

September 27, 2018

Dear Representative,

On behalf of the eight undersigned organizations, we are writing to urge you to vote against HR 5381, the “GRATER Act”. HR 5381 mandates that Federal agencies transfer all credit and guarantee risk assumed by the government to the private sector, to the maximum extent possible. This mandate would put Wall Street in the driver’s seat in the pricing and execution of critical Federal guarantee programs ranging from mortgage and student lending to disaster relief, and could result in significantly increased costs for taxpayers.

It is important to understand that transferring credit risk to the private sector does not necessarily minimize the cost of such risk to taxpayers. The private sector must be compensated to accept credit risk. The costs of such compensation may and often do exceed the financing costs that would be experienced by the Federal government.

Furthermore, in times of financial stress private sector guarantors are more likely to be unable to execute on their credit guarantees than the Federal government is. Experience has shown that in times of stress investors often prefer to deal with the government and private sector guarantors may fail to deliver on credit guarantees. Several striking examples of this occurred in the 2007 to 2009 financial crisis period. During this period, private sector bond insurers almost all failed and mortgage insurers became too financially weak to cover losses.¹ In addition, private student lenders exited student loan markets, leading the Federal government to intervene to ensure students could continue to receive funding for college.²

The Federal government may thus have lower overall financing costs than the private sector for guarantee risk, especially when the possibility of a failure to deliver during market stress is taken into account. This means that both taxpayers and beneficiaries of guarantees can benefit from risk guarantees that are assumed by the Federal government in a clear and transparent way. Attempts to transfer all of these risks to the private sector may be harmful to the public. The appropriateness of private sector risk transfer is a highly context-specific determination. The sweeping mandate to transfer all risks to the private sector in HR 5381 is misguided and appears designed more to benefit financial intermediaries who want Federal government business than it is to benefit taxpayers or the public.

We are also concerned that sponsors have not taken account of all the potential implications of the sweeping language in this bill. Federal risk guarantees and backstops exist in numerous areas of financial markets, including mortgage debt, student debt, and disaster insurance including flood and earthquake insurance. Credit assistance to the financial sector during market stress, such as the Treasury line of credit for bank resolution or Federal Reserve emergency lending, can also be viewed as a credit guarantee. The broad mandate in HR 5381 to transfer all possible credit risk to the private sector could lead to profound changes across all of these areas, including

¹ Bergstresser, Daniel, Randolph Cohen and Siddarth Shenai, “Financial Guarantors and the 2007-2009 Credit Crisis”, Harvard Business School Working Paper 11-051, November, 2010. Available at <http://www.hbs.edu/faculty/Publication%20Files/11-051.pdf>. Thomas, Helen, “Mortgage Insurers, the Latest Link Under Strain”, FT Alphaville, April 9, 2008. Available at <https://ftalphaville.ft.com/2008/04/09/12182/mortgage-insurers-the-latest-link-under-strain/>

² National Consumer Law Center, Student Lending Handbook, Available at <https://library.nclc.org/sl/0103>

an increase in costs and a decline in funding reliability during emergencies. At the very least, much more study is called for in considering the kind of radical mandate included in HR 5381.

We therefore urge you to reject HR 5381. Thank you for your attention.

Sincerely,

Americans for Financial Reform

Center for Responsible Lending

Consumer Action

Consumer Federation of America

National Community Reinvestment Coalition

New Jersey Citizen Action

Prosperity Now

Woodstock Foundation