STATEMENT

of

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on

"FHA: Issues for the Future"

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before the

Housing and Transportation Subcommittee

Of the

Banking, Housing, and Urban Affairs Committee

United States Senate

Thank you for holding this hearing and inviting the Mortgage Bankers Association (MBA)[1] to share its views with the Subcommittee on "*FHA: Issues for the Future*." My name is Regina M. Lowrie and I am the President of Gateway Funding Diversified Mortgage Services, LP in Horsham, Pennsylvania and Chairman of the Mortgage Bankers Association. I am here today because MBA believes that the Senate must act to make important legislative changes to the National Housing Act if the Federal Housing Administration (FHA) is to continue to be a financially sound tool for lenders to use in serving the housing needs of American families who are unserved or underserved by conventional markets.

In 1994, I founded Gateway with only seven employees and $1.5 million in startup capital. Over the past 12 years, I have grown the company to over 800 employees working in more than 58 offices, originating $3 billion in loans annually throughout Pennsylvania, Delaware, New Jersey and Maryland. I am proud of the work of Gateway, and of the mortgage industry itself, in providing opportunities for homeownership for families of this great land.

When I started Gateway, the programs of FHA were invaluable in enabling us to serve families who otherwise would have no other affordable alternative for financing their home. Ten years ago, FHA loans comprised 40 percent of Gateway's volume. We worked hard to be a good partner with FHA in administering its programs and, together, FHA and Gateway enabled tens of thousands of families to purchase their first home.

Today, though, the story is very different. While Gateway has grown significantly, our ability to use the FHA program has declined precipitously. Gateway has been able to adapt 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.

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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.**

The numbers are troublesome. In 1990, 13 percent of total originations in the U.S. were FHA-insured mortgages. In 2004, that number dropped to near 3.5 percent. More importantly, in 1990, 28 percent of new home sales (which are typically a large first-time homebuyer market) were financed through programs at FHA or the Department of Veterans Affairs (VA); today that number has dropped to under 12%.

MBA cites these numbers not because we believe that there is a certain marketshare that FHA should retain, but rather because these numbers are consistent with many lenders' views that FHA has not kept up with changes in the market. These numbers point to a decline, not just in marketshare, 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*® one year ago, 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.

This is a very unfortunate perspective, especially because FHA is vitally needed today. Thus, MBA is not focused on FHA marketshare in and of itself, but rather because it signals whether or not FHA's valuable programs are reaching the people they should.

MBA is committed to supporting FHA. Nowhere in Washington will you find a stronger supporter of the FHA and the programs it offers. Mortgage lenders are the private delivery system that allows FHA to reach borrowers with affordable homeownership financing and rental housing opportunities, especially low- and moderate-income families, first-time homebuyers, minorities, and the elderly. Every day, mortgage lenders sit down with the very families FHA seeks to serve to discuss how we can help them realize their dreams. Maybe we understand better than most that without FHA, many American families simply would not have had and will not have the opportunity to own their own home.

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 housing 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 have increasingly focused on expanding homeownership for those families who would otherwise either be unable to obtain financing or 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.

Additionally, the FHA program has been a stabilizing influence on the nation's housing markets due to the fact that it is consistently available under the same terms at all times and in all places. FHA does not withdraw from markets.

FHA Single-family Programs

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. FHA has always performed a market stabilizing function by ensuring that mortgage lending continued after local economic collapses or regional natural disasters when many other lenders and mortgage insurers pulled out of these markets.

FHA's primary single-family program is funded through the Mutual Mortgage Insurance Fund (MMIF), which operates similar 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 transfer 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.

FHA Multifamily Programs

While much focus over the past several months has been 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. There are a number of families and elderly citizens who either prefer to rent or who 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 cross the nation. As well, FHA is 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 year, 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.

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 first quarter of 2006, the national homeownership rate stood at 68.5 percent, but only 51 percent of minorities owned their own home. Only 48 percent of African-Americans and 49.4 percent of Latinos owned their own homes. This compares with 75.5 percent of non-Hispanic white households.

By the end of 2005, 84.3 percent of families earning more than the median income owned their own home, while only 53.1 percent of families below the median income owned their own home.

These discrepancies are tragic because homeownership remains the most important wealth-building tool the average American family has.

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 FHA borrowers using FHA to purchase a home were first-time homebuyers. Today, that rate has climbed to about 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. Home Mortgage Disclosure Act (HMDA) data reveal that in 2004, 14.2 percent of FHA borrowers were African-Americans, compared with 5.4 percent of conventional borrowers. Hispanic borrowers made up 15.3 percent of FHA loans, while they only were 8.9 percent of the conventional market. Combined, African-American and Hispanic borrowers constituted 29.5 percent of FHA loans, doubling the conventional market's rate of 14.3 percent. In fact, in 2004, FHA insured nearly as many purchase loans to African-American and Hispanic families as were purchased by Fannie Mae and Freddie Mac combined.

The same data demonstrates FHA's tremendous service to those American families earning near or below the national median income. Over 57 percent of FHA borrowers earned less than $50,000, which is more than double the rate of the conventional market, where fewer than 28 percent of borrowers earned less than $50,000.

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 giving up.

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 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 twenty first century, FHA should be empowered to incorporate private sector efficiencies that 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 one year, FHA has 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. Lenders still report that FHA is difficult to work with and that oversight activities often focus on minor compliance deficiencies in a loan file rather than focusing on issues of true risk to FHA's insurance funds. FHA is designed to serve higher risk borrowers and MBA believes that those auditing FHA lenders must understand this and be able to differentiate this aspect of the program from intentional abuse.

MBA is confident in the Commissioner's ability to address these and other issues that are within his control. There is much though, that is beyond FHA's control and needs Congressional action.

FHA Reform is Urgent

MBA is concerned that while FHA is currently sound and under the strong leadership of Commissioner Montgomery, without imbuing FHA with the flexibility to adapt to 21st century mortgage markets, the health of FHA operations will be at risk in the future. While the annual audit of the MMIF has consistently found over the past 10 years that the fund is operating soundly and well in excess of capital ratios established by Congress, there have also been signs that statutory constraints are causing FHA to be adversely selected.

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* comprising 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 higher costs of originations, lessening prominence in the market, out-dated technology, adverse selection, and the inability to efficiently develop products 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 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.

2. 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.

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

Ability to Invest Revenues in Technology

Technology's impact on U.S. 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 this past January, 8 years after the fact. This delay occurred despite the fact that over the same 8 years, FHA's operations generated billions of dollars in excess of program costs that was 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.

MBA proposes the creation of a separate fund specifically for FHA technology, funded by revenues generated by the operation of the MMIF. MBA suggests the establishment of a revenue and a capital ratio benchmark for FHA, wherein, if both are exceeded, FHA be authorized by Congress to use a portion of the excess revenue generated to invest in its technology. Such a mechanism would allow FHA to invest in technology upgrades, without requiring additional appropriations from Congress.

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 dollar investment amount.

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 U.S. mortgage markets 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.

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 roll-out 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 statutes 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. Each year 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.

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 unserved or underserved today.

<u>**Legislative Activity**</u>

MBA is supportive of much of the legislation that is currently before Congress, and I would like to take a moment to offer our perspective on various provisions.

On April 4, 2005, Representatives Bob Ney and Maxine Waters introduced the *Expanding American Homeownership Act of 2006,* H.R. 5121. This bi-partisan bill, which has over 67 co-sponsors, marks the first time FHA is being looked at by Congress in a comprehensive way in over 10 years.

In general, H.R. 5121 significantly streamlines and modernizes the National Housing Act and seeks to unleash FHA from a 74 year-old statutory regime that constricts its effectiveness. Among other things, H.R. 5121 would provide for flexible downpayments, flexible risk-based premiums, an increase in mortgage limits, an extension of mortgage terms, reform of FHA's condominium program, and changes to the Home Equity Conversion Mortgage (HECM) program.

MBA would note that the Congressional Budget Office (CBO) has recently reported that H.R. 5121 would generate $247 million in revenues for the U.S. Treasury in 2007 and $2.3 billion in revenues during fiscal years 2007 – 2011. This report makes it obvious that the reforms proposed in H.R. 5121 are not only beneficial to FHA and to the homebuyers it serves, but it is beneficial to the U.S. government's bottom line.

More importantly to this Subcommittee is legislation that has been discussed or introduced in the Senate. Currently, MBA is aware of three bills that affect FHA that have been introduced and one that may be introduced. MBA would like to briefly comment on each one.

MBA would like to review a number of provisions that we understand may be part of legislation introduced in the Senate as a companion bill to H.R. 5121.

Downpayment Requirements

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

MBA supports the elimination of the statutory requirement that the borrower provide a minimum cash investment. Improving FHA's products with such downpayment flexibility is one of the most important innovations FHA can be empowered to make. 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.

The private market has already demonstrated that the downpayment can be replaced with other risk-mitigating features without significantly hurting performance. Many borrowers will be in a better financial position if they keep the funds they would have expended for the 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.

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 some 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 is charged the same premium as a borrower who puts down 3% of their own funds, despite the fact 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 borrower 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 born solely by those making a 3% downpayment.

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

In December 2004, FHA eliminated the practