KIRWAN INSTITUTE for the Study of Race and Ethnicity

THE FUTURE OF FAIR HOUSING and FAIR CREDIT

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FANNIE, FREDDIE, AND THE FUTURE OF FAIR HOUSING

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The **Kirwan Institute for the Study of Race and Ethnicity** is a university-wide interdisciplinary research institute. We generate and support innovative analyses that improve understanding of the dynamics that underlie racial marginality and undermine full and fair democratic practices throughout Ohio, the United States, and the global community. Responsive to real-world needs, our work informs policies and practices that produce equitable changes in those dynamics.

FANNIE, FREDDIE, AND THE FUTURE OF FAIR HOUSING

Our research and analysis of Fannie and Freddie reveals two key takeaways. First, Fannie and Freddie were neither outright responsible for the current subprime and foreclosure crisis, nor will their restructuring alone eradicate the problem without broader financial reform. Second, sustainable homeownership, especially for marginalized borrowers, is not just about turning on the spigot of credit. Sustainable homeownership is about many factors, including human capital and mobility. We need to address the bigger picture of sustainable homeownership, research the different paths that lead to sustained homeownership for marginalized groups, and then determine how Fannie and Freddie can best be restructured to be more responsive to targeted groups' needs. The literature to date is largely silent on how policy in general, and Fannie and Freddie in particular, could be restructured or managed differently to improve sustainable homeownership in neighborhoods of opportunity.

This paper represents a first step in that direction. Section I begins with a brief discussion on the key players influencing Fannie and Freddie, past and present. Section II provides an abbreviated history of how the Enterprises roles and missions have changed through the years. Sections III and IV discuss the Enterprises obligations to affirmatively further fair housing, and the outcomes of the Enterprises activities with regards to low- and moderate-income borrowers, respectively. The paper concludes with a call to action for developing an affirmative fair housing agenda for Fannie and Freddie.

Introduction

The spectacular failure of Fannie Mae and Freddie Mac (the Enterprises) in 2008 and their subsequent conservatorship has drawn increasing attention to what went right, and what went wrong, with Fannie and Freddie as policymakers, advocates, and analysts alike grapple with what the future holds for the Enterprises, and for the US housing financial system as a whole. As we continue in this debate, it is critical to bear in mind that Fannie and Freddie were neither outright responsible for the current subprime and foreclosure crisis, nor will their restructuring alone eradicate the problem without broader financial reform. Indeed, “the systemic failures stemmed from the proliferation of poorly underwritten mortgages channeled through the so-called shadow banking system of unregulated private label securities.”[1]

The US mortgage system is best characterized as a dual, “separate and unequal,” credit delivery system, where “all too often, lower-income and minority communities are served by a distinctly different set of organizations offering a distinctively different mix of products.”[2] These distinctively different products are more representative of discriminatory terms of credit, epitomized by predatory loans, as opposed to an outright denial of credit, which had historically been the case. Nationally, the subprime and foreclosure crises that resulted in the Great Recession provide compelling evidence that we cannot sustain racially disparate policies and practices in our provision of credit and housing. The segregated housing and credit markets have deep roots, beginning in the 1930s when racialized home financing federal policies, such as red-lining that denied credit to entire neighborhoods, were institutionalized by the Federal Housing Agency. During the 1990s, the predatory and subprime markets exploded, and many qualified borrowers of color were channeled into subprime loans. Communities of color, historically the recipients of targeted disinvestment, found themselves flooded with high-cost credit, often of a predatory nature. The system simply imploded after 70-plus years of mounting pressure. In the continuing aftershocks of the financial collapse,

> “ …the lesson policymakers should be taking away from the crisis is that level playing fields are necessary, particularly when it comes to affordable [and fair] access to credit. When safe, affordable, and well-underwritten loans must compete against unregulated, exotic mortgage products priced without regard to underlying asset value or risk and marketed by brokers with misaligned incentives, the results are disastrous, both for homeowners and the larger economy. We must ensure that parallel systems cannot again emerge….”[3]

Nonetheless, Fannie and Freddie's status as mortgage giants in the US financial system necessitates an honest and urgent assessment of their impact and significance in the US mortgage markets. Critics have argued that the Enterprises weren't well- regulated, and were highly leveraged and thus posed significant risk to the mortgage market. Supporters have argued that Fannie and Freddie successfully generated an efficient secondary market and improved credit access for low- and moderate- income borrowers. Whatever your position, clearly Fannie and Freddie are *the* key players in the mortgage market--by the second quarter of 2008, the combined GSE market share of new mortgage business stood at 84%, compared to 46% by the second quarter of 2007.[4] As of the second quarter of 2009, Fannie, Freddie, and the FHA, purchased or guaranteed 9 out of 10 new mortgages.[5]

But the discussion of the future of Fannie and Freddie cannot exclusively focus on issues of safety and soundness. There are essentially two broad policy objectives that must be pursued: decreasing the systemic risk posed by the Enterprises (for example, by limiting their mortgage portfolios), and connecting marginalized borrowers and communities to sustainable homeownership opportunities. These are not necessarily incompatible goals, yet the discussions by the media and officials for the most part have pitted them against each other. Although increasing the safety and soundness of Fannie and Freddie will take concentrated effort and time, it is in the realm of the doable. Solutions have been debated for years, and are fairly straightforward, such as increasing capital requirements and imposing portfolio size limits. However, these regulations—*if not properly designed*—could have a negative impact on affordable and fair housing goals. The Enterprises have long held a responsibility to increase lending and improve housing market outcomes for marginalized borrowers and communities by meeting established numeric goals. Whether the Enterprises were successful in meeting these expanded affordable housing obligations is a matter of debate. Although the Enterprises have generally met numeric lending goals[6] set forth, this has not necessarily translated into overall improved housing market outcomes and homeownership opportunities for marginalized borrowers and communities.

The indisputable racial footprint of the subprime and foreclosure crisis, and the larger economic recession, further begs the question of whether the Enterprises have a duty to affirmatively further fair housing, and if so, whether their past actions have achieved this. Importantly, this is not the same question as to whether the Enterprises have achieved their stated affordable housing goals. Affirmatively furthering fair housing is a question not only of access to sustainable credit, but *where* the housing is located—whether marginalized homebuyers have the opportunity to purchase housing in stable or appreciating neighborhoods and thereby access the opportunity to build wealth as well as gain access to other opportunity structures critical for achieving one's full potential: good schools, quality grocery stores, access to health care, and so forth. If analysis reveals they have not complied with this duty, then what enforcement actions are available and by whom to ensure that going forward, a fair housing agenda stays prominent in the Enterprises activities? Before delving into a more targeted discussion of the missions of the Enterprises, a few more fundamental issues are reviewed, including who is deciding what happens to Fannie and Freddie, who are the key players; and what were the Enterprises' roles and requirements before, what are they now, and what can they do going forward?

I. Who's Running the Show

There are a variety of key players—people with power and interest over the Enterprises—and this composition has changed over the course of the Enterprises' history. The following is a brief list of past and current players, and their interests related to the Enterprises.

