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Modernization of Federal Housing Administration Programs

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Chairman Dodd, Ranking Member Shelby and members of the Committee, thank you for holding this hearing and inviting the Mortgage Bankers Association (MBA)[1] to share its views on modernizing the Federal Housing Administration (FHA). My name is David Kittle and I am the President of Principle Wholesale Lending, Inc. in Louisville, Ky. and Vice-Chairman of the Mortgage Bankers Association (MBA). I am here today because MBA believes Congress must act to make important legislative changes to the National Housing Act if the FHA is to continue to be a tool for lenders to use in serving the housing needs of American families who are not served or are underserved by conventional markets.

When I started in the mortgage business, the programs of FHA were invaluable in enabling us to serve families who otherwise would have no other affordable alternative for financing their home. In fact, my first home was financed with an FHA mortgage, and when I was a loan officer in1983, over 90 percent of the loans I closed were FHA loans (320 out of 343 loans made that year). Moreover, from 1994, when I started my first mortgage company, until 1999, FHA was about 38 percent of my business.

Today, though, the story is very different. For example, since 1999, my company's FHA volume has steadily declined and now represents less than 2 percent of the company's business. While most lenders, investors and insurers have been able to adapt quickly to changes in the mortgage markets, but FHA has been prevented from doing so. The needs of low- and moderate-income homebuyers, of first-time homebuyers, of minority homebuyers, and of senior homeowners have changed. FHA's programs, though, have not followed their historic path of adaptation to meet these borrowers' changing needs.

The numbers are troublesome. In 1990, 18 percent of total originations in the U.S. were FHA-insured mortgages. Currently, that number has dropped to under three percent.[2] More importantly, in 1990, 12.5 percent of new home sales were financed through programs at FHA; today that number has dropped to under 5 percent.

MBA cites these numbers not because we believe that there is a certain market share that FHA should retain, but rather because these numbers are consistent

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[1] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 500,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 3,000 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mortgagebankers.org.

[2] Source: *Inside Mortgage Finance, March 2, 2007.*

with many lenders' views that FHA has not kept up with changes in the market. These numbers point to a decline, not just in market share, but in FHA's potential to positively impact homeownership. This loss of impact does not stem from the fact that FHA is no longer relevant, but rather that statutory constraints prohibit FHA from adapting its relevance to consumer needs today.

A recent anecdote illustrates this point very well. A story ran in *RealtyTimes®* on June 21, 2005, in which a Baltimore, Md. real estate agent unabashedly advises homebuyers to avoid FHA financing. The agent states: "Approved FHA loan recipients, same notice to you, don't bother bringing it to the table during a sellers' market. More times than not, your offer will be rejected. We know that VA and FHA loans allow you the means of purchasing more home for the mortgage, but it only works if you are the only game in town." His advice was based on the often true notion that FHA-insured financing is slower and more laborious than conventional financing, which means FHA's valuable programs are not reaching the people they should.

FHA Background

FHA was created as an independent entity by the National Housing Act on June 27, 1934, to encourage improvement in housing standards and conditions, to provide an adequate home financing system by insurance of home mortgages and credit and to exert a stabilizing influence on the mortgage market. FHA was incorporated into the newly formed U.S. Department of Housing and Urban Development (HUD) in 1965. Over the years, FHA has facilitated the availability of capital for the nation's multifamily and single-family housing market by providing government-insured financing on a loan-by-loan basis.

FHA offers multifamily and single-family insurance programs that work through private lenders to extend financing for homes. FHA has historically been an innovator. Over the past several decades, the mission of FHA's single-family programs has increasingly focused on expanding homeownership for those families who would otherwise either be unable to obtain financing or unable to obtain financing with affordable terms. FHA's multifamily programs have allowed projects to be developed in areas that otherwise would be difficult to finance and provides needed rental housing to families that might otherwise be priced out of a community.

The Need for FHA Today and Tomorrow

The FHA single-family programs are vital to many homebuyers who desire to own a home but cannot find affordable financing to realize this dream. While the FHA has had a number of roles throughout its history, its most important role today is to give first-time homebuyers the ability to climb onto the first rung of the homeownership ladder and to act as a vehicle for closing the homeownership gap for minorities and low- and moderate-income families.

