



REGULATION & LEGISLATION

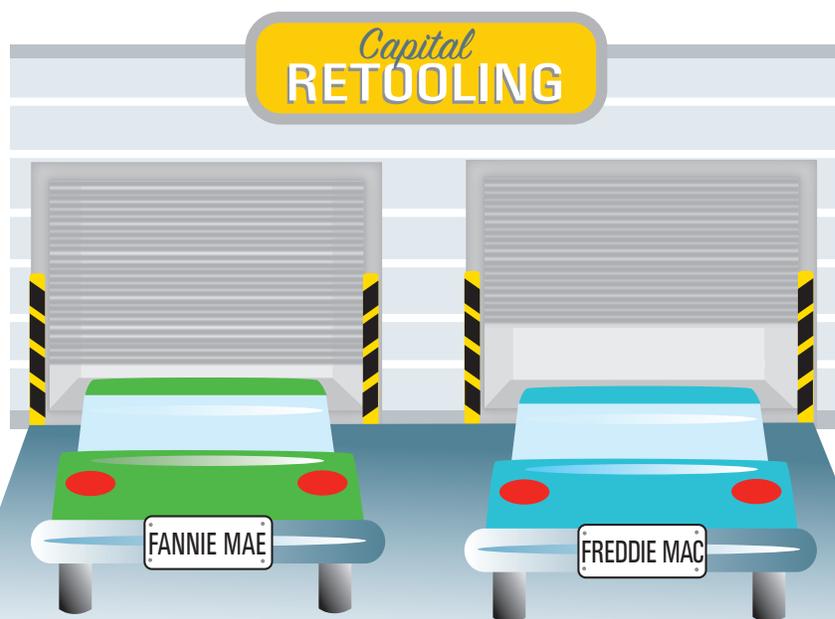
John J. McKechnie

Calabria Presses Ahead with Restructuring in Effort to End GSE Conservatorships

By John J. McKechnie

FHFA Director Mark Calabria spent last fall continuing his work on restructuring, recapitalizing, and eventually, releasing Fannie Mae and Freddie Mac from their 11-year conservatorships. These moves could have significant and far-reaching effects on the housing finance market—effects to which credit unions should pay close attention.

The first and arguably most important step is the soon-to-be released FHFA plan to recapitalize the failed mortgage giants. It will be a new regulation that sets capital requirements for Fannie Mae and Freddie Mac, and it will be proposed early this year. This means that FHFA is pushing back the timeline for releasing the companies from conservatorship—at one time, speculation was that the GSEs could exit government control in 2021. Now, there is a longer horizon.



According to sources at FHFA, the agency had deliberated for months over whether it would be able to make marginal changes to the capital rule proposed in June 2018 under former director Mel Watt, or whether it would need to start from scratch. Clearly, Calabria and his top advisors decided to go back to square one.

In several speeches, Calabria pointed to developments since the Watt Era—namely Treasury and FHFA's decision

in September to allow Fannie and Freddie to start retaining earnings—as the reason for going back to the drawing board.

“In fairness to all interested parties, the comments submitted during the previous rulemaking were submitted under a different set of assumptions about the future of the enterprises,” Calabria said in a statement. “During the process of the rulemaking, important issues were identified that will be addressed in the re-proposal.” The rule, he added, “will be finalized within a timeline fully consistent with ending the conservatorships.”

So, when will the conservatorships finally end? And what other reforms are being planned that will reshape the way Fannie and Freddie function when they do restart independent operations?

CAPITALIZATION PROCESS SEEN AS KEY

Again, the capitalization process is the key. In a mid-November press conference, Calabria said explicitly that, while he expects Fannie Mae and Freddie Mac to be out of government control by the time his term ends in 2024, that will not happen unless they hold sufficient capital. “I certainly hope and expect they will leave before I leave,” Calabria commented. “If they’re not ready, they’re not ready. And I’m not going to force them out.”

Calabria added that he expects initial public offerings from Fannie and Freddie in the next few years. “If all is going well, [in] 2021, 2022 we will see very large public offerings from these companies,” Calabria said during a speech to the Conference of State Bank Supervisors in November. “We will be allowing these companies to raise the capital they need so they can get out. That could tee up a conservatorship exit around 2022 or 2023.”

EXPECT NEW OR REVISED FHFA REGULATIONS

What the brave new post-Fannie/Freddie conservatorship world will look like is more difficult to determine. Calabria has provided no specific vision for future GSE activities, beyond his expectation that they will compete with private capital in a new secondary market.

But Calabria also says that the GSEs have a large number of supervisory issues that will be addressed through new or revised FHFA regulations. These include more rigorous and stringent appraisal standards, a response to expected changes in qualified mortgage (QM) underwriting policies, and FHFA guidance on how Fannie and Freddie will deal with the shift in interest rate benchmarks.

■ Specific to the appraisal issue, it is clear that Calabria believes that changes to Fannie/Freddie appraisal standards and practices have the potential to completely reshape the landscape of the appraisal industry. Because of that, Calabria said “I think it’s important that we press pause, that we do a request for information, that we hear from stakeholders such as those in the appraisal industry, and that we are thoughtful about how this transpires without simply saying go.”

■ FHFA has also been reviewing next steps regarding the Consumer Financial Protection Bureau’s Qualified Mortgage rule, which requires lenders to assess a borrower’s ability to repay. Fannie- and Freddie-backed loans are automatically deemed QM compliant. But that exemption, known as the QM patch, will sunset in January 2021, and the CFPB has said it intends to let the patch expire. The House of Representatives



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is considering legislation that would give lenders a choice between using Appendix Q, a set of unpopular standards cited by the CFPB for complying with the qualified mortgage rule’s 43% debt-to-income limit, and guidelines used by Fannie and Freddie that determine ability to repay. Senior FHFA staff say Calabria believes QM ultimately needs a legislative fix.

■ Calabria also said that he is also focused on transitioning Fannie and Freddie from the London Interbank Offered Rate (LIBOR) to a new benchmark. “If you ask me what topic I’ve spent more time on than I thought I would coming in, it’s LIBOR transition,” Calabria said. “LIBOR is going away. ... At some point in the middle of next year, we will instruct Fannie and Freddie to no longer purchase LIBOR [adjustable-rate mortgages].”

CALABRIA CHARTS DIFFERENT COURSE

Regardless of outcomes, the contrast between Director Calabria and his predecessors is apparent, and growing more so every day. “We plan to be a much more data-driven regulator than we did in the past,” Calabria said, noting that FHFA is currently lacking a sufficient number of Ph.D. economists. “If we can get data out that market participants and regulators find useful, we’re going to get it out.”

Amid all this uncertainty, one thing is certain: credit union mortgage lenders need to be agile and flexible as these changes play out. ▲

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