Previous Players

The Federal Housing Enterprise Financial Safety and Soundness Act of 1992 (the GSE Act) created the Office of Federal Housing Enterprise Oversight (OFHEO), an independent agency within HUD charged with the duty to oversee and enforce the capital requirements and safety and soundness of Fannie and

Freddie. There were important limitations to this agency however, including inadequate resources for monitoring and the inability to take enforcement actions if it was found that the safety and soundness of the GSEs was deteriorating, unlike the authority available to federal bank regulators.[7] The GSE Act also granted the HUD Secretary expanded authority to regulate and enforce the affordable housing goals (and extended them to Freddie), which had been authorized in 1968 for Fannie but lacked any enforcement mechanism. It further granted the Secretary authority to approve any new mortgage program unless it was found to violate the GSEs' charters or the public interest.[8]

Given their structure as private, for-profit enterprises (but with government-chartered missions), the Board and shareholders had clear power over Enterprise decisions. In the early 2000s, numerous media reports revealed excessive risk taking practices, internal memos discussing the increasing pressure to recapture market share and therefore profits (especially through the intentional targeting of the subprime market), and numerous accounting scandals that inflated returns.[9] The accumulation of these risky practices and irresponsible management decisions led to a buildup of credit risk that ultimately led to their conservatorship.[10]

Current Players

The Federal Housing Finance Agency (FHFA) was created as part of the Housing and Economic Recovery Act (HERA) of 2008[11] on July 30, 2008. The creation of the new, independent federal agency represented a consolidation of regulatory and supervisory authorities previously under the purview of OFHEO, HUD, and the Federal Home Finance Board (regulator of the 12 Federal Home Loan Banks.) Broadly, the FHFA was created to improve the safety and soundness supervision of Fannie, Freddie, and the FHLBs, as well as improve the mission supervision of these agencies. In response to the financial meltdown in October 2008 and rapidly deteriorating economic conditions, and after an intense review of the Enterprises that revealed substantial market, credit, and operational risks, FHFA was authorized to serve as conservator of Fannie and Freddie and help stabilize the housing market.[12] Though the Enterprises' staff and management continue with the day-to-day operations of the two agencies, "the Enterprises consult with and obtain approval of the Conservator before taking action on transactions involving capital; creation of any subsidiaries or affiliates; certain hiring, terminating, and compensation…; and certain other actions that either involve transactions greater than $50 million, relate specifically to the conservatorship, or are likely to cause significant reputation risk."[13]

The Presidential Administration is also a key player, and has used the Enterprises to inject some stability and confidence back into the US housing market, specifically through loan modification and foreclosure mitigation programs (discussed below). However, the Administration will not be revealing their longer term plans for the Enterprises until the 2011 Budget, which will be announced in February. Questions over the future form of the Enterprises remain unanswered, but there are three general proposals (wholly government-owned, re-constitution as GSEs, and privatization) that seem to have gained the most traction, and for which the GAO released an analysis in September 2009. While these three broad forms have been at the center of recent discussions of restructuring Fannie and Freddie, it is becoming more and more apparent that the extremes are not likely to gain much support, and that reconstituted GSEs, with better regulation, is the most likely candidate.[14] Please refer to **Attachment A** for a brief review of the proposed forms.

The Federal Reserve, through expanded authority granted under HERA, has been a critical player in the Enterprises activities. In September 2008, the Federal Reserve committed to supporting the mortgage market and the Enterprises by purchasing their debt obligations and mortgage-backed securities (MBS) in order to reduce the costs and increase the availability of credit for home purchases. As of March 2009, the Federal Reserve committed to purchasing Enterprise debt up to $200 billion each, and purchasing MBS up to $1.25 trillion.[15] However, the Federal Reserve will begin winding down its support of the Enterprises, beginning in the first part of 2010.

The Treasury Department also has a vested interest in the Enterprises. HERA expanded Treasury's scope of authority to provide stability to the Enterprises and increase investor confidence in Enterprise debt and MBS.[16] It is currently the main stockholder of the Enterprises at 79.9%, and has to date provided $111 billion in funding. Recent activity, however, has changed the nature of that aid. On Christmas Eve, the Administration and Treasury pledged unlimited support to the Enterprises by lifting the portfolio caps the previous administration had put in place (in the hopes to avoid a sharp increase in interest rates once the Fed winds down its assistance), and lifting the cap ($400 billion) on the level of assistance the Treasury could offer the Enterprises.[17] In doing so, the Administration has provided the Enterprises with increased flexibility and capacity to carry out its activities, specifically the mortgage modification programs, without worrying about incurring losses, as well as providing the opportunity for a more aggressive approach to the continuing housing market crisis.

Future Players

Who the key future players are will depend on the future form the Enterprises take. For the immediate term, even the next several years, we can expect a continued influence of Treasury as the Enterprises continue to pay their commitments to Treasury (through their Senior Preferred Stock Purchase agreements), and of the Administration, as interest in and need for programs targeted at helping distressed homeowners avoid foreclosure continues. The ultimate details will be worked out in Congress.

In the meantime, the Administration has convened a task force, made up of officials from FHFA, Treasury, HUD, the National Economic Council, and the Council of Economic Advisors, to begin discussing the options for moving forward.

II. Enterprises' Roles: Past, Current, and Future

The Enterprises have undergone significant structural and mission-related changes throughout their history. Created as a government agency in 1938, Fannie Mae was initially charged with the duty to purchase and sell FHA-guaranteed and VA-guaranteed loans in the 1930s and 1940s. It operated in this capacity until the 1950s, when it was charged with the mission to increase liquidity through creating a secondary mortgage market for FHA and VA loans, and reduce regional disparities in interest rates. In 1968 Fannie was reorganized as a government-sponsored enterprise, and the authority and responsibility to serve LMI borrowers was granted. Freddie Mac was created in 1970 to develop a secondary market for conventional mortgage loans; it did not have a housing mission. In 1989, Freddie was reorganized as a government-sponsored entity. The 1992 GSE Act was passed in response to increasing concerns over the safety and soundness of both GSEs, especially in light of the recent Savings and Loan crisis. The Act clarified the housing finance, and expanded the housing mission, responsibilities for both of the GSEs. Whether the Enterprises were successful in meeting these expanded affordable housing obligations is a matter of debate. While generally meeting numeric goals set forth, this has not necessarily translated into overall improved housing market outcomes and homeownership opportunities for marginalized borrowers and communities.

In 2008, the Enterprises were placed in conservatorship. While in conservatorship, their missions have focused on mortgage affordability and availability, foreclosure mitigation, and general housing market stabilization.[18] **Attachment B** provides a more detailed timeline of events.

