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The Honorable Shaun Donovan
Secretary
U.S. Department of Housing and Urban Development
451 7th Street SW
Washington, DC 20410

The Honorable Mel Watt
Director
Federal Housing Finance Agency
400 7th Street SW
Washington, DC 20024

Dear Secretary Donovan and Director Watt:

I am writing to bring to your attention the recent increase in investor owned rental properties and the development of single family rental backed securities and ask that your agencies address unanswered questions about these new financial products. Part of the mission of the Department of Housing and Urban Development and the Federal Housing Finance Agency is to promote quality, affordable housing and to strengthen the nation's housing market as a whole. I believe that your offices are perfectly positioned to provide further details on these new financial products and the impact they could have on homeowners and renters.

California's Inland Empire, which I represent, was hit particularly hard by the wave of foreclosures that occurred as a result of the financial crisis. Between 2008 and 2011, Riverside County saw 134,910 household foreclosures – a rate of one in every ten homes. After the flood of foreclosures, the Inland Empire housing market has seen record low prices and interest rates. Despite these strong incentives to buy, families and first-time homebuyers are finding it hard to purchase a home. It is increasingly the case that these homes are being purchased by investment companies looking to rent out the property, leaving the family purchaser of modest means shut out of the market. Many of the properties were distressed or real estate owned (REO) before institutional investors purchased them and converted them to rentals. While Southern California provides a clear example of this new trend, it is not the only region that has seen a rise in investment owned properties. Similar stories are coming out of Florida, Arizona, Nevada, and Georgia.

Now, these same investors have developed a new financial product linked to rental properties, a single family rental backed security. Last fall, Blackstone partnered with Deutsche Bank to announce the first rental backed security, offering $479 million in bonds backed by the rental income from some 3,207 properties in Arizona, California, Florida, Georgia, and Illinois. At the end of January, another large investor, American Homes 4 Rent announced a partnership with JPMorgan Chase, Goldman Sachs and Wells Fargo to sell $500 million in similar bonds. If these offering are successful, more firms may be encouraged to follow Blackstone and American Homes 4 Rent's lead. According to a report by the Center for American Progress, the market for rental backed securities could grow to $70 billion by 2016.

The Federal Reserve as well as a few ratings agencies raised concerns about these new bonds. Moody's Analytics gave the bonds in the highest traunch a Triple-A rating, but Fitch and Standard & Poor's refused to give the bonds a Triple-A rating, citing their limited track record and vulnerability due to the intricacy of maintenance expenses, capital expenditures, property tax fluctuation, and the potential for local municipality involvement. Additionally, a report by economists at the Federal Reserve raised concerns about the impact of rental backed securities on local housing markets where a majority of the properties are located, and argued that, "it will be important to monitor the development of markets for bonds backed by rental-income streams for the development of potentially destabilizing structures or concentrated exposures."

The issues raised by Fitch Ratings and the Federal Reserve point to possible risk that could harm renters and local housing markets if these bonds are affected by a downturn. It is with that in mind, that I request that the HUD and the FHFA gather additional information about these new financial instruments. I would hope that information would include:

1. A list of local housing markets with high concentrations of rental properties linked to rental-backed securities, and analysis of common trends within these communities.
2. The impact of REO to rentals and rental backed securities on mortgage credit availability, rental prices, and housing prices in highly impacted communities.
3. Detailed information about the impact of large investor purchasers on first-time homebuyers' ability to enter the market.
4. An evaluation of trends in FHA approved mortgages in impacted communities.
5. A comparison between the rehabilitation, ongoing maintenance, and management costs that large investors spend on REO to rental properties with other actors, and how that impacts local neighborhoods.
6. An evaluation of the impact of REOs to rentals on neighborhood engagement and safety.
7. Analysis of the impact of a mass selloff of REO to rentals on local, state, and national housing markets.
8. Performance data from the Distressed Asset Stabilization Program including how many loan modifications, short-sales, deeds-in-lieu and foreclosures occurred among the distressed notes sold to investors in the 2012 and 2013 national and neighborhood stabilization outcome DASP pools.
9. Share performance data from the FHFA's 2012 REO-to Rental pilot program including current vacancy rates, average rents, changes in property values, and an assessment of the quality of property management.

Proper oversight of new financial innovations is key to ensuring we don't go down the same road of the unchecked sub-prime mortgage backed security, and create an unsustainable bubble that will wreak havoc when it bursts. I encourage HUD and FHFA to collect data on rental backed securities so that all parties can have a thorough understanding of the potential risks associated with these bonds. For further information, please contact Amanda Eaton, on my staff, at 202-225-2305.

Sincerely,

Mark Takano
Member of Congress