Despite this country's recent record high levels of homeownership, not all families share in this dream equally. As of the fourth quarter of 2006, the national homeownership rate stood at 68.7 percent, but only 51 percent of minorities owned their own home. Only 48.2 percent of African-Americans and 49.5 percent of Latinos owned their own homes. This compares with 76 percent of non-Hispanic white households.

At the end of 2006, 84.5 percent of families earning more than the median income owned their own home, while only 52.9 percent of families below the median income owned their own home.[3]

These discrepancies are tragic because homeownership remains the most effective wealth-building tool available to the average American family.

FHA's Record

More than any other nationally available program, during the 1990s, FHA's impact focused on the needs of first-time, minority, and/or low- and moderate-income borrowers.

In 1990, 64 percent of borrowers using FHA-insured mortgages to purchase a home were first-time homebuyers. Today, that rate has climbed to over 80 percent. In 1992, about one-in-five FHA-insured purchase loans went to minority homebuyers. That number in recent years has grown to more than one-in-three. Minorities make up a greater percentage of FHA borrowers than they do conventional market borrowers.

FHA is particularly important to those minority populations experiencing the largest homeownership gaps. According to recent data provided by HUD, both first-time homebuyers and minorities continue to make up a significant portion of FHA's customer base. To date in FY 2007, FHA has insured 184,399 purchase mortgages and 147,121 of them, or 79.8 percent, went to first-time homebuyers. Minorities have received 46,083 FHA-insured mortgages, or 31.3 percent.[4]

Data also demonstrates FHA's tremendous service to those American families earning near or below the national median income. Ironically, as the above numbers reveal, FHA's mission to serve underserved populations has become increasingly focused during the same period as the decline in FHA's presence in the market. FHA's impact is being lost at the very time when it is needed most. The result is that American families are either turning to more expensive financing or opting not to buy a home.

It is crucial that FHA keep pace with changes in the U.S. mortgage markets. While FHA programs can be the best and most cost-effective way of expanding

[3] Source: U.S Census Bureau, Housing and Household Economic Statistics Division
[4] Source: *FHA Outlook*, June 1-15, 2007

lending to underserved communities, we have yet to unleash the full potential of these programs to help this country achieve important societal goals.

To be effective in the 21st century, FHA should be empowered to allow it to develop products and programs to meet the needs of today's homebuyers and anticipate the needs of tomorrow's mortgage markets, while at the same time being fully accountable for the results it achieves and the impact of its programs.

Under the strong leadership of its current Commissioner, Brian Montgomery, FHA has undertaken significant changes to its regulations and operations in a very short time. In just a little more than one year, FHA streamlined the insurance endorsement process, improved appraisal requirements and removed some unnecessary regulations. By doing so, Commissioner Montgomery has also instilled a spirit of change and a bias for action within FHA.

MBA compliments the Commissioner on his significant accomplishments to date, though we recognize that more work lies ahead. MBA is confident in the Commissioner's ability to address those issues that are within his control. There is much, though, that is beyond FHA's control and needs Congressional action.

Single-family FHA-insured mortgages are made by private lenders, such as mortgage companies, banks and thrifts. FHA insures single-family mortgages with more flexible underwriting requirements than might otherwise be available. Approved FHA mortgage lenders process, underwrite and close FHA-insured mortgages without prior FHA approval. As an incentive to reach into harder-to-serve populations, FHA insures 100 percent of the loan balance as long as the loan is properly underwritten.

FHA has a strong history of innovating mortgage products to serve an increasing number of homebuyers. FHA was the first nationwide mortgage program; the first to offer 20-year, 25-year, and finally 30-year amortizing mortgages; and the first to lower downpayment requirements from 20 percent to ten percent to five percent to three percent. Today, FHA's Home Equity Conversion Mortgage (HECM) has spawned a growing reverse mortgage market, which will pave the way for the private market in serving the needs of senior homeowners.

FHA's primary single-family program is funded through the Mutual Mortgage Insurance Fund (MMIF), which operates similarly to a trust fund and has been completely self-sufficient. This allows FHA to accomplish its mission at little or no cost to the government. In fact, FHA's operations have transferred surplus funds to the U.S. Treasury each year, thereby reducing the Federal deficit. FHA has always accomplished its mission without cost to the taxpayer. At no time in FHA's history has the U.S. Treasury ever had to "bail out" the MMIF or the FHA.

Unleashing FHA's Potential

In reviewing the status of FHA over the past decade, MBA has come to the conclusion that FHA faces severe challenges in managing its resources and programs in a quickly changing mortgage market. These challenges have already diminished FHA's ability to serve its public purposes and have also made it susceptible to fraud, waste and abuse. Unaddressed, these issues will cause FHA to become less relevant, and will leave families served by its programs with no alternative for homeownership or affordable rental housing.

In the fall of 2004, MBA formed a *FHA Empowerment Task Force* comprised of MBA member companies experienced in originating single-family and multifamily FHA loans. The Task Force discussed the long-term issues confronting FHA with the goal of developing legislative proposals that would empower it to manage its programs and policies more effectively.

The Task Force identified FHA's inability to efficiently develop products, higher costs of originations, lessening prominence in the market, out-dated technology and adverse selection as problems for FHA. Per the Task Force's recommendations, MBA proposed the following three steps to unleash FHA from overly burdensome statutory processes and restrictions, and to empower FHA to adopt important private sector efficiencies:

1. FHA needs greater autonomy to make changes to its programs and to develop new products that will better serve those who are not being adequately served by others in the mortgage market.

2. FHA needs the ability to use a portion of the revenues generated by its operations to invest in the upgrade and maintenance of technology to adequately manage its portfolios and interface with lenders.

3. FHA needs greater flexibility to recruit, manage and compensate employees if it is to keep pace with a changing financial landscape and ensure appropriate staffing to the task of managing $450+ billion insurance funds.

Flexibility to Create Products and Make Program Changes

FHA programs are slow to adapt to changing needs within the mortgage markets. Whether it is small technical issues or larger program needs, it often takes many years and the expenditure of great resources to implement changes. This process overly burdens FHA from efficiently making changes that will serve homebuyers and renters better and protect FHA's insurance funds. Today's mortgage markets require agencies that are empowered to implement changes quickly and to rollout or test new programs to address underserved segments of the market.

A prime example of this problem can be found in the recent experience of FHA in offering hybrid adjustable rate mortgage (ARM) products. A hybrid ARM is a mortgage product which offers borrowers a fixed interest rate for a specified period of time, after which the rate adjusts periodically at a certain margin over an agreed upon index. Lenders are typically able to offer a lower initial interest rate on a 30-year hybrid ARM than on a 30-year fixed rate mortgage. During the late 1990s, hybrid ARMs grew in popularity in the conventional market due to the fact that they offer borrowers a compromise between the lower rates associated with ARM products and the benefits of a fixed rate period.

In order for FHA to offer this product to the homebuyers it serves, legislative approval was required. After several years of advocacy efforts, such approval was granted with the passage of Public Law 107-73 in November 2001. Unfortunately, this authority was not fully implemented until the spring of 2005.

The problem began when PL 107-73 included an interest rate cap structure for the 5/1 hybrid ARMs that was not viable in the marketplace. The 5/1 hybrid ARM has been the most popular hybrid ARM in the conventional market. As FHA began the rulemaking process for implementing the new program, they had no choice but to issue a proposed rule for comment with a 5/1 cap structure as dictated in legislation. By the time MBA submitted its comment letter on the proposed rule to FHA, we had already supported efforts within Congress to have legislation introduced that would amend the statute to change the cap structure. MBA's comments urged that, if passed prior to final rulemaking, the 5/1 cap fix be included in the final rule.

On December 16, 2003, Public Law 108-186 was signed into law amending the hybrid ARM statute to make the required technical fix to the interest rate cap structure affecting the 5/1 hybrid ARM product. At this point, FHA was ready to publish a final rule. Regardless of the passage of PL 108-186, FHA was forced to go through additional rulemaking in order to incorporate the fix into regulation. Thus, on March 10, 2004, FHA issued a Final Rule authorizing the hybrid ARM program, with a cap structure that made FHA's 5/1 hybrid ARM unworkable in the marketplace. It was not until March 29, 2005, that FHA was able to complete rulemaking on the amendment and implement the new cap structure for the 5/1 hybrid ARM product.

The hybrid ARM story demonstrates well the statutory straitjacket under which the FHA operates. A four-to-six-year lag in introducing program changes is simply unacceptable in today's market. Every month that a new program is delayed or a rule is held-up means that families who could otherwise be served by the program are prevented from realizing the dream of homeownership or securing affordable rental housing.