The Enterprises' future role and activities is of course the subject of much debate. The outcomes of these debates are especially important for affordable housing advocates for the four following reasons:[19]

- Their ability and willingness to provide long- term, fixed- rate financing which provides a sustainable means to homeownership;
- Their importance in multi-family housing. Their involvement with, and in some cases guarantees on, multi-family loans have enabled the completion of a substantial number of developments, including a substantial number of LIHTC projects, purchasing approximately 40% of credits in

past years. [20] Their importance in times of economic crisis is even more pronounced for the multifamily housing sector: between October 2007 and September 2008, the Enterprises together provided 82% of net new multifamily financing;[21]

- Their willingness to buy and/or securitize loans from any bank that meets their underwriting standards helps to "level the playing field" some for smaller community banks; and lastly,
- Their potential to provide additional resources for affordable housing activities, for example, through the Housing Trust Fund requirements.[22]

III. A Duty to Affirmatively Further Fair Housing

Fannie and Freddie are under a general obligation to not discriminate against purchasers of mortgages,[23] and to assist HUD in discovering information on lenders with which they do business to ensure that the lenders are not violating the Fair Housing Act (FHA).[24] Fannie and Freddie must also comport their underwriting and appraisal guidelines to the FHA.[25] Therefore, in addition to any affirmatively furthering fair housing obligations made by virtue of government sponsorship or HUD funding, the Enterprises are under a duty to abide by the FHA.[26] HUD and the Department of Justice share enforcement responsibility in all Title VIII claims.[27] In addition, private parties can make their own claims.[28]

The Secretary of HUD has broad power to enforce and investigate Title VIII claims. Briefly, HUD has the power to receive private claims, initiate investigations, and make claims itself.[29] In addition, once a complaint has been made, HUD has the power to litigate Fair Housing claims in front of an Administrative Law Judge.[30]

The Department of Justice US Attorney's Office and the Civil Rights Division have concurrent authority to enforce Title VIII of the Civil Rights Act.[31] Under Title VIII, the Attorney General and Department of Justice may enforce the Fair Housing Act in two ways. First, if the Attorney General finds upon investigation that there is a pattern of practice of housing discrimination "or the discriminatory denial of rights protected by [Title VIII] to any group of persons,"[32] he or she may initiate civil actions for enforcement.[33] Second, the Attorney General may join a private party suit if the suit is "of general public importance."[34] In addition, the US Attorney may "participate or take the lead in investigating and initiating" fair lending cases.[35] Finally, when HUD files a charge and one party chooses to bring suit in federal court, The Attorney General, through the Civil Rights Division must "initiate and maintain a lawsuit in federal court on behalf of the individual victim."[36]

Why Affirmatively Furthering Fair Housing Matters

Fannie and Freddie are part of a system of credit and housing that has historically been marked by racial discrimination in housing policy. The federal government has a well-documented history of racializing federal policy. For example, the Home Owners Loan Corporation (HOLC), established in 1933 under President Hoover in an effort to provide mortgage relief to homeowners and lenders in the wake of the foreclosure crisis during the Great Depression, developed racial underwriting and appraisal practices. Specifically, HOLC created a neighborhood-ranking system that judged credit-worthiness based on the following four categories:

> "the highest category going to new, racially homogenous, all-white neighborhoods. Outlying Jewish and white working-class neighborhoods were given a second grade, while neighborhoods near a contiguous African American neighborhood were assigned a third category of housing value. The lowest appraisal value was given to all-African American neighborhoods, regardless of the age of the dwellings or the income of the residents."[37]

The Federal Housing Authority, created in 1934 as part of the New Deal legislation, incorporated the policies of HOLC, including the racially discriminatory appraisal methods, neighborhood ranking system, and amortized payment schedule.[38] Both HOLC and FHA required private institutions to adopt "land use tools and subdivision regulations to protect property values" and staff warned developers and realtors that "if a neighborhood is to retain stability it is necessary that properties shall continue to be occupied by the same social and racial classes" and lenders to "not insure mortgage on homes unless they were covered by a racially restrictive covenant, located in racially homogenous neighborhoods, and removed from blighting influences such as poor schools and older housing."[39] In short, "the FHA institutionalized a racially separate and unequal system of home financing that favored suburban building for whites while precluding insurance for homes in racially mixed and nonwhite neighborhoods in the inner city."[40] Fannie Mae, as the offspring of the FHA, inherited this legacy.

This story has gotten lost in the recent debates over not only reforming Fannie and Freddie, but reforming the broader financial system. For example, in discussing the housing market, advocates and analysts hold up the 30-year fixed rate mortgage as the triumph of the US housing finance system, a product introduced by HOLC, standardized under the FHA, and continued through the Enterprises. While the innovation of this "modern long- term, fixed- rate mortgage that we all take for granted…."[41] undoubtedly expanded the possibility of homeownership to millions of Americans since its inception (homeownership rose from 44% in the late 1930s to 64% by the mid-'60s alone), [42] these loans were exclusively offered to white suburban homeowners, to the neglect of households of color and inner city homes. The historic exclusion of households of color and continued disinvestment in urban communities of color created the credit-starved communities ripe for exploitation through predatory products. Exclusion of credit today is less about outright denial of credit, and more about the terms of credit—borrowers of color were 30% more likely to receive a high-cost loan than white borrowers, even after controlling for differences in risk and other factors, such as borrower income and property location.[43] Hispanic and African Americans borrowers were channeled into the subprime market, even though they could have qualified for a prime loan (i.e. long-term amortizing, fixed-rate mortgage).

Subsequent laws have been passed attempting to correct for these policies, such as the Fair Housing Act (1968), the Equal Credit Opportunity Act (1974), and the Community Reinvestment Act (1977). However, other laws have been passed that work against them. For example, layered on top of an already-uneven landscape of opportunity came waves of financial deregulation. Beginning in the 1980s and culminating in the Gramm-Leach-Bliley Act in 1999, Congressional legislation effectively dismantled the system of protections—for both banks and borrowers—established in the 1930s. These acts included the Deregulation and Monetary Control Act of 1980 (DIDMCA), which eliminated state interest rate ceilings on home mortgages where the lender has a first lien; the Alternative Mortgage Transaction Parity Act of 1982 (AMTPA), which dismantled state regulations over alternative mortgage transactions; and the Tax Reform Act of 1986, which disallowed consumer tax deductions on credit cards, but allowed tax deductions on mortgage interest. While the intent of the deregulation legislation was to attract global capital to a competitive market and protect depositories from interest rate risk,[44] it also opened the floodgates to unscrupulous practices and incentivized consumers to gamble with their home equity. As Jesus Hernandez summarized,

> "[these] federal financial policies set the condition for the new subprime market to boom. They eliminated the interest rate caps, so you could charge whatever interest rate you wanted. They allowed for adjustable rate mortgages and balloon payments. They overrode local government restrictions on high-cost lending products. They eliminated the tax write-offs on consumer credit, making high cost mortgages less expensive than your credit card…so everybody put the debt onto their house."[45]

Affirmatively furthering fair housing, therefore, is more than just providing homeownership to those historically excluded. It means the ability for homeowners to buy a house in a stable or appreciating neighborhood, and thereby access the opportunity to build wealth and access other opportunity structures critical for achieving one's full potential, such as good schools, quality grocery stores, access to health care, and so forth. This is different from setting and meeting numeric affordable housing goals. Research shows that meeting these affordable housing goals has not necessarily improved marginalized homeowners' access to improved housing market outcomes, such as the ability to buy in a stable neighborhood. Achieving homeownership in a declining neighborhood does not improve one's ability to achieve wealth and the American Dream. In order to realize this objective we must also pursue affirmative fair credit, where appropriate loans are offered to homeowners based on their situation. Achieving homeownership through highly risky credit products also does not provide a means to sustainable homeownership. It is clear that in order to fix the housing market, and affirmatively further fair housing, we also need to fix the credit system, and affirmatively further fair credit.

