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Comment Intake Mortgage Refinances and Forbearances RFI
Consumer Financial Protection Bureau
1700 G Street NW
Washington, DC 20552

Re: Mortgage Refinances and Forbearances RFI: Docket No. CFPB-2022-0059

To Whom It May Concern:

Thank you for the opportunity to submit comments to the Consumer Financial Protection Bureau on the Request for Information (RFI) regarding (1) ways to facilitate mortgage refinances for consumers who would benefit from refinancing, especially consumers with smaller loan balances; and (2) ways to reduce risks for consumers who experience disruptions in their financial situation that could interfere with their ability to remain current on their mortgage payments.

We write on behalf of The Pew Charitable Trusts, a non-governmental research and public policy organization dedicated to serving the public. We strive to improve public policy by conducting rigorous analysis, linking diverse interests to pursue common cause, and focusing on tangible results. In July 2020, The Pew Charitable Trusts launched its Home Financing project to study the dearth of small mortgages relative to the availability of low-cost site-built and manufactured homes, and the alternative arrangements some people use instead to purchase homes when mortgages are not accessible.

Mortgages are the most common way for Americans to finance their home, but research shows that only about one-third of low-cost homes are financed with mortgages. Due in part to the lack of small mortgages, some borrowers turn to alternative arrangements—such as personal property loans for manufactured homes, lease purchase agreements, and land contracts—to finance their home purchases. While some households have successfully converted to homeownership using these arrangements, alternative financing often comes with added risks for buyers, including hidden costs, the threat of eviction, and a loss of equity. Additionally, in some of these arrangements, the buyer lacks clear ownership of the property.

This comment letter will focus on ways to facilitate refinances for small mortgage borrowers and, more specifically, borrowers who would benefit from refinancing their alternative arrangements into small mortgages. Updates to the rules surrounding refinancing present an opportunity to improve access to safe, affordable home financing to low- and moderate-income families that want to purchase low-cost homes.

In general, we encourage the Bureau to recognize the substantial benefits of small mortgages in the banking system. We also recommend that the Bureau expand its focus on beneficial refinances to include borrowers using alternative financing arrangements. Doing so may require a better understanding of who uses alternative financing, their pathway into those arrangements, and their experiences and outcomes.

Pew's responses to several of the questions from the Bureau appear in the following pages. Though we are limiting our comments to issues related to refinancing of small mortgages and alternative financing, we look forward to continuing to engage the Bureau, lenders, and other stakeholders on these issues and others as we release new research. Thank you again for the opportunity to comment on this Request for Information and for undertaking this essential work.

Sincerely,

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Our comments will broadly focus on the following questions:

Barriers to refinancing

1. What barriers may prevent consumers from accessing falling interest rates through refinancing and what solutions could lower those barriers, particularly for consumers with smaller loan balances? Are there particular issues in obtaining refinances or would any particular approaches be more effective for certain types of homeowners, such as servicemembers, older adults, and first-time homeowners
2. To what extent do large fixed costs of refinancing and limited profitability for smaller loan balances limit beneficial refinances? What potential policies could lower costs for beneficial refinances

Targeted and streamlined refinances

1. How can the Bureau support industry efforts to facilitate beneficial refinances through targeted and streamlined refinance programs?
2. What are the current barriers to widespread use or promotion of existing refinance programs and, relatedly, what features of refinance programs are important to promoting widespread use?

Home purchase and refinance loans under $150,000 are in short supply

Accessing safe and affordable mortgages is a key step to achieving homeownership and the traditional fixed-rate mortgage is regarded as the gold standard in home financing. To date, most of Pew's work has examined mortgage originations, but many of the challenges, opportunities, and lessons learned have implications for mortgage refinances.

The share of small mortgage originations, including both purchase and refinance loans, has fallen sharply over the last decade. According to the Urban Institute, new mortgages with balances between $10,000 and $70,000 fell by 17% between 2009 and 2016, while loans between $70,000 and $150,000 fell by 1%.[1] In contrast, loans between $150,000 and $300,000 increased by 61%. The U.S. Department of Housing and Urban Development (HUD) found a similar trend in refinances for mortgages with balances below $70,000. Originations of these loans fell by more than half between 2009 and 2020.[2]

