Regulation and Legislation

Complicated Washington Chessboard Awaits Housing Finance Reform

By John J. McKechnie

Like a very complex and ever-changing chessboard, it looks like a new dynamic for housing finance reform in the early days of the incoming Trump administration. ■ But how much are the issues involving housing finance and the credit union system really changing?

"Congress only works in two circumstances: consensus and crisis, and there is nothing resembling a consensus on what to do with the GSEs."

Here is a primer on the players and the issues to watch as President Trump and the Republicans on Capitol Hill try to enact an ambitious agenda that could reshape much of the financial services landscape.

TREASURY SECRETARY STEPHEN MNUCHIN

Former hedge fund manager Mnuchin wasted no time in making news just weeks after the election by signaling support for a change to the Fannie/Freddie status quo: "We will make sure that when they are restructured, they are absolutely safe and don't get taken over again. But we've got to get them out of government control."

Mnuchin expanded on these comments during his confirmation hearing in the Senate Finance Committee. During questioning Mnuchin said, "We shouldn't just leave Fannie and Freddie as is for the next four or eight years. ... It is my objective to find a bipartisan solution" to rebuilding Fannie Mae and Freddie Mac. "These are very important entities to provide the necessary liquidity for housing finance."

Mnuchin's statements are the first clear signal of the Trump administration's position on housing finance, and they differ from the stance taken by House Financial Services Chairman Jeb Hensarling and other Republicans who want to eliminate the GSEs altogether. Mnuchin added that he has "no interest" in re-establishing the companies in their original form.

Separately, sources close to the Trump presidential transition said a plan developed by former FHFA Acting Director Ed DeMarco appears to have gained traction with the incoming administration. The proposal would turn Fannie Mae and Freddie Mac into lender-owned insurers and expand Ginnie Mae's authority.

REP. JEB HENSARLING, SEN. MIKE CRAPO

Hensarling (R-Texas), the House Financial Services Committee Chairman, and Crapo (R-Idaho), the Senate Banking Committee Chairman, will set the timetable for whatever housing finance reform occurs in the 115th Congress. But there is little in the way of early agreement as to what reform legislation would look like.

Hensarling intends to pass a bill that winds down Fannie Mae and Freddie Mac over a five-year period and replaces them with private capital.

Crapo and Senate Republicans have advocated a more measured approach to GSE reform. Their plan, which was first passed with bipartisan support in 2013, would also do away with the conserved mortgage giants and replace them with a new, mutually-owned federal backstop.

Congressional observers do not expect housing finance reform to move through the legislative labyrinth until this fall at the earliest, with some suggesting that the trigger for action on Capitol Hill may not come until spring 2018, when Fannie/Freddie deplete their capital and could be compelled to ask Treasury for funds.

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FHFA DIRECTOR MEL WATT

A holdover from the Obama administration, in theory Watt will continue to serve until his term expires in January 2019. And while Watt has worked on building a common securitization

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platform (seen as paving the way to eventual merger of Fannie/Freddie), he has also been forthright in putting the ball of GSE reform squarely in Congress's court.

Watt presents a mixed picture. On one hand he has made statements suggesting FHFA would support a policy change that would permit Fannie and Freddie to rebuild capital while remaining under government control. On the other, in a late 2016 letter to housing industry trade groups, Watt said, "I continue to believe that conservatorship is not a desirable end state and that Congress needs to tackle the important work of housing finance reform."

Look for FHFA to continue its managerial role of the GSE conservatorships, and to defer to Congress and Treasury for direction on policy.

CFPB DIRECTOR RICHARD CORDRAY

Another Obama holdover, and arguably the most controversial agency head in the federal government, a Cordray-helmed CFPB will continue to make waves. The question is simply how much longer will Cordray be able to serve?

His term concludes in July 2018. However, a successful federal court challenge to CFPB means that Cordray's future hangs in the balance—if that court decision is upheld, President Trump could remove Cordray at will.

Cordray has stated his intent to finish his term, and consumer and liberal activist groups are circling the wagons in his defense.

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Another factor is Congress. The above-mentioned Hensarling bill that would reform Dodd-Frank contains a provision to create a five-member commission at CFPB. Democrats have vowed to resist this. Cordray and CFPB will present an early flashpoint.

Bottom line: The fundamental architecture of the U.S. housing finance system remains largely as it was before the 2008 crisis hit. Fannie and Freddie still exist, and combined with Ginnie Mae, these federal entities account for almost 98% of the market for new residential mortgage-backed securities.

At the time of the crisis, the continuation of this relative status quo would have been considered unthinkable. And while Congress and the new administration acknowledge the need for an end to the GSE conservatorships and a recasting of the roles for the various other players (including Ginnie Mae, FHA, and the Federal Home Loan Bank System), a general sense of inertia still prevails.

Congress and the administrations, both Obama and Trump, have been unwilling to alter what is widely considered to be a still fragile housing finance system.

There are two critical questions for credit unions to watch as D.C. policymakers grapple with possible reforms:

- How will any new system provide access for smaller financial institutions such as credit unions to a secondary mortgage market?
- What role can and should the federal government play in guaranteeing the existence of a healthy and vibrant secondary market that provides mortgage credit to a broad cross-section of mortgage market consumers?

The questions are obvious, the answers, elusive, as Washington turns the page to the Trump era.

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