IV. Research Review: Moving the Missions Forward

Although increasing the safety and soundness of Fannie and Freddie will take concentrated effort and time, it is in the realm of the doable. Solutions have been debated for years, and are fairly straightforward, such as increasing capital requirements and imposing portfolio size limits. However, these regulations—*if not properly designed*—can have a negative impact on affordable and fair housing goals. Several proposals to achieve reduced risk have been offered: regulating more tightly what kind of mortgages could be held; imposing fees for issuance of debt; directly limiting the size of the portfolio; and increasing the capital requirements.[46] However, these all reduce profit, and therefore might ultimately limit housing goals. Another proposal would be to direct the GSEs to only purchase smaller mortgages, which benefit lower-income households, but may push out middle and upper income homeownership support (which would be politically unattractive).[47]

The Enterprises are expected to improve housing market conditions because they have to meet established numeric lending goals. The three categories are low-income borrowers, underserved areas, and special affordable borrowers.[48] The goals specify a percentage of loans purchased that must qualify for these categories, and these categories are not mutually exclusive (one loan could count towards meeting more than one goal). The focus of these goals is to improve homeownership rates for low and moderate income (LMI) borrowers and improve housing conditions for LMI borrowers and neighborhoods.

The research to date has shown limited improvements in housing market conditions for LMI borrowers and underserved areas as a result of increased GSE activity. Various studies have assessed housing market conditions along a number of indicators, including homeownership rates, vacancy rates, median house values, and single family home prices, to name a few. For example, one study found that in assessing borrowing activity and homeownership rates in tracts designated as "underserved", there was no positive GSE effect on conforming mortgage lending activity and homeownership.[49] This conclusion was despite the fact that the GSEs had apparently met their housing goals. One possible explanation is that the increase in GSE activity is crowding out other secondary mortgage market actors; in this study, the researchers suggest that the increased activity in the conforming sector may come at the expense of lending activity in the non-conforming sector, or may crowd out other private, un-subsidized secondary market intermediaries. The study did find, however, positive effects of CRA activity in the non-conforming sector, and a positive but small effect on homeownership rates, suggesting that the CRA does in fact increase the supply of credit in marginalized communities. Another study focused on the ability of the GSE affordable housing goals to improve housing market conditions and homeownership rates.[50] The study assessed three indicators of housing market conditions—homeownership rates, vacancy rates, and median house value-- and found that GSE-targeted tracts in the study area did not show statistically significant improvements in housing market conditions, suggesting that the affordable housing goals of the GSEs did little to improve local homeownership rates or improve local housing conditions. The implicit expectation that improving access to credit for marginalized borrowers or areas would increase homeownership and in the process create healthier neighborhoods has not been supported by research.[51]

Yet the picture becomes more complex. There may be positive effects of "GSE crowd out." One study found that a ten percent increase in GSE market share corresponded to a 2.7% decrease in subprime market share, representing a potential cost savings of about $100 million.[52] Greater GSE activity was associated with a reduction of subprime activity in a neighborhood, and was also found to be more pronounced in neighborhoods with high concentrations of minority households. When contextualized with the findings that anywhere from 30-50% of subprime borrowers could have qualified for prime loans, growth in GSE activity may prove on balance, beneficial.[53] The study also found that increases in FHA market share corresponded to decreases in subprime market share, but with a smaller magnitude than that found with GSE market share. The negative relationship found between both GSE and FHA market share with subprime market share lends support for government involvement, in some form, in promoting *sustainable* homeownership opportunities for historically marginalized borrowers. This observation differs from the absence of significant effects on homeownership or housing market conditions when assessing GSE impact alone.

The relationship between subprime lending activity and GSE activity bears some emphasis. Not only have the Enterprises been targeted as one of the instigators of subprime lending in an effort to achieve their affordable housing goals—a charge which does not bear out in fact[54]—but their presence in the secondary mortgage market may actually serve to protect marginalized borrowers from the abuses of predatory lending. While the non-covered subprime market has collapsed, targeted affordable lending programs do work and offer alternatives for going forward. Research comparing community reinvestment loans facilitated under the CRA with prime-type characteristics performed better than subprime loans originated with a broker (thus originated outside the scope of regulations, and often carried excessively risky features, such as adjustable rates and prepayment penalties).[55] In fact, broker-originated loans with risky terms were four to five times more likely to default than community reinvestment loans.[56]

The Enterprises could take a lead role in encouraging sustainable non-prime or prime-type lending, similar to what private, federally insured depositories undertake through the CRA. Tighter regulations of the type or quality of subprime loans allowed to qualify towards affordable housing goals should also be re-instated and vigorously enforced.[57] For example, Immergluck (2004) discusses how though there were HUD restrictions eventually placed on the types of loans that Enterprises could include towards their LMI lending goals, and the Enterprises enacted voluntary restrictions on purchases of loans with certain features, these were not comprehensive enough to seriously limit the abuses visited on borrowers. The greater influence of the Enterprises in the secondary markets and these restrictions *could have* reduced the excessive pricing on subprime loans if these restrictions had been more comprehensive (across all abusive loan features) and more strict (lower 'thresholds' for what qualified as 'high cost'), because the Enterprises would not (hypothetically) purchase loans with certain features, and therefore independent mortgage companies had an incentive to make more responsible subprime loans if they wanted to improve their liquidity

One finding from research on Freddie and Fannie outcomes is that access to prime credit is not the only barrier—maybe even not the most important barrier—facing marginalized borrowers, or more accurately, different groups of marginalized borrowers. For example, the issue of mobility may be a substantial barrier for transient populations such as immigrants, given the high entry and exit costs of homeownership relative to renting.[58] Research indicates that interest rates—which have been a selling point of the GSEs—may have little influence on long run homeownership trends.[59] One study found no direct impact from interest rate changes on long run homeownership; changes in interest rates may change the timing of homeownership (accelerate it for some) but not the long term affordability of homeownership, and may increase housing starts in the short term.[60] A study assessing FHA lending found similar results—FHA lending was not found to *enable* homeownership for those who would never be able to buy but for the FHA, but rather, was found to accelerate it (or allow borrowers to consume more housing than they would be able to from conventional lenders).[61] The study also found that renters who qualified as "FHA only" borrowers waited years after qualifying for the FHA loan before purchasing homes. This lag between qualifying and purchasing may indicate that there are other barriers or considerations in homeownership beyond credit access. Results indicated that income and demographic factors may play a more important role in homeownership rates, and that these factors can be different for different racialized groups. For example, Painter et.al. (2000) found that differences in income, immigrant status, and education can fully explain the gap between Latino and white homeownership rates, but only part of the gap between Black and white homeownership rates. For the former group, interventions targeted at affordability and human capital may be more beneficial than credit policies.[62] This differentiates between access to credit and the cost of credit, finding that the cost of credit may not be directly as important a barrier to homeownership as other barriers, such as perpetual low income or less wealth, which may speak more to the continuing racial disparities in education, labor, and health. More generally, changes in interest rates—the cost of borrowing—will benefit those for whom the cost of credit is the main barrier,[63] but not impact borrowers struggling with the *cumulative* effects of marginalization. Therefore, lowering interest rates (i.e. the cost of borrowing) may improve access somewhat, but there are other remaining income and demographic factors that are critical for making homeownership a sustainable opportunity for these borrowers. Again, this suggests that we may not fully understand the pathways to homeownership that matter the most for targeted groups.

