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FANNIE MAE & FREDDIE MAC REFORM

Before FHA was created in 1934, mixed-use development was quite common. Mixed-use commercial streets - Main Streets - were common partly because lenders appreciated that risk was spread over different types of real estate. For example, a flower shop with an apartment above provided two sources of income. One might perform well when the other was not. But now lenders look at mixed-uses as adding risk - "one use or the other could fail so better not to allow it at all." As a result, the signal to investors and developers is if you want financing, better not allow mixed-use.

Despite this regulatory stance, in recent years mixed-use developments have steadily gained popularity. We know this not so much from new development, but rather from the demographic trends that show attraction to existing urban and suburban places with housing, retail and commercial property in close proximity.

New development has not served this demand partly because of federal policies and practices that discourage mixed use-settlement. Specifically FHA, Fannie Mae, Freddie Mac, and HUD's 221d4 program all limit non-residential to 20% (25% in Freddie Mac's case) of the total value or imputed rent of a given development. Combined with the tendency of private lenders to copy federal underwriting rules, this excludes almost all of America's pre-World War II Main Streets from the secondary mortgage markets and from HUD's capital program for rental housing. It also excludes live/work units - a newer form popular in Europe and Canada - from benefiting from the federal or federally chartered programs.

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Especially in these uncertain economic times, the government should try to heed market demand and allow housing to resume its place as a catalyst for economic growth. In the article "The Next One Hundred Million," University of Utah professor Arthur C. Nelson estimates that the current supply of unattached single-family housing already exceeds projected demand and will continue to do so until 2037. Further analysis by Nelson (see “Reshaping America’s Built Environment”) indicates that as the glut of large-lot homes continues to flood the market, an emerging demand for smaller housing in walkable, mixed-use settings is on the rise. Simply put, the demand for *housing types* has changed in the marketplace, but current government policies obstruct developers from meeting public demand.

In the last few decades, both commercial and residential real estate have become commodities traded daily on exchanges. Some blame these markets for the Great Recession. While the truth is more complicated, if the federal government continues to steer investment in a direction inconsistent with consumer preferences, these investments will inevitably underperform. Federal regulations currently hamper market recovery by assigning risk by *type of development*, disfavoring mixed-use areas that have performed better during the current housing crisis. The worst performing and riskiest investments

– single-use, sprawled-out areas at the metropolitan edge - are still preferentially classified. Oddly, the federal remedy to the housing crisis has been to assign risk to one of the few segments of the housing market in which demand is growing.

The net effect of all this is that:

1. Americans are denied access to housing and living arrangements, which considerable evidence shows they prefer.

2. Investors and developers are discouraged from developing walkable and environmentally sustainable communities that meet growing market demand.

3. American small businesses and entrepreneurs are denied access to live/work developments that are proving popular and successful in other advanced nations.

4. US housing policy conflicts with the HUD/DOT/EPA Sustainability Partnership that seeks to improve the environmental and economic performance of the US economy.

CNU suggests that HUD and Treasury relax or eliminate restrictions on housing adjacent or attached to non-residential development. Risk should be assigned based on credit worthiness, not by the government's dictate that separate-use zoning reduces risk, when clearly it does not. Such reform will:

1. Allow investors and developers to produce the communities people are looking to place their families and their dollars.

2. Enable investors and developers to create and capture value in building out sustainable communities.

3. Unlock economic potential for the creation of new forms of business and traditional Main St.-style development.

4. Align government policies to accomplish stated federal goals and priorities.

As Christopher Leinberger, writing for *The Atlantic*, has stated, "Housing is such a large part of the economy that a sustained, robust recovery is difficult to imagine without a corresponding recovery in the building, buying, and selling of houses. Indeed, housing has usually helped lead us out of prior recessions." Working with our partners at the National Town Builders Association (NTBA), the National Association of Home Builders (NAHB), the National Association of Realtors, and the Center for Neighborhood Technology (CNT), the Congress for the New Urbanism has advocated for FHA, Fannie Mae, Freddie Mac, and 221d4 to raise and/or eliminate the restrictive covenants of commercial space in mixed-use developments. By recognizing the latent demand hindered by the current restrictions in place, FHA, HUD, Fannie and Freddie have an opportunity to not only support smart-growth policies attuned to the goals of the HUD/USDOT/EPA Sustainability Partnership, but also help jumpstart much-needed economic growth.

Reform Fannie Mae and Freddie Mac to allow the market to meet demand.

For further information, visit www.cnu.org/fanniereform