Ability to Invest Revenues in Technology

Technology's impact on mortgage markets over the past 15 years cannot be overstated. Technology has allowed the mortgage industry to lower the cost of homeownership, streamline the origination process, and has allowed more borrowers to qualify for financing. The creation of automated underwriting systems, sophisticated credit score modeling, and business-to-business electronic commerce are but a few examples of technology's impact.

FHA has been detrimentally slow to move from a paper-based process, and it cannot electronically interface with its business customers in the same manner as the private sector. During 2004 and 2005, over 1.5 million paper loan files were mailed back and forth between FHA and its approved lenders and manually reviewed during the endorsement process. Despite the fact that FHA published regulations in 1997 authorizing electronic endorsement of loans, FHA was not able to implement this regulation until January of 2006, eight years later. This delay occurred despite the fact that over the same eight years, FHA's operations generated billions of dollars in excess of program costs that were transferred to the U.S. Treasury.

MBA believes FHA cannot create and implement technological improvements because it lacks sufficient authority to use the revenues it generates to invest in technology. Improvements to FHA's technology will allow it to improve management of its portfolio, garner efficiencies and lower operational costs, which will allow it to reach farther down the risk spectrum to borrowers currently unable to achieve homeownership. MBA believes that such an investment would yield cost savings to FHA operations far in excess of the investment amount.

In fact, one member of the Senate has taken action to address this issue by introducing S. 947, the "21st Century Housing Act," which would authorize funding to pay for much needed technology improvements.

Greater Control in Managing Human Resources

FHA is restricted in its ability to effectively manage its human resources at a time when the sophistication of the mortgage market demands market participants to be experienced, knowledgeable, flexible and innovative. To fulfill its mission, FHA needs to be able to attract the best and brightest. Other Federal agencies, such as the Federal Deposit Insurance Corporation (FDIC), that interface with and oversee the financial services sector are given greater authority to manage and incentivize their human resources. MBA believes that FHA should have similar authority if it is to remain relevant in providing homeownership opportunities to those families underserved by the private markets. FHA should have more flexibility in its personnel structure than that which is provided under the regular Federal civil service rules. With greater freedom, FHA could operate more efficiently and effectively at a lower cost. Further, improvements to FHA's ability to manage its human capital will allow FHA to attract and manage the talent necessary to develop and implement the strategies that will provide opportunities for homeownership to underserved segments of the market.

In addition to increasing funding for technological improvements to FHA, S. 947 would call on the Secretary to consult with, and maintain comparability with, the compensation of officers and employees of the FDIC, thereby giving the Secretary the tools to recruit and retain qualified and capable staff.

MBA believes the above three changes will allow FHA to become an organization that can effectively manage risk and self-adapt to shifting mortgage market conditions while meeting the housing needs of those families who continue to be not served or underserved today.

MBA Supported FHA Modernization Principles

MBA supported much of the FHA legislation before the 109th Congress, and I would like to take a moment to offer our perspective on various principles that should be contained in any FHA legislation this Committee considers.

Raising Maximum Mortgage Limits for High Cost Areas

There is a strong need for FHA financing to be relevant in areas with high home prices. MBA supports raising the FHA's maximum mortgage limits to 100 percent of an area's median home price (it is currently pegged at 95 percent) and raising the ceiling to 100 percent of the GSEs' conforming loan limits (currently limited to 87 percent) and the floor to 65 percent (currently 48 percent). Raising the FHA limits to the GSEs' limits in these areas strikes a good balance between serving a greater number of borrowers and taking on additional risk.

Additionally, in many low-cost areas, FHA's loan limits are not sufficient to cover the costs of new construction. New construction targeted to first-time homebuyers has historically been a part of the market in which FHA has had a large presence. MBA believes raising the floor will improve the ability of first-time homebuyers to purchase modest, newly constructed homes in low-cost areas since they will be able to use FHA-insured financing.

Downpayment Requirements

MBA supports the elimination of the complicated formula that is currently detailed in statute for determining the downpayment. The calculation is outdated and unnecessarily complex. The calculation of the downpayment alone is often cited by loan officers as the reason for not offering a FHA product.