Policy decisions dictating Enterprise activity, for example the numeric levels at which the goals are set, have impacts on affordable housing goals of other market participants. Policymakers must consider the full range of impacts of Enterprise goals on these other participants' activities to mitigate the chance for 'substitution effects'—we want policies to complement each other, not to crowd each other out. For example, CRA (private market-oriented) and FHA (government-led) policies target similar borrowers as those in the Enterprise affordable housing goals. Research has indicated that one explanation for less-than-optimal homeownership outcomes from increased GSE activity is that this increased activity essentially substituted for FHA loans—the Enterprises were able to "cream" the best credit-quality borrowers who otherwise would have qualified for FHA loans; as a result, and faced with a higher risk pool, the FHA tightened its underwriting standards and reduced its loan volume.[64] Other research has indicated that the Enterprises lag other institutions in improving credit access to LMI borrowers, with possible explanations that this may be a result from increased enforcement of the CRA during the 1990s.[65]

The incentives under which the Enterprises operate—and the subsequent form they take—are critical, and offer a real leverage point for change. For example, research has indicated that although the Enterprises are meeting their housing quotas, the geography of their targeted borrowers tends to be more affluent neighborhoods that *just* qualify as an underserved area; activity may not be extending far enough into those neighborhoods that most need it to stabilize because it is more costly to do so, and so expected to have lower returns.[66] GSE shares tend to be lower in central cities, lower in tracts with the highest minority concentrations, and lower in tracts with high vacancy rates.[67]

Conclusion: Developing a Fair Housing Agenda for Fannie and Freddie

There is a clear disconnect between policy objectives and policy outcomes. As we have seen, there has been little to no net improvement in housing market conditions or homeownership rates for the intended beneficiaries, despite the fact that the Enterprises have been "successfully" meeting their affordable housing goals. It is also not clear the extent to which the crowd out effect posed by Enterprise activity harms or helps marginalized communities; on the one hand, they may crowd out subprime activity. On the other hand, they may crowd out FHA activity. And by most accounts, the Enterprises do not perform as well as other institutions in meeting the credit needs of these communities. These findings have several implications for developing an action plan for the Enterprises to affirmatively further fair housing.

First, we have about two decades or more of critique over not only their structure as GSEs, but of their performance in furthering fair housing; however, there has been no affirmative action plan developed in response to these criticisms. Research surrounding the housing market outcomes of GSE activity has for the most part stopped short of providing concrete solutions for affirmatively furthering fair housing, instead remarking upon the inadequacies of the current policies and structures.

Second, and related, although the Enterprises have more or less consistently met their affordable housing goals, there has been no demonstrable improvement in housing market outcomes for targeted groups. Not only have the Enterprises not been the best provider for meeting these goals—lagging other secondary market actors-- but their activities have generally not been shown to have positive impacts for their target populations (i.e. no positive effect on LMI homeownership; no positive effect on housing and neighborhood conditions). This is alarming because the research also indicates that the GSEs *are* being deemed successful in meeting the goals dictated to them. Again, it is important to note the geography of GSE activity. The analysis by An et.al. (2007) also showed that loan-purchase activity declines with tract median income (purchase activity at 35% for tracts with AMIs at 120%; falls to about 18% for tracts at 80% or below AMI) and purchase activity decreases as minority shares increases (about 30% for tracts with minority shares 30% or above; about 20% for tracts below 30% minority).[68]

Third, the Justice Department should be involved—the federal government is not doing enough to curb discrimination in lending. Because of the plenary authority to act on behalf of victims of housing and lending discrimination; the rampant abuses of lending agents (and the complicity of the Enterprises in these regard, who purchased "junk" private label securities of Wall Street investors)[69]; and the Enterprises' affirmative role in fair housing, it is crucial that the Justice Department act to curb and remedy the lending and housing situation in the United States. The Department must not only continue to investigate pattern and practice discrimination but also to use its discretionary power to join private discrimination suits under Title VIII. Housing and lending discrimination in violation of the Fair Housing Act leads to plummeting neighborhood housing values, loss of home equity, an uneven credit market for African American and other marginalized borrowers, and the continuation of discrimination and blocked opportunity for marginalized borrowers. This is clearly a problem of general public importance and must be addressed immediately. The Justice Department has the ability to address this and must continue to fight for the requirement to affirmatively further fair housing.

Finally, there is no coordinated, explicit focus on Fannie and Freddie reform as it pertains to affirmatively furthering fair housing. The Justice Department represents just one entry point for change—albeit an important one—but we would be well-served to highlight different intervention points in an effort to create a more robust advocacy platform. Such a position recognizes that affirmatively furthering fair housing objectives operate within a larger system of housing finance and affordable housing policies, both within and beyond the scope of Enterprise "jurisdiction." Within this system, there are several actors charged with the goal to provide fair housing. Policies directed at one actor will therefore necessarily interact with the activities and outcomes of policies directed at a different actor. Exploring these interactions, feedback loops, and rebound effects is critical for the design and implementation of a comprehensive, effective, and affirmative fair housing policy. Currently, the major actors within this system are not talking to each other. Our general observation is that while advocates agree that the restructuring of Fannie and Freddie is of critical importance, they feel there is too much else going on at the moment that takes precedence. For example, some are focusing their attention on CRA reform. We stress that these are not necessarily different issues, and neglecting one to focus on the other limits our opportunity to make significant inroads in addressing fair housing. This segmented approach sets the stage for incremental changes that essentially maintain the current overall structure of affordable housing, which in turn will continue to dictate less than optimal results. These are not independent reforms: changes in one area will have impacts in the other areas. Policymakers, experts, and advocates in each of these areas—CRA, FHA, and the Enterprises at a minimum—must be engaged together in a broader conversation about affirmatively furthering fair housing. To truly promote an affirmative fair housing agenda, especially as it relates to Fannie and Freddie, we must ensure that we keep a mindful balance between advocating for remedial actions pursued by the Justice Department, as well as developing affirmative and creative strategies that encourage the Enterprises to be leaders in fair housing and fair credit.

ATTACHMENT A, A REVIEW OF PROPOSED FORMS FOR THE ENTERPRISES

Following is a brief review of the proposed forms, their potential functions, and elements of regulatory structure and oversight.[70]

Proposal 1: Government Corporation. Functions would include focusing on purchasing qualifying mortgages and issuing MBS but eliminating mortgage portfolios, and transferring responsibility for homeownership to targeted groups to the Federal Housing Agency (FHA). Key elements of regulatory structure and oversight include: risk-sharing agreements with private lenders or mortgage insurers; appropriate disclosures in the federal budget of risks and liabilities (previously off-budget status as GSE); and robust congressional oversight of operations.

Proposal 2: Re-establish as GSE, for-profit with government oversight. Proposal calls for restoring the Enterprises to their pre-conservatorship status but with additional controls to minimize risk, such as eliminating or reducing the Enterprises' mortgage portfolios, or subjecting the Enterprises to public-utility type regulation (i.e. business activity restrictions and profitability limits) and establishing executive compensation limits. Another proposal calls for converting the Enterprises from publicly-traded, shareholder owned corporations to cooperative associations owned by mortgage lenders. Key elements of regulatory structure and oversight include reducing or eliminating portfolios to increase safety/soundness; establishing capital standards that reflect risks; additional regulations (i.e. executive compensation, or public utility- type regulations); financial disclosures in budget; and strong congressional oversight.