Rising home prices can explain some of these changes. The average purchase price of a single-family residence has more than doubled since 2011, which has reduced the number of low-cost homes available for purchase.[3] Still, many parts of the country contain a significant stock of low-cost housing, particularly in rural areas of the Southeast, Middle Appalachia, Texas, and the Great Plains, as well as older industrial areas in the Midwest and urban areas throughout the South.[4] In these regions and others, hundreds of thousands of homebuyers have purchased low-cost properties in recent years.[5] However, these buyers often struggle to obtain mortgage financing. Data from Urban Institute shows that low-cost homes are less likely to be sold with mortgages[6] and that small mortgages are denied more frequently than larger mortgages.[7]

The lack of small mortgages stems from lenders' inability to profitably originate those loans

To better understand the shortage of small mortgages, Pew conducted a series of interviews with mortgage lenders. As part of those interviews, lenders identified several structural and regulatory barriers that inhibit small mortgage originations. Two of the most significant barriers identified were the high fixed cost of mortgage origination and the structure of loan officer compensation.

High fixed lending costs are a significant barrier to small mortgage originations. The major cost drivers of originating a loan are labor, technology, compliance, and appraisal fees. These costs tend to be roughly the same, regardless of loan size. In contrast, the revenue lenders earn increases with loan size, which makes it far more profitable for lenders to originate large mortgages than small mortgages. Regulatory

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[1] A. McCargo et al., "Small-Dollar Mortgages for Single-Family Residential Properties" (Urban Institute, 2018), 2, https://www.urban.org/research/publication/small-dollar-mortgages-single-family-residential-properties.
[2] U.S. Department of Housing and Urban Development, "Financing Lower-Priced Homes: Small Mortgage Loans" (2022), 2-3, https://www.huduser.gov/portal/portal/sites/default/files/pdf/Financing-Lower-Priced-Homes-Small-Mortgage-Loans.pdf.
[3] U.S. Federal Housing Finance Agency, Purchase Only House Price Index for the United States [HPIPONM226S], retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/HPIPONM226S, November 21, 2022.
[4] U.S. Department of Housing and Urban Development, "Financing Lower-Priced Homes," 7.
[5] McCargo et al., "Small-Dollar Mortgages for Single-Family Residential Properties," 3. Urban Institute found that in 2015, more than 643,000 homes sold for $70,000 or less.
[6] Ibid., 3-4.
[7] L. Goodman, B. Bai, and W. Li, "Real Denial Rates: A Better Way to Look at Who Is Receiving Mortgage Credit" (working paper, Urban Institute, 2018), 19-20, https://www.urban.org/sites/default/files/publication/98823/real_denial_rates_1.pdf.

requirements add to the cost of originating small mortgages and, in some cases, limit lenders' flexibility to provide tailored small mortgage products. For instance, the Bureau's ability-to-repay/qualified mortgage rule (ATR-QM rule) increased mortgage origination costs by an estimated $139 per loan.[8] Although lenders passed some of these costs onto borrowers in the form of origination charges and fees, they retained an estimated $95 of the added costs. On the margin, these added costs may serve as a disincentive for lenders to make additional small mortgages.

The structure of loan officer compensation may also limit the incentive for lenders to originate small mortgages. Lenders have cited the Bureau's Loan Originator Compensation rule, which prohibits compensation adjustments based on a loan's terms or conditions, as a barrier.[9] The rule is designed to protect consumers by reducing the ability for loan originators to steer consumers into loans with excessively high interest rates and fees.[10] However, lenders state the rule also prevents them from offering variable compensation to loan officers, which could create incentives to serve the small mortgage market. Pew does not yet have data to know how the Loan Originator Compensation rule has impacted the ability of borrowers to obtain a small mortgage. We encourage the Bureau to evaluate these concerns as it continues to examine how best to protect mortgage seekers while also ensuring they have sufficient access to affordable financing.

Although these barriers were identified in the context of home purchase mortgages, the same barriers likely affect small mortgage refinances. Disincentives created by loan officer compensation structures also likely extend beyond the home purchase market and into the refinance market. Furthermore, much like the home purchase market, research suggests that small mortgage refinances cost proportionally more than large mortgage refinances.[11]

However, the availability of small mortgage refinances may be affected by other factors that do not impact the home purchase market. For example, lenders often charge higher interest rates on small mortgage non-cash out refinance loans than on similar large balance loans.[12] A lesser rate reduction coupled with similar upfront fees means that refinances may be less beneficial for some small mortgage borrowers.