MBA also supports improving FHA's products with downpayment flexibility. Independent studies have demonstrated two important facts: first, the downpayment is one of the primary obstacles for first-time homebuyers, minorities, and low- and moderate-income homebuyers. Second, the downpayment itself, in many cases, is not as important a factor in determining risk as are other factors. Many borrowers will be in a better financial position if they keep the funds they would have expended for a large downpayment as a cash reserve for unexpected homeownership costs or life events.

We believe that FHA should be empowered to establish policies that would allow borrowers to qualify for FHA insurance with flexible downpayment requirements and decide the amount of the cash investment they would like to make in purchasing a home. To this end, the Secretary of HUD should be authorized to determine the appropriate level of downpayment requirements. We stand ready to work with Congress to ensure that such flexibility maximizes homeownership opportunities for underserved communities without compromising the safety and soundness of FHA.

Adjusting Mortgage Insurance Premiums for Loan Level Risk

MBA believes that FHA would be able to serve more borrowers, and do so with lower risk to the MMIF, if they are able to adjust premiums based on the risk of each mortgage they insure. A flexible premium structure could also give borrowers greater choice in how they utilize the FHA program.

It is a fact that some borrowers and loans will pose a greater risk to FHA than others. At some level, FHA should have the authority to adjust premiums based upon borrower or loan factors that add risk. Such adjustment for risk need not be a complicated formula. MBA believes FHA could significantly mitigate the risk to the MMIF by selecting a small number of risk factors that would cause an adjustment from a base mortgage insurance premium (MIP).

A current example of this would be the fact that borrowers receiving a gift of the downpayment on a FHA-insured mortgage are charged the same premium as a borrower who puts down three percent of their own funds, despite the fact that FHA's experience indicates that the former represents a higher risk loan. FHA could better address such a risk in the MMIF by charging a higher MIP to offset some of the additional risk that such a loan poses. In this manner, while a borrower receiving a gift of funds for the downpayment will still receive the benefits of FHA financing, they themselves would share some of the risk, rather than having the risk borne solely by those making a three percent downpayment.

Creating a risk-based premium structure will only be beneficial to consumers, though, if FHA considers lowering current premiums to less risky loans. We would not support simply raising current premiums for higher risk borrowers.

Lengthening Mortgage Terms

MBA supports FHA's ability to develop products with mortgage terms up to 40 years. Currently, FHA is generally limited to products with terms of no more than 30 years. Stretching out the term will lower the monthly mortgage payment and allow more borrowers to qualify for a loan while remaining in a product that continues to amortize. MBA supports lengthening the mortgage terms and believes FHA should have the ability to test products with these features and, based on performance and homebuyer needs, to improve or remove such products.

Improvements to the Reverse Mortgage Program

FHA modernization legislation should include changes to the FHA's Home Equity Conversion Mortgage (HECM) program, such as: the permanent removal of the current 250,000-loan cap and the creation of a single, national loan limit for the HECM program. The HECM program has proven itself to be an important financing product for this country's senior homeowners, allowing them to access the equity in their homes without having to worry about making mortgage payments until they move out. The program has allowed tens of thousands of senior homeowners to pay for items that have given them greater freedom, such as improvements to their homes that have allowed them to age in place, or to meet monthly living expenses without having to move out of the family home.

MBA believes it is time to remove the program's cap because the cap threatens to limit the HECM program at a time when more and more seniors are turning to reverse mortgages as a means to provide necessary funds for their daily lives. MBA further believes that the HECM program has earned the right to be on par with other FHA programs that are subject only to FHA's overall insurance fund caps. Additionally, removing the program cap will serve to lower costs as more lenders will be encouraged to enter the reverse mortgage market.

Additionally, authorizing the HECM program for home purchase will improve housing options for seniors. In a HECM for purchase transaction, a senior homeowner might sell a property they own to move to be near family. The proceeds of the sale could be combined with a reverse mortgage, originated at closing and paid in a lump sum, to allow a senior to purchase the home without the future responsibility of monthly mortgage payments. Alternatively, a senior homeowner may wish to take out a reverse mortgage on a property that is less than one year old, which is defined as "new construction" by FHA.

Finally, the HECM program should have a single, national loan limit equal to the conforming loan limit. Currently, the HECM program is subject to the same county-by-county loan limits as FHA's forward programs. HECM borrowers are disadvantaged under this system because they are not able to access the full value of the equity they have built up over the years by making their mortgage payments. Currently, a senior homeowner living in a high-cost area is able to access more equity than a senior living in a lower cost area, despite the fact that their homes may be worth the same and they have the same amount of equity built up. Reverse mortgages are different than forward mortgages and the reasons for loan limits are different, too. FHA needs the flexibility to implement different policies, especially concerning loan limits.

Improvements to FHA Condominium Financing

MBA supports moving FHA's coverage of condominium units from the General Insurance Fund to the Mutual Mortgage Insurance Fund. It is unfortunate to note that FHA insurance on condominium units has dropped at a higher rate than the overall decline in FHA's originations. This decline contradicts the fact that in costly markets, condominium units are typically the primary type of housing for first-time homebuyers. FHA should have a much bigger presence in the condominium market.

As this Committee moves the process of FHA reform forward, there are issues that I would like to bring to your attention that warrant particularly close consideration.

The Definition of "Higher-Risk" Borrowers

If this Committee wishes to craft a provision defining "higher-risk" borrowers, MBA suggests giving the Secretary authority to set underwriting and corresponding pricing standards for a "higher-risk" category so that borrowers in the future will not have to wait on the sometimes cumbersome Congressional process.

Treatment of FHA Non-Conveyable Properties

As you know, FHA provides credit insurance against the risk of foreclosure losses associated with loans originated according to FHA standards. FHA generally pays an insurance claim when it takes title (conveyance) to a property as a result of foreclosure. To convey a property and receive insurance benefits, however, FHA requires that the property be in "conveyance condition" (i.e., saleable condition). Properties that have sustained damage attributable to fire, flood, earthquake, tornado, hurricane, boiler explosion (for condominiums), or the lender's failure to preserve and protect are not eligible for insurance benefits unless they are repaired prior to conveyance of the property to the FHA. While HUD has in the past accepted properties in "as is" (damaged) condition on a case-by-case basis, this is rarely done. Moreover, HUD will deduct from the "as is" claim the estimated cost of repair. HUD should accept conveyance of damaged properties and not adjust the claim for the cost of repair when there was no failure on the part of the servicer to obtain hazard or flood insurance pursuant to federal law or if a borrower is eligible to apply for CDBG grant funds, but fails to do so. In addition, to the extent that a property is not conveyable (i.e., condemned, demolished by local, state, or federal government or deemed to be a Superfund site, etc), HUD should be permitted to pay the full claim without taking conveyance of the property. We do not believe HUD has the statutory authority to manage claims in this manner.

In March, the House passed H.R. 1227, the “Gulf Coast Hurricane Housing Recovery Act of 2007,” which includes a provision dealing with this issue. Last month, Chairman Dodd introduced S. 1668, “The Gulf Coast Housing Recovery Act of 2007,” which also includes a fix to this serious problem. MBA applauds Congress’ attention to this issue, especially in light of HUD’s and Louisiana’s actions to revamp the Road Home grant program in a manner that no longer promotes rebuilding. This decision exacerbates servicers’ losses. These are losses for which FHA lenders never thought they were signing up, and represent another barrier to wide-scale use of the FHA in the marketplace.

Broker Supervision

FHA must approve all mortgage lenders and loan correspondents who wish to originate or underwrite FHA-insured loans. Non-supervised mortgagees (e.g. mortgage brokers) and loan correspondents outside of the federal regulatory regime must establish an ability to meet both FHA’s financial and legal standards in order to be approved.

This is currently satisfied through a minimum net worth requirement and the submission of a yearly financial audit. These requirements demonstrate the mortgagee or loan correspondent has a certain level of financial solvency and employs necessary controls to provide reasonable assurance that FHA products are offered in compliance with all applicable regulations, such as laws governing fair housing and nondiscrimination.

Some industry participants have proposed amending this approval process by allowing mortgage brokers to substitute a surety bond in lieu of the existing annual net worth auditing requirements. It is important to note that the annual financial statement (AFS) is the federal government’s only opportunity to ensure that the 7,500 non-supervised mortgagees, loan correspondents, and brokers who offer FHA-insured loans are doing so in accordance with all applicable laws and regulations. Kenneth Donohue, HUD’s Inspector General, recently stated that “[t]he AFS is an integral part of FHA’s monitoring of its approved mortgagees, and [the Inspector General] does not believe that its minimal cost…is sufficient cause to increase the risk of loss to the taxpayer that may result from its elimination.” MBA believes that, especially in the current climate of rising FHA defaults, Congress should not loosen the supervision of entities offering products backed by FHA and the American taxpayer.