Proposal 3: Privatize. Proposal calls for abolishing the Enterprises in their present form and dispersing their mortgage lending activities and risk management throughout the private sector. Some propose the establishment of a federal mortgage insurer to help protect mortgage lenders against catastrophic mortgage losses. Key regulatory structure and oversight elements include: establishing an appropriate oversight structure for a new federal mortgage insurer, which might include appropriate regulations and capital standards, the disclosure of risks/liabilities in the federal budget, and congressional oversight.

ATTACHMENT B, TIMELINE OF FANNIE AND FREDDIE ROLES AND ACTIVITIES

Following is a brief review of important structural and mission-related changes through their history.[71] In setting up this timeline, however, it is critical to note the parallel history of housing discrimination in the United States, especially as it relates to the racialization of federal housing policy, as the Enterprises emerged within this context.

- **1933:** Home Owners Loan Act is passed, creating Home Owners Loan Corporation, in response to the foreclosure crisis precipitated by the Great Depression. HOLC was commissioned to buy mortgages of distressed borrowers, and refinance them into more affordable terms.[72] However, there was a clear racial impact, as HOLC developed a neighborhood ranking system for credit-worthiness of the housing it financed that favored white, homogenous, new neighborhoods over older, mixed, or African-American neighborhoods (regardless of income or age of dwellings).
- **1934:** The Federal Housing Agency (FHA) was created to provide government insurance to mortgage lenders. The precedent of overtly racist underwriting and appraisal practices, introduced under HOLA, were carried on by the FHA.[73] The FHA is credited with setting industry standards in underwriting and origination. Because the FHA employed discriminatory policies, the adoption of FHA practices facilitated the institutionalization of racial discrimination in housing finance in the private market.[74]
- **1938**: FHA created a national mortgage association, which would become Fannie Mae. During the late ‘30s and the ‘40s, duty to buy and sell FHA-guaranteed loans. In 1948 received authority to also buy and sell VA-guaranteed loans.
- **1954**: Fannie Mae chartered to provide liquidity in the secondary market, and provide support in times of economic stress. The Housing Act of 1954 also reorganized Fannie as a mixed-ownership corporation, with both the federal government and mortgage lenders as shareholders.
- **1950s** and **1960s**: limits on interest rates that thrifts could offer, and state regulations that limited banks’ ability to branch into different states, contributed to liquidity constraints on banks/thrifts and regional disparities in mortgage interest rates. Fannie’s ability to purchase nationwide alleviated these constraints.
- **1968**: Fannie was divided into two agencies. Ginnie Mae was created to guarantee (i.e. full faith and credit of US government) the FHA and VA loans from within HUD. Fannie was reorganized as a private, shareholder owned entity but with the federal charter overseen by HUD (i.e. a GSE), which included a general authority to require a “reasonable portion of mortgage purchases serve LMI borrowers.”
- **1970**: Freddie Mac was created to develop secondary market for conventional mortgage loans; owned by the Federal Home Bank Board.
- **1971-72**: Freddie created the first mortgage backed security. Fannie bought its first non-FHA/VA conventional loan.
- **Early 1980s**: Fannie experiences mortgage portfolio troubles from climbing interest rates (S&L failures); Fannie issues first MBS.
- **1989**: Freddie becomes publicly traded (GSE)

- **1992**: The 1992 GSE Act established OFHEO as independent oversight agency within HUD to ensure safety and soundness of the GSEs. Expanded the affordable housing mission by setting annual numeric housing goals, established by HUD. Three targets for the goals: purchase of mortgages serving LMI families; special affordable housing for families (i.e. families in low-income areas, and very low-income families); and housing located in central city, rural, and other “underserved” areas.
- **1990s**: Rapid growth of the Enterprises
- **2000s**: Housing bubble bursts, GSEs engage subprime markets; practice bad accounting; conservatorship.
    - **Early 2000s**: start buying Alt-A and subprime securities
    - **2003-04**: accounting scandals uncovered by OFHEO at both GSEs
    - **2008**: HERA passed, created FHFA
        - **September 2008**: FHFA as conservator of Fannie and Freddie; abolished OFHEO; HUD’s mission authority over affordable housing goals transferred to FHFA.
    - **2008-09**: Administration/FHFA use Fannie and Freddie to focus on mortgage affordability, mortgage availability, and foreclosure mitigation, in efforts to stabilize the housing market, through:
        - **i.** Foreclosure moratorium from November 2008-January2009
        - **ii.** Making Home Affordable Program[75]: helped develop with Administration, Treasury, and HUD. Designed to help prevent foreclosures for homeowners that qualify. Freddie is charged with servicer compliance; Fannie works with servicers to implement the program. The key elements of the program:
            1. Home Affordable Modification Program: loan modification guidelines and incentives for servicers, borrowers and lender/investors to engage in successful loan modifications
            2. Home Affordable Refinance Program: homeowners with conforming loans owned or guaranteed by Fannie Mae or Freddie Mac to refinance their loans into more affordable mortgages

Endnotes

[1] Andrew Jakabovics, Center for American Progress. "The Future of The Mortgage Market and the Housing Enterprises Testimony Before the US Senate Committee on Banking, Housing and Urban Affairs." October 9. 2009. Page 1. Available at

[2] William Apgar et. al. at the Joint Center for Housing Studies, Harvard University. "Credit, Capital and Communities: The Implications of the Changing Mortgage Banking Industry for Community Based Organizations." March 9, 2004 Report. Accessed at http://www.jchs.harvard.edu/publications/communitydevelopment/ccc04-1.pdf

[3] Supra n. 1, at 5.

[4] Remarks by Treasury Secretary Henry M. Paulson Jr. on the Role of the GSEs in Supporting the Housing Recovery before the Economic Club of Washington, January 7, 2009. Accessed September 23, 2009 at http://www.treas.gov/press/releases/hp1345.htm

[5] Timiraos, Nick. "Industry Seeks Fannie, Freddie Overhaul." *The Wall Street Journal* September 2, 2009. Accessed November 2, 2009 at http://online.wsj.com/article/SB125186013970178403.html

[6] The GSEs have three specific groups they are targeting: 'Underserved areas' (neighborhoods where income is less than 90% area median income, or where the share of minorities is at least 30% and AMI is 120%); 'low-to-moderate income borrowers' (borrowers having less than area median income); and 'special affordable borrowers' (borrowers who are low- or very-low income). The Secretary establishes the percentage of loans purchased that must qualify for one or more of these categories. For 2008 and 2009, for example, the new housing goals are: Low- and moderate-income housing goal, 43%; Special affordable housing goal, 18%; Underserved areas housing goal, 32%. Note: These percentages are lower than the housing goals initially established by HUD for the period 2005-2008 because of the current housing and economic conditions.

[7] United States Government Accountability Office. "Fannie Mae and Freddie Mac: Analysis of Options for Revising the Housing Enterprises' Long-term Structures." September 2009. Page 17

[8] *Id*. The 1992 Act also specified three target groups for the affordable housing goals:

[9]Duhigg, Charles. "Pressured to Take More Risk, Fannie Reached Tipping Point." *The New York Times*, October 5, 2008.

