach found in S. 1217 where private capital stands in front of the guarantee is workable, and believe this type of approach offers a viable public-private solution.

Key Elements of the Current System

Fannie Mae and Freddie Mac play important roles in the ability of credit unions to offer mortgage loans to their membership. A major part of this comes from the ease of transaction credit unions currently experience when using software provided by Fannie Mae and Freddie Mac.

At Apple FCU, we underwrite to Freddie Mac guidelines using their Loan Prospector program. The Loan Prospector program is used for all mortgage loans including jumbo loans. Our Lending operating system is called MortgageBot. Mortgage lenders and investors make a lending decision by looking at some basic factors: a person's capacity to repay a loan, a person's credit experience, the value of the property being financed, and the type of mortgage. Freddie Mac's Loan Prospector program dramatically speeds up the mortgage lending process and reduces the cost of getting a mortgage by using statistical computer models based on traditional underwriting factors. Loan Prospector never uses factors such as a borrower's race, ethnicity, age, or any other factor prohibited by the nation's fair housing laws. This type of digital underwriting and standardization makes the entire process user friendly must be maintained in any new system.

While digital underwriting and standardization provide for ease of transaction, it should be noted that becoming an approved lender through Freddie Mac is not an easy process. While NAFCU understands and supports thorough requirements to ensure unscrupulous lenders are kept out of the marketplace, lawmakers must recognize the considerable amount of time it can take to become an approved lender at the various GSEs and account for such time in a transition to any new system.

Furthermore, even though Apple FCU is not currently using it, the function of the cash window at the GSEs as a single loan execution process is also vital to credit unions moving forward.

S. 1217 and the Creation of the New Federal Mortgage Insurance Corporation

As the Committee is aware, S. 1217 would replace the Federal Housing Finance Agency (FHFA) with a new Federal Mortgage Insurance Corporation (FMIC). The legislation also establishes a new statutory conforming loan limit of $417,000 for a single family residence. NAFCU has concerns about the impact this could have on the availability of loans in high-cost areas. NAFCU asks the Committee to consider if it is best to have the conforming loan limit defined in statute, or could it be better served by being evaluated and established by the regulator?

Any number of governance models could be sufficient should the new Federal Mortgage Insurance Company (FMIC) envisioned in S.1217 become a reality. If there is a single director at the FMIC, NAFCU believes there should an advisory board with at least one dedicated credit union representative. If the FMIC is governed by a board, there should be at least one credit union representative on the board. It should be noted that prior to the financial crisis, credit unions didn’t always have an equal voice at the GSEs (due to limited volume) to assure pricing from the GSEs that reflected the quality of credit union loans. The changes that occurred during the crisis helped mitigate this concern, and we hope that continues under a new system.

While NAFCU appreciates the recognition of “community based financial institutions” in statute, it’s imperative that legislative text is explicit in requiring robust experience specifically in the credit union space.

Funding of the FMIC should be done in a way as to limit the cost to financial institutions as much as possible. NAFCU believes it would be important to have an office at the new regulator with a dedicated focus and expertise on the needs of community institutions such as credit unions. In its reports to Congress, NAFCU supports credit union specific language on how the FMIC has provided liquidity, transparency, and access to mortgage credit in support of a robust secondary mortgage market and production of RMBS. As the FMIC establishes a fee structure, small financial institutions appreciate the clarification in statute that fees established by the FMIC should be "uniform" and can't be based on "volume to be purchased by an issuer." NAFCU believes it is critical to have a fee schedule that rewards loan quality, and we would support going further to expressly state this in the bill.

The FMIC would also have the ability to approve issuers. NAFCU would support clarification in statute that credit unions can securitize loans. While the NCUA is considering regulations in this regard, statutory clarification could help clear up any ambiguity.

S. 1217 and the Proposed Mutual Securitization Company

In the context of S.1217, NAFCU believes the concept in Sec. 215 of the legislation that establishes the FMIC Mutual Securitization Company is a workable solution. It is important that such an entity would help ensure that there is guaranteed access to the secondary market at all times for all credit unions. As noted above, while the NCUA is contemplating giving credit unions the ability to securitize mortgages, such authority does not currently exist. Therefore, the functions that the mutual would perform are especially vital to credit unions, as well as community banks and other small lenders, to help ensure access to the secondary market. We applaud the supporters of S. 1217 for including this key element, especially Senators Jon Tester and Mike Johanns for their leadership in this area.

While NAFCU believes that the mutual is a viable option, there are ways that it can be improved. NAFCU has concerns about the $15 billion cap for participation in the mutual that exists in S. 1217 as entities below this arbitrary asset size threshold will be unable to generate enough volume to ensure liquidity. NAFCU has suggested that, if there is a cap, it should be much higher (no less than $250 billion) to give most regional banks the opportunity to participate and generate the volume needed for the mutual to be successful.

