STATEMENT OF

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(OFHEO)

ON THE
"GREEN RESOURCES FOR ENERGY EFFICIENT
NEIGHBORHOODS ACT OF 2008"

BEFORE THE COMMITTEE ON FINANCIAL SERVICES

UNITED STATES HOUSE OF REPESENTATIVES

JUNE 11, 2008

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Thank you for the opportunity to testify on the Green Resources for Energy Efficient Neighborhoods Act of 2008. I am the Chief Economist of the Office of Federal Housing Enterprise Oversight, the safety and soundness supervisor for Fannie Mae and Freddie Mac (the Enterprises). My testimony does not necessarily reflect the views of the President or the Secretary of HUD. OFHEO supports the broad goal of enhancing energy efficiency in American homes, but we have some reservations about diverting the Enterprises' focus from their current responsibilities.

This legislation would, among other things, broaden the mission of Fannie Mae and Freddie Mac to encompass the promotion of energy efficiency and conservation. Improved energy efficiency has long been a national priority, and opportunities for energy savings in housing include greater use of insulation, multi-paned windows, automatic setback thermostats, solar energy systems, reduced window areas, earth sheltering, and more efficient appliances, among others. Recent increases in the price of oil are strong reminders of the desirability of conserving energy and reducing dependence on fossil fuels.

Both Fannie Mae and Freddie Mac have had energy-efficient mortgage programs for a number of years. These programs expand their underwriting standards in two ways. First, energy-efficient improvements being made to a property at the time of a loan can be added to the appraised value or purchase price of the house. This allows for the financing of the improvements, with the funds held in escrow until the improvements are complete. Second, the reduced energy costs associated with documented energy-saving features of a house may be taken into account in assessing a borrower's ability to pay by adding the anticipated monthly savings to the borrower's income for the purpose of determining debt-to-income ratios.

These programs have met with little success over the years. The underwriting modifications do not often have a significant effect on whether a loan is approved, and the cost of obtaining documentation of energy savings may often offset the benefits.

This legislation seeks to dramatically increase the Enterprises' efforts by using both incentives and requirements associated with the housing goals currently administered by HUD. Section 4 of the GREEN Act elaborates a provision of H.R. 3321. It would provide at least 25 percent additional credit toward any goal, subgoal, or target for which a loan was otherwise qualified, if the property the loan finances meets any of a set of energy efficiency standards or if the borrower has reduced the energy consumption of the structure by at least 30 percent. Because the legislation specifies that the availability of this credit cannot be used by the regulator to increase the goal, the purchase of additional energy-efficient loans would mean easier-to-meet standards for affordable housing loans.

Section 6 of the bill would create new goals for energy-efficient and location-efficient mortgages. For this purpose, "energy-efficient" means loans underwritten to take into account energy savings of alterations or new construction when considering the adequacy of a borrower's income. This is potentially a broad definition, as it is not clear what minimal amount of energy savings are necessary to qualify. Some clarification of this could improve the chance for meaningful energy saving and lessen the likelihood of inefficient spending.

The goal for location-efficient mortgages might also benefit from greater clarity. The definition specifies loans for which borrower income has been augmented for qualification purposes by savings to be realized because the property location results in decreased transportation costs. This implies a comparison of the property in question with a standard, but it is unclear what kind of standard is intended. Proximity of public transportation or the borrower's distance from his or her employment site are possible choices, but any real savings would be dependent on the borrower's actual behavior, which may not involve any use of public transportation or, in the latter case, on the borrower remaining with the same employer. Imputing savings that do not actually occur could reduce underwriting accuracy, rather than achieve the desired improvement.

A third section directly affecting the Enterprises is Section 5. It would expand the Enterprises' purchase and guarantee authorities to include energy-efficient and location-efficient mortgages. As drafted, it would appear that the new authority would include loans in excess of the conforming loan limits, and loans in excess of 80 percent of property value that are not covered by mortgage insurance or other credit enhancements. Such authority would create considerable safety and soundness concern. If energy- and location-efficient loans are broadly defined, this could constitute a significant expansion of Enterprise charter authorities into areas with much more risk than is currently permitted.

The size of the losses the Enterprises have absorbed over the past year and their current importance to the successful function of our residential mortgage market recommend against substantial expansion of their risk-taking authority at this time. However, as Director Lockhart has said many times, these turbulent mortgage markets highlight the critical need for GSE reform legislation such as that passed by the House (H.R. 1427) with strong bi-partisan support in May and later incorporated into H.R. 3221. In the Senate last month, the Banking Committee passed similar legislation with a strong vote, and the full Senate is expected to act quickly. Both bills would combine OFHEO with the Federal Housing Finance Board to create a new, stronger regulator to oversee Fannie Mae, Freddie Mac, and the 12 Federal Home Loan Banks. This new regulator would be funded entirely by the Enterprises, separate from the annual appropriations process, be given the authority to set new capital standards for the entities it regulates, and otherwise have important powers of bank regulators, such as independent litigating authority and the power to establish a receiver. The bills would also combine in one agency the safety and soundness and mission oversight that are now divided between OFHEO and HUD. OFHEO greatly appreciates the strong sustained support for this legislation shown by Chairman Frank and the Members of this Committee.