[10] Supra n. 7. at 7, stating "…the [E]nterprises incurred substantial credit losses on their retained portfolios and their guarantees on MBS. These losses resulted from pervasive declines in housing prices, as well as specific enterprise actions such as their guarantees on MBS collaterized by questionable mortgages, and their investment in Private Label MBS backed by subprime loans."

[11] The Housing and Economic Recovery Act 2008 is a comprehensive piece of legislation designed to address the housing market instability that became apparent throughout 2007, and markedly so during the early part of 2008. The Act includes provisions for housing finance reform (including reforms of federal housing regulatory agencies), foreclosure prevention provisions, and tax-related provisions.

[12] James B. Lockhart III (Director, Federal Housing Finance Agency) "Statement on the Appointment of FHFA as Conservator for Fannie Mae and Freddie Mac before the Senate Committee on Banking, Housing, and Urban Affairs." September 23, 2008. Page 3. Available at http://www.fhfa.gov/webfiles/17/92308FHFAHearingStatementcorrected092608.pdf

[13] James B. Lockhart III (Director of Federal Housing Finance Agency), "Statement on The Present Condition and Future Status of Fannie Mae and Freddie Mac before the House Financial Services Committee, Subcommittee on Capital Markets, Insurance, and Government Sponsored Enterprises." June 3, 2009. Page 8. Available at http://www.fhfa.gov/webfiles/2707/FHFA_Director's_Testimony_Final.pdf

[14] Supra n. 5.

[15] Supra n. 7, at 10. The Fed has provided similar support to Federal Home Loan Banks.

[16] To this end, three facilities were developed: (1.) Senior Preferred Stock Purchase Agreements, which provided an effective guarantee for investors of GSE obligations (any negative equity at either GSE will be offset by Treasury investment); support was initially capped at $200 billion for each GSE. Under this agreement, shares carry a 10% coupon, and a quarterly dividend payment as compensation for the commitment; limits were also placed on their portfolio size pursuant to this agreement, not to exceed $850 billion on December 31, 2009, and since lifted. (2.) GSE MBS Purchase Program, scheduled to expire 12-31-2009. (3.) GSE Credit Facility which allows the Enterprises to borrow funds if they are unable to issue debt in the financial markets, scheduled to end 12/31/2009 (as of September 2009, the Enterprises hadn't used this authority.)

[17] Timiraos, Nick. "Questions Surround Fannie, Freddie." *The Wall Street Journal.* December 30, 2009. Accessed January 6, 2010 at
http://online.wsj.com/article/SB10001424052748704234304574626630520798314.html?mod=dist_smartbrief
[18] Supra n. 13, at 4.
[19] Zigas, Barry. "What does the Future Hold for Fannie and Freddie?" *Shelterforce*, Fall 2009. Available at www.shelterforce.org/article/print/1769
[20] The Federal Reserve Board of Governors and the Federal Reserve Bank of St. Louis. "Innovative Ideas for Revitalizing the LIHTC Market." November 2009. Page 4. Available at
http://www.federalreserve.gov/communitydev/other20091110a1.pdf
[21] Supra n. 1, at 3
[22] Supra n. 7, at 41. HERA established a Housing Trust Fund, to be funded through assessments on Enterprises' unpaid principal balance on new business, equal to 4.2 basis points (or .042%). 65% of this assessment would go to HUD and the Trust Fund; 35% would go to Treasury's CDFI trust fund. However, given the current financial conditions of the Enterprises, and the economy in general, assessments have been stalled.
[23] 12 U.S.C. § 4545 (2009) (Stating that HUD shall "prohibit each enterprise from discriminating in any manner in the purchase of any mortgage because of race, color, religion, sex, handicap, familial status, age, or national origin, including any consideration of the age or location of the dwelling or the age of the neighborhood or census tract where the dwelling is located in a manner that has a discriminatory effect")
[24] *Id.* The Enterprises are also required by regulation to assist the Secretary in investigations of potential violations of the Equal Credit Opportunity Act (ECOA). Should violations of either FHA or ECOA be found, the Enterprises are instructed to take remedial actions against the violating lenders, "including suspension, probation, reprimand, or settlement".

[25] *Id.* (Stating that HUD must "periodically review and comment on the underwriting and appraisal guidelines of each enterprise to ensure that such guidelines are consistent with the Fair Housing Act . . .").
[26] Title VIII of the Civil Rights Act of 1968 requires that the U.S. Department of Housing and Urban Development (HUD) and all executive departments and agencies "affirmatively further the Fair Housing Act." 42 U.S.C. § 3608(d) (2008).

[27] 42 U.S.C. §§ 3612-3614 (2008).
[28] *Id.* at § 3613.
[29] *Id.* at § 3610.
[30] *Id.* at § 3612.
[31] UNITED STATES DEPT. OF JUSTICE – UNITED STATES ATTYS' OFFICE, U. S. ATTYS' MANUAL 8-2.180 (1997).
[32] *Id.* at 8-2.231.
[33] 42 U.S.C. § 3614 (2008).
[34] *Id.* at § 3613(e)
[35] *Id.*
[36] U.S. DEPT. OF JUSTICE – U.S. ATTYS' OFFICE, UNITED STATES ATTYS' MANUAL 8-2.231 (1997).
[37] Gotham, Kevin Fox. "Racialization and the State: The Housing Act of 1934 and the Creation of the Federal Housing Agency." *Sociological Perspective*, Vol. 34, No. 2: 291-371. Summer 2000. Page 306.
[38] *Id.*
[39] *Id.* at 307
[40] *Id.*
[41] Supra n. 1, at 4
[42] Kuttner, Robert. "The Bubble Economy." *The American Prospect.* September 24, 2007. Accessed April 24, 2009 at
http://www.prospect.org/cs/articles?article=the_bubble_economy
[43] Bocian, Debbie Gruenstein, Keith S Ernst, and Wei Li. "Unfair Lending: The Effect of Race and Ethnicity on the Price of Subprime Mortgages." Center for Responsible Lending. May 31, 2006. Page 3. Available at
http://www.responsiblelending.org/mortgage-lending/research-analysis/rr011exec-Unfair_Lending-0506.pdf
[44] Richard K. Green and Susan M. Wachter, "The Housing Finance Revolution," Prepared for the 31st Economic Policy Symposium: Housing, Housing Finance & Monetary Policy, Federal Reserve Bank of Kansas City. See p. 21 ff.
http://www.kansascityfed.org/publicat/sympos/2007/PDF/2007.08.21.WachterandGreen.pdf
[45] Jesus Hernandez, presentation on panel "Reverse Redlining, Foreclosure and the Wealth Gap" at The Kirwan Institute's National Convening Subprime Lending, Foreclosure and Race, October 2-3, 2008. Transcript available at
http://4909e99d35cada63e7f757471b7243be73e53e14.gripelements.com/pdfs/events/Panel_1_Transcript.pdf