FHA Multifamily Programs

While the thrust of recent modernization efforts focus on FHA's single-family programs, it is important to underscore the critical role of FHA's multifamily programs in providing decent, affordable rental housing to many Americans. Approximately 30 percent of families and elderly citizens either prefer to rent or cannot afford to own their own homes. FHA's insurance of multifamily mortgages provides a cost-effective means of generating new construction or rehabilitation of rental housing across the nation. FHA is also one of the primary generators of capital for healthcare facilities, particularly nursing homes.

While the FHA has implemented a number of significant improvements to its single-family program over the last two years, the same focus needs to be applied to improving the multifamily programs. MBA hopes that process improvements on the multifamily side of FHA will soon be discussed and implemented.

MBA supports raising the mortgage limits in high cost areas from 140 percent and 170 percent, respectively, to 170 percent and 215 percent. In the face of rapidly rising building costs in many of the nation's cities, this increase is necessary to allow developers to continue providing affordable housing in those areas that need it the most.

Additionally, MBA opposes any unnecessary increases in the Mortgage Insurance Premium (MIP) on FHA multifamily housing programs. Unfortunately, the Administration's FY 2008 budget proposes increases of more than 35 percent in the MIP on many key multifamily programs. This proposal will significantly increase the cost of, and in some cases prohibit, rehabilitating and developing rental housing for working families. An increase in premium fees will translate directly into higher rents and lead to the production of fewer affordable units, thereby reducing availability and affordability of rental housing. MBA encourages legislative language that would prohibit HUD from increasing the MIP unless the increase is necessary to cover the costs of the programs as calculated in accordance with the Credit Reform Act of 1990.

Response to Natural Disasters

Hurricane season is again upon us. The disasters of Hurricanes Katrina and Rita point to the need for a financially solvent FHA that is not restricted by onerous processes and procedures. The FHA program must be ready to assist homeowners and renters who lost everything amid the destruction of the hurricanes. It must have the necessary wherewithal to step in and help work out the existing mortgages in disaster areas. FHA must have the programs necessary to meaningfully assist in the rebuilding effort. Giving FHA the mechanisms to fund adequate technology improvements, flexibilities in managing human resources, and greater authority to introduce products will ensure FHA can step in to help communities when disasters occur. It is critical that Congress act quickly to ensure that FHA is adequately prepared to help homeowners and renters before the next major disaster strikes.

Downpayment Assistance Programs

Without Congressional action this year, many families face a serious risk of being unable to access FHA financing due to a ruling last year by the Internal Revenue Service (IRS). On May 4, 2006, the IRS released Revenue Ruling 2006-27, which may lead the IRS to rescind the nonprofit status of a large number of organizations who receive funding from property sellers in providing downpayment assistance to FHA borrowers. FHA regulations require that nonprofits providing a downpayment gift have an IRS nonprofit exempt status. Due to the ruling, the IRS has indicated that it is investigating 185 organizations which provide downpayment assistance.

MBA expects the IRS ruling and, if adopted, FHA's Proposed Rule "Standards for Mortgagor's Investment in Mortgaged Property, to have a dramatic effect on FHA's purchase production. Before the ruling, more than one-third of FHA purchase loans had some type of downpayment assistance. Such programs currently serve tens of thousands of FHA's primary clientele: first-time homebuyers, low- and moderate-income families and minorities.

Conclusion

Finally, as Members of this Committee are well aware, recent market events and regulatory actions in the mortgage industry have led to a number of lenders either significantly tightening underwriting standards or leaving the business altogether. MBA believes the individuals who will be most directly impacted by these events are the consumers that FHA was created to serve: first-time homebuyers, low-income families and those with less than perfect credit histories. It is in light of these realities that we ask Congress to move quickly and empower FHA with the authority it needs to provide consumers with affordable, viable lending options needed to help them achieve homeownership.

On behalf of MBA, I would like to thank the Committee for the opportunity to present our views on the important programs offered by FHA. MBA looks forward to continuing to work with Congress and HUD to improve FHA's ability to serve aspiring homeowners and those seeking affordable rental housing.