When small mortgages are unavailable, some borrowers instead use riskier, costlier alternatives

Borrowers who do not use mortgages must either purchase their home using cash or alternative financing or forgo homeownership. Cash purchases have become increasingly common in recent years

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[8] R. Chrisman and M. Lind, "Regulatory Outlook 2018 Report: Ability to Repay and Qualified Mortgage Regulations" (Stratmor Group, 2018), 3-4, http://www.stratmorgroup.com/wp-content/uploads/STRATMOR-Insights-April-2018.pdf.
[9] Mortgage Bankers Association, "Mba Members Urge Bureau to Change Loan Originator Compensation Rule," *MBA Newslink*, Oct. 24, 2018, https://newslink.mba.org/mba-newslinks/2018/october/mba-newslink-wednesday-10-24-18/mba-members-urge-bureau-to-change-loan-originator-compensation-rule/.
[10] Loan Originator Compensation Requirements under the Truth in Lending Act (Regulation Z), 78 Fed. Reg. 11279-427 (Feb. 15, 2013).
[11] K.P. Brevoort, "Do Low Mortgage Balances Limit Refinancing Opportunities?" (Board of Governors of the Federal Reserve System, 2022), 12, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4163151.
[12] Ibid., 18.

and currently account for about one-quarter of all home sales.[13] Most homebuyers, however, lack the financial resources to pay for their home using cash, so cash buyers tend to be wealthy individual and institutional investors who have greater access to capital.[14]

Alternative financing arrangements, which include personal property loans, lease-purchase agreements, and land contracts, are sometimes used when mortgage financing is unavailable.[15] Research from the Federal Reserve has shown that neighborhoods with less access to mortgage financing tend to have higher incidence of land contracts than comparable neighborhoods with greater mortgage access.[16] That research also determined that the median land contract property was valued at just $75,000—a price point that could otherwise be served by small mortgages.

To better understand where alternative financing exists and how many people have used these arrangements, Pew conducted a first-of-its-kind national survey of borrowers using alternative financing. The survey revealed that 36 million Americans have used alternative arrangements at some point in their lives—22% of them more than once—and that 7 million Americans are currently using these arrangements to finance their home purchases.[17]

The survey found that low-income households with annual incomes under $50,000 are 7 times more likely to use alternative financing than those earning $50,000 or more.[18] Among racial and ethnic groups, Hispanic borrowers are 1.5 times more likely to use alternative financing as borrowers nationally.[19] Roughly 34% of Hispanic households and 23% of Black households have ever used alternative financing, compared to just 19% of White households.[20] The disparities in the usage of alternative financing arrangements likely reflect longstanding inequities in the broader home financing system. The survey also revealed that personal property loans (also known as "home only" or "chattel" loans) used to purchase manufactured homes are the most common form of alternative financing. About 11% of home borrowers have used these loans to purchase manufactured homes.[21]

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[13] National Association of Realtors, "Realtors Confidence Index" (2022), https://cdn.nar.realtor/sites/default/files/documents/2022-09-realtors-confidence-index-10-20-2022.pdf.

[14] T. Malone, "Single-Family Investor Activity Bounces Back in the First Quarter of 2022" (CoreLogic, 2022), https://www.corelogic.com/intelligence/single-family-investor-activity-bounces-back-in-the-first-quarter-of-2022/.

[15] The Pew Charitable Trusts, "What Has Research Shown About Alternative Home Financing in the U.S.?" (2022), 1-3, https://www.pewtrusts.org/en/research-and-analysis/issue-briefs/2022/04/what-has-research-shown-about-alternative-home-financing-in-the-us.

[16] A. Carpenter, T. George, and L. Nelson, "The American Dream or Just an Illusion? Understanding Land Contract Trends in the Midwest Pre- and Post-Crisis" (Joint Center for Housing Studies of Harvard University, 2019), 8, https://www.jchs.harvard.edu/sites/default/files/media/imp/harvard_jchs_housing_tenure_symposium_carpenter_george_nelson.pdf.

[17] The Pew Charitable Trusts, "Millions of Americans Have Used Risky Financing Arrangements to Buy Homes" (2022), 4-6, https://www.pewtrusts.org/en/research-and-analysis/issue-briefs/2022/04/millions-of-americans-have-used-risky-financing-arrangements-to-buy-homes.

[18] Ibid., 7.

[19] The Pew Charitable Trusts, "Hispanic Homebuyers Most Likely to Use Risky Financing; New Survey Sheds Light on Use of Alternative Financing among Latino Households," April 27, 2022, https://www.pewtrusts.org/en/research-and-analysis/fact-sheets/2022/04/hispanic-homebuyers-most-likely-to-use-risky-financing.

[20] The Pew Charitable Trusts, "Millions of Americans Have Used Risky Financing Arrangements to Buy Homes," 6-7.

[21] Ibid., 5-6.