In terms of an approval process for entities to participate in the mutual, standards could be set out by the new mutual board of directors, which should be elected by the membership. The board should include credit union representation (including at least one federal credit union representative) that is proportionately equal to other industry representatives on the board. Furthermore, since the mutual would be the guaranteed route to access the secondary market for small lenders, especially in difficult times, it is important that there be a streamlined process to become a member. Conversely, we also believe it should not be made too difficult for an entity to leave the mutual should they desire.

Credit unions did not cause the financial crisis, and NAFCU believes that historical mortgage lending data should be taken into account as the secondary mortgage market is reformed. NAFCU believes that fee structures associated with the mutual, whether it is to capitalize or to sustain the mutual over time, should be based on loan quality as opposed to the volume of loans an entity is able to generate. If politically feasible, Congress should consider the mutual having some type of government seed money that will help the mutual get off the ground and encourage qualifying entities to participate from day one. Such funds could be paid back over a period of years from the profits of the mutual.

NAFCU believes it would be viable to have the mutual be governed by the new Federal Mortgage Insurance Corporation (FMIC) as outlined in S. 1217. It should be noted NAFCU believes the mutual's board of directors should be empowered to make day-to-day operating decisions and that it should be self-regulated to the greatest extent possible.

Finally, the new mutual will likely need technology and/or other infrastructure from the current GSEs to begin operations. NAFCU believes that sale of technology to the mutual should be done at the most reasonable price possible. The pricing and sale of technology will have a direct impact on the costs necessary to capitalize the mutual.

The Role of Federal Home Loan Banks (FHLBs) in S. 1217

The Federal Home Loan Banks serve an important function in the mortgage market as they provide their credit union members with a reliable source of funding and liquidity. Reform of the nation's housing finance system must take into account the consequence of any legislation on the health and reliability of credit unions.

NAFCU supports the FHLBs being one option for credit union access to the secondary mortgage market as proposed in S. 1217. Currently, about 17% of credit unions belong to their regional FHLB.

Whether or not a credit union would use their FHLB membership as a primary channel to access the secondary market would be subject to many factors, including the current relationship between the credit union and their FHLB. Because the extent to which credit unions that are a member of their FHLB utilize current services varies greatly, we would expect the same should FHLBs become issuers in a new housing finance system. While NAFCU is supportive of the idea, we believe this cannot be the only mechanism in place for credit unions to gain access to the secondary market. Other options such as the proposed mutual and private placement must be available to credit unions as well. Having multiple options will allow credit unions to choose the avenue that works best for them and help ensure a healthy competition for their loans, which can help with fair pricing.

Transition to a new Housing Finance System

Should Congress act to reform the nation's housing finance system, getting the transition right will be critical. More than anything, to ensure a smooth transition to a reformed secondary mortgage market, credit unions need certainty that changes outlined in legislation and accompanying regulation will function as intended. Credit unions must be kept up-to-date during this transitional period and lawmakers should build flexibility into the transitional period to account for unforeseen implementation challenges. NAFCU believes that Congress should first agree on a set of reforms and then, based on the nature and complexity of such reforms, establish a timeframe for transition. Arbitrarily pledging to adhere to a transitional timeframe before a set of reforms are agreed upon could create otherwise avoidable issues for new entities created under the bill and outside stakeholders.

In an effort to ease the transition, Congress should consider moving currently approved Fannie and Freddie lenders into a new system en bloc and giving them an expedited certification. This could reduce confusion and, if executed properly, could make the process run more smoothly for all involved. It can take time for lenders to be certified with the GSEs, and this time to certify, whether to the GSEs or to a new system, should be factored in to the transition time.

NAFCU also believes it is important that a new system be up and running before the ability of Fannie Mae and Freddie Mac to guarantee MBS is shut down. One way to accomplish this may be to have the two entities exist in a winding down capacity during the first six months of a new system. For example, they could still collect mortgages from lenders and move them through a new mutual to test the process. Lenders could use them and/or transition to the mutual or other options during this timeframe to allow for a smooth transition.

The Importance of Servicing Rights to Credit Unions

Any new housing finance system must contain provisions to ensure credit unions can retain servicing rights to loans they make to their members. While many turn to credit unions for lower rates and more palatable fee structures, they also want to work with a reputable organization they trust will provide them with high quality service. Because credit unions work so hard to build personal relationships with their members, relinquishing servicing rights has the potential to jeopardize that relationship in certain circumstances.

At Apple FCU, we currently retain servicing rights on all of our loans. This was especially beneficial during the economic crisis, as it allowed our members to approach us when they got in trouble and allowed us to work with them on their loan and keep them in their home. Furthermore, we believe the National Credit Union Administration, in conjunction with the FHFA or whatever entity replaces the FHFA moving forward, should set standards for other items important to small lenders. Such a process should be subject to public comment and take into account the operational expertise of small lenders. The Board of Directors of the mutual (should this idea be adopted) should also have a significant voice in the process.

Underwriting Criteria in Any New System

NAFCU has concerns about the “Qualified Mortgage” (QM) standard included in S. 1217 for loans to be eligible for the government guarantee. We believe underwriting standards may be best left to the new regulator and do not think that they should be established in statute. Doing so would allow the regulator to address varying market conditions and act in a counter-cyclical manner if needed.

Furthermore, given the unique member-relationship credit unions have, many make good loans that work for their members that don’t fit into all of the parameters of the QM box. Using the CFPB QM standard for the guarantee would continue to discourage the making of non-QM loans.

In particular, NAFCU would support the following changes to the QM standard to make it more amenable to the quality loans credit unions are already making:

> *Points and Fees*
>
> NAFCU strongly supports bipartisan legislation in both the Senate and House to alter the definition of “points and fees” under the “ability-to-repay” rule set to take effect in January of next year. NAFCU has taken advantage of every opportunity available to educate and weigh in with the CFPB on aspects of the ability-to-repay rule that are likely to be problematic for credit unions and their members. While credit unions understand the intention of the rule and importance of hindering unscrupulous mortgage lenders from entering the marketplace, it is time for Congress to step in and address unfair and unnecessarily restrictive aspects of this CFPB rule.
>
> NAFCU supports exempting from the QM cap on points and fees: (1) affiliated title charges, (2) double counting of loan officer compensation, (3) escrow charges for taxes and insurance, (4) lender-paid compensation to a correspondent bank, credit union or mortgage brokerage firm, and (5) loan level price adjustments which is an upfront fee that the Enterprises charge to offset loan-specific risk factors such as a borrower’s credit score and the loan-to-value ratio.

Making important exclusions from the cap on points and fees will go a long way toward ensuring many affiliated loans, particularly those made to low- and moderate-income borrowers, attain QM status and therefore are still made in the future.

Loans Held in Portfolio

NAFCU supports exempting mortgage loans held in portfolio from the QM definition as the lender, via its balance sheet, already assumes risk associated with the borrower's ability-to-repay.

40-year Loan Product

Credit unions offer the 40 year product their members often demand. To ensure that consumers can access a variety of mortgage products, NAFCU supports mortgages of duration of 40 years or less being considered a QM.

Debt-to-Income Ratio

NAFCU supports Congress directing the CFPB to revise aspects of the 'ability-to-repay' rule that dictates a consumer have a total debt-to-income (DTI) ratio that is less than or equal to 43 percent in order for that loan to be considered a QM. This arbitrary threshold will prevent otherwise healthy borrowers from obtaining mortgage loans and will have a particularly serious impact in rural and underserved areas where consumers have a limited number of options. The CFPB should either remove or increase the DTI requirement on QMs.

We would also like to caution against the perpetuation of the use of one brand of credit scoring model. Both Fannie Mae and Freddie Mac require loans that are underwritten using FICO scoring models. We believe any new system should be open to other possible credit scoring models as well.

Finally, NAFCU cautions against the 5 percent minimum down payment requirement found in S. 1217 for a loan to be government guarantee eligible. Down payment isn't the only indicator in determining underwriting soundness and we believe a hard down payment requirement will reduce a lender's flexibility in matching consumers with a product that best suits their needs.

Loan Pricing

Prior to the financial crisis, credit unions did not always receive fair pricing based on quality from the GSEs for their loans, as many pricing models were based on volume. This has improved in recent years and NAFCU believes it is critical that this fair pricing based on quality is maintained in any new system.

Furthermore, while we would support the ability of the mutual to handle non-QM loans, and even support a guarantee program for non-QM loans (beyond the emergency power established in S. 1217), NAFCU believes it is important that the pricing for these non-QM loans reflects the risks that they could pose to the system.

Conclusion

NAFCU appreciates the Banking Committee's bipartisan approach to housing finance reform and the inclusive nature of the process. While the proposal in S. 1217 represents a positive step in the housing finance reform debate, we believe there are aspects of the bill that can be improved. In the end, whatever approach is taken to reform, it is vital that credit unions continue to have unfettered guaranteed access to the secondary market and get fair pricing based on the quality of their loans. The government must also continue to play a role by providing some form of government guarantee to help stabilize the market.

Thank you for the opportunity to provide our input on this important issue. NAFCU member credit unions look forward to working with Chairman Johnson, Ranking Member Crapo, committee members and your staffs as housing finance reform legislation moves through the legislative process.

I thank you for your time today and would welcome any questions that you may have.