[46] Jaffee, Dwight M. and John M. Quigley. “Housing Subsidies and Homeowners: What Role for Government Sponsored Enterprises?” January 2007. Presented at the Brookings-Wharton Conference on Urban Affairs, Washington DC, October 19-20, 2006.
[47] *Id.*
[48] The 1992 GSE Act defines ‘Underserved areas’ as those neighborhoods where income is less than 90% area median income, or where the share of minorities is at least 30% and AMI is 120%; ‘low-to-moderate income borrowers’ are defined as having less than area median income; and the ‘special affordable’ borrowers as those who are low- (incomes less than 80% AMI) to very low-income (incomes less than 60% AMI).
[49] Gabriel, Stuart and Stuart Rosenthal. “The GSEs, CRA, and Homeownership in Targeted Underserved Neighborhoods.” Paper presented at the Conference on the “Built Environment: Access, Finance, and Policy,” Lincoln Institute of Land Policy, Cambridge MA, December 7-8, 2007. The authors also observe that the limited effects of increased GSE activity on homeownership may be due to a ‘crowding out’ of the alternate, non-conforming loan market segment (i.e. increases in conforming loan sector are offset by decreases in the non-conforming sector).
[50] Bostic, Raphael W. and Stuart A. Gabriel. “Do the GSEs matter to low-income housing markets? An assessment of the effects of the GSE loan purchase goals on California housing outcomes.” *Journal of Urban Economics* 59: 458-475. 2006.
[51] Freeman, Lance, George Calaster and Ron Malega. “The Impact of Secondary Mortgage Market and GSE Purchases on Home Prices: A Cleveland Case Study.” *Urban Affairs Review* 42(2): 193-223. November 2006. Finding no significant relationship between secondary market purchasing rates of home-purchase mortgages and home prices for under-served census tracts in Cleveland, Ohio.
[52] An, Xudong and Raphael Bostic, “Have the Affordable Housing Goals been a Shield against Subprime? Regulatory Incentives and the Extension of Mortgage Credit.” Working paper with the School of Policy, Planning, and Development Lusk Center for Real Estate, University of Southern California, April 2006.
[53] *Id.* at 17, citing Carr and Scheutz (2001).
[54] Duhigg, Charles, “Pressured to Take More Risk, Fannie Reached Tipping Point.” *The New York Times,* October 5, 2009. Accessed September 29, 2009 at http://www.nytimes.com/2008/10/05/business/05fannie.html
The subprime market took off between 2001 and 2004, growing from $160 billion to $540 billion. Fannie did not make significant forays into the market until 2004/05; between 2005 and 2008, it purchased or guaranteed at least $270 billion in risky loans, almost three times over all previous years combined. In large part, this was in an effort to regain market share—and thus profits—lost to subprime lenders.
[55] Ding, Lei and Wei Lei. “Risky Borrowers or Risky Mortgages? Disaggregating Effects Using Propensity Scoring Methods.” Working Paper with Center for Community Capital, University of North Carolina, December 2008.
[56] *Id.* at 1.
[57] An article in *The Washington Post* also refers to remarks by Allen Fishbein, adviser to former Assistant HUD Secretary William C. Apgar that HUD failed to use its regulatory power to disallow the GSEs from counting subprime securities toward their affordable housing goals, “contrary to good lending practices.” Leonnig, Carol. “How HUD Mortgage Policy Fed the Crisis.” *The Washington Post* June 10, 2008. Accessed September 28,2009 at http://www.washingtonpost.com/wp-dyn/content/article/2008/06/09/AR2008060902626.html

[58] Painter, Gary and Christian L. Redfearn. “The Role of Interest Rates in Influencing Long Run Homeownership Rates.” *Journal of Real Estate Economics* 25(2/3): 243-267. 2002.
[59] *Id.*
[60] *Id.*
[61] Goodman, John L and Joseph B. Nichols, “Does FHA Increase Home Ownership or Just Accelerate It?” *Journal of Housing Economics* 6: 184-202. 1997.
[62] Supra n. 58, at 260.
[63] *Id.* at 249.
[64] An, Xudong and Raphael Bostic. “GSE Activity, FHA Feedback, and Implications for the Efficacy of the Affordable Housing Goals.” *Journal of Real Estate Finance and Economics* 36: 207-231. 2008.
[65] Freeman et.al., supra n. li, at 208, citing Evanoff and Segal (1996). See also Gabriel and Rosenthal (2008), who found that although the CRA and GSE affordable housing goals were both met, only the CRA activities had a positive impact on homeownership rates and mortgage lending activity.
[66] Bhutta, Neil. “GSE Activity and Mortgage Supply in Lower-Income and Minority Neighborhoods: The Effect of the Affordable Housing Goals.” Federal Reserve Board *Finance and Economic Discussion Series*, Division of Research & Statistics and Monetary Affairs. Working Paper, 2009-03. Stating that “insofar as these stable neighborhoods are a

relatively low priority for advocates, these results demonstrate how a broadly targeted GSE Act might interact with the GSE profit-motive to yield effects that are out of line with the intent of the law." Page 18.
[67] Supra n. 64, at 218.
[68] An, Xudong, Raphael Bostic, Yongheng Deng, and Stuart Gabriel. "GSE Loan Purchases, the FHA, and Housing Outcomes in Targeted, Low-Income Neighborhoods." Brookings-Wharton Papers on Urban Affairs: 2007.

[69] See Christopher L. Peterson, "Fannie Mae, Freddie Mac, and the Home Mortgage Foreclosure Crisis." Loyola University New Orleans Journal of Public Interest Law, Vol. 10, pp. 149-170, 2009. Private label securitization (PLS) on Wall Street took off during the 1990s; at that time, Fannie and Freddie steered clear of these securities that were backed by subprime and Alt-A loans. However, amidst declining market share, the GSEs both increased their presence in the subprime markets: in 1998, Freddie had purchased about $25 billion in PLS, and in 1997, Fannie had purchased only $18.5 billion. However, by the end of 2007, Freddie owned $267 billion in PLS, and Fannie owned $127.8 billion. Between 2003 and 2005 alone, the Enterprises' combined PLS holdings increased from 9.9% of their total combined mortgage portfolio, to 22% (162-163). It was the losses on these private label securities, backed by subprime and predatory loans, that ultimately necessitated the conservatorship of the Enterprises—some losing as much as 90% of their value from their date of purchase. Theresa R. DiVenti, "Fannie Mae and Freddie Mac: Past, Present, Future." *Cityscape: A Journal of Policy Development and Research*, Vol. 11, No. 3, pp. 231-242, 2009. Available at http://www.huduser.org/portal/periodicals/cityscpe/vol11num3/ch11.pdf
[70] Adapted from GAO report, supra n. 1, at 29-37.
[71] Adapted from GAO report, *Id.* at 11-12.
[72] Peterson, Christopher L. "Predatory Structured Finance." *Cardazo Law Review* Vol. 28, No. 5: 2185. 2007. Page 2195.
[73] *Id.*
[74] Fox Gotham, Kevin. "Racialization and the State: The Housing Act of 1934 and the Creation of the Federal Housing Administration." *Sociological Perspectives,* Vol. 43, No. 2, pp. 291-317.
[75] However, only 4% of loan modifications have made it past the trial modification phase of the program to a permanent loan modification. Renae Merle, "Foreclosure relief program is stuck in first: JUST 4 PERCENT IN FINAL STAGE: Thousands now risk losing mortgage help," *The Washington Post*, December 11, 2009. http://www.washingtonpost.com/wp-dyn/content/article/2009/12/10/AR2009121003834.html

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