Alternative financing users would benefit from refinancing into mortgages, but face steep challenges

In most cases, borrowers using alternative financing arrangements would be better with mortgages given the differences in costs and consumer protections. Pending Pew research indicates that some borrowers using alternative financing could otherwise afford mortgages. In fact, many alternative financing arrangements have higher costs than traditional mortgages. For example, personal property loan borrowers have interest rates that are nearly 4 percentage points higher than manufactured housing homeowners with mortgages.[22]

Besides reducing borrowing costs, refinancing alternative arrangements into mortgages could also strengthen homeownership protections for borrowers. For example, in land contracts and lease purchases, the buyer lacks clear ownership of the property either because transactions are not recorded or because the seller—rather than the buyer—holds the property title. The legal ambiguity creates uncertainties about which party is responsible for paying property taxes and addressing maintenance or repair issues. The lack of clear ownership rights also limits the extent to which buyers can accrue equity in their homes.

Finally, mortgages offer substantially more consumer protections than alternative arrangements. Most states do not provide substantive consumer protections for those using alternative arrangements.[23] This can lead to a host of issues for buyers, including inflated sales prices, above-market interest rates, hidden costs or fees, substandard housing quality, the inability to receive the title at the end of the contract, few jurisdictions that require pre-sale appraisals, lack of disclosure about existing liens, and increased risk of eviction or foreclosure.[24]

Borrowers using alternative arrangements face many barriers to refinancing. For one, alternative arrangements are often used to purchase homes with lower property values. As previously noted, lenders are reluctant to originate small mortgages to finance lower-priced properties, whether the loan is for purchase or refinance.

The characteristics of alternative financing borrowers are also heavily tilted toward groups that are unlikely to refinance. Alternative financing is disproportionately used by racial minorities, low-income households, and owners of manufactured homes. Research has shown that Black and Hispanic borrowers face challenges refinancing in part because of inadequate credit scores, equity, and income.[25] Similarly, many Black and Hispanic borrowers lack the liquid assets necessary to afford the closing costs

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[22] Consumer Financial Protection Bureau, "Manufactured Housing Finance: New Insights from the Home Mortgage Disclosure Act Data" (2021), 25, https://files.consumerfinance.gov/f/documents/cfpb_manufactured-housing-finance-new-insights-hmda_report_2021-05.pdf.

[23] National Consumer Law Center, "Summary of State Land Contract Statutes" (2021), 3-4, https://www.pewtrusts.org/en/research-and-analysis/white-papers/2022/02/less-than-half-of-states-have-laws-governing-land-contracts.

[24] The Pew Charitable Trusts, "Alternative Home Financing in the U.S.," 6.

[25] K. Gerardi, P. Willen, and D.H. Zhang, "Mortgage Prepayment, Race, and Monetary Policy" (working paper, Federal Reserve Bank of Boston, 2020), 19, https://www.bostonfed.org/publications/research-department-working-paper/2020/mortgage-prepayment-race-and-monetary-policy.aspx.

that must be paid in order to refinance.[26] For many of the same reasons, low-income borrowers are less likely to refinance than high-income borrowers.[27]

Personal property loan borrowers face additional unique barriers to refinancing. These loans are typically used to purchase homes not titled as real estate, which render those properties ineligible to receive mortgage financing. Although personal property loans are still eligible for rate and term adjustments, few borrowers are able to take advantage of this opportunity in practice. In 2019, just 4% of personal property loans were refinanced compared with 44% of mortgages for site-built homes and 33% of mortgages for manufactured homes. As noted by the Bureau in their whitepaper, more research is needed to understand why so few personal property loans are refinanced.[28]

The Bureau's role in expanding beneficial refinances for alternative financing borrowers

In recent years as average interest rates fell below 3%, some borrowers had opportunities to refinance their loans. For some, this helped them sustain homeownership–particularly during the pandemic when many households were impacted by wage losses–by reducing their monthly payments and defaults and, by extension, increasing their monthly savings and improving their financial position.

However, access to refinancing was inconsistent across eligible homeowners. The shortage of small mortgage refinancing opportunities affects not only those already in mortgages, but also those looking to move out of costly and risky alternative financing arrangements.

Currently, there are programs at the federal level that help homebuyers refinance land contracts into mortgages. For example, land contracts executed at least 12 months prior to application are eligible for "no-cash out" refinancing by Fannie Mae, provided the loan-to-value ratio is determined by dividing the new loan amount by the lesser of the total acquisition cost (defined as the purchase price indicated in the land contract, plus any fully documented costs the purchaser incurred for rehabilitation, renovation, or energy conservation improvements) or the appraised value of the property at the time the new mortgage loan is closed.[29] Freddie Mac provides a similar no-cash out refinance loan for land contracts executed 12 months prior to the application for refinance, provided the loan-to-value ratio is calculated using the current appraised value of the property and the borrower provides third-party documentation evidencing payments in accordance with the land contract for at least 12 months.[30] The Federal Housing Administration (FHA) will insure refinancing to pay off recorded land contracts and the unpaid principal balance will be deemed to be the outstanding balance on the recorded land contract.[31] Apart from the specific provisions for determining property values, lenders follow the general guidelines for refinancing mortgages provided by Fannie Mae, Freddie Mac, and FHA. We encourage the Bureau to work with

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[26] Federal Reserve Board, Survey of Consumer Finances, 2019, https://www.federalreserve.gov/econres/scfindex.htm. According to the Federal Reserve, about 59% of Hispanic borrowers, 53% of Black borrowers, and 32% of White borrowers had less than $5,000 in liquid assets.
[27] S. Agarwal et al., "Refinancing Inequality During the Covid-19 Pandemic" (working paper, Federal Deposit Insurance Corporation, 2021), 28-30, https://www.fdic.gov/analysis/cfr/working-papers/2021/cfr-wp2021-08.pdf.
[28] Consumer Financial Protection Bureau, "Manufactured Housing Finance," 4.
[29] Fannie Mae, "Selling Guide," accessed Nov. 8, 2022, https://selling-guide.fanniemae.com/Selling-Guide/Origination-thru-Closing/Subpart-B2-Eligibility/Chapter-B2-1-Mortgage-Eligibility/Section-B2-1-3-Loan-Purpose/1032989481/B2-1-3-05-Payoff-of-Installment-Land-Contract-Requirements-11-13-2012.htm.
[30] Freddie Mac, "Seller/Servicer Guide," accessed Nov. 8, 2022, https://guide.freddiemac.com/app/guide/section/4404.1.
[31] U.S. Department of Housing and Urban Development, "Fha Single Family Housing Policy Handbook 4000.1" (2022), https://www.hud.gov/program_offices/housing/sfh/handbook_4000-1.

other agencies to examine refinancing requirements for land contract borrowers and determine if there are opportunities to streamline the pathway from land contracts into mortgages.

Pew encourages the Bureau to consider targeted and streamlined refinance programs that could increase refinancing opportunities for borrowers using small mortgages and alternative arrangements. Such programs have been used to facilitate beneficial refinances through reduced underwriting and documentation requirements, which can lower the transaction costs of refinancing and help borrowers reduce their interest rates and monthly payments. For example, as others have noted, there are important takeaways from the Home Affordable Refinance Program (HARP) that supported homeowners with mortgages during the Great Recession. In short, the reduction in monthly mortgage payments led to fewer defaults.[32]

The Bureau could also facilitate the creation of new products that enable refinancing of alternative arrangements. For example, the Texas Department of Housing and Community Affairs has a program that offers financing for local governments, public housing authorities, and nonprofits to convert contracts for deed into traditional mortgages.[33] The program enables refinancing coupled with either reconstruction or new construction of site-built housing, replacement of an existing manufactured home, or rehabilitation of housing in communities along the Texas-Mexico border. Streamlining mortgage lending requirements for programs like this one could significantly reduce costs for lenders and improve access to financing, especially for specific communities that rely heavily on alternative financing and have been historically underserved in the mortgage market.

Thank you again for the opportunity to comment on this request for information and provide data on small mortgage refinances. We look forward to continuing to engage on these topics with the Bureau as our work develops.

[32] Urban Institute, "A Streamlined Home Refinancing Program Would Lower Monthly Payments and Prevent Defaults," *Urban Wire* (blog), April 8, 2021, https://www.urban.org/urban-wire/streamlined-home-refinancing-program-would-lower-monthly-payments-and-prevent-defaults; Douglas A. McManus, Kadiri Karamon, and Jun Zhu,, "Refinance and Mortgage Default: A Regression Discontinuity Analysis of Harp's Impact on Default Rates," *Journal of Real Estate Finance and Economics* 55, no. 4 (2018), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3074635.https://www.urban.org/urban-wire/streamlined-home-refinancing-program-would-lower-monthly-payments-and-prevent-defaults

[33] Texas Department of Housing and Community Affairs "Contract for Deed (Cfd) Program," accessed Nov. 8, 2022, https://www.tdhca.state.tx.us/home-division/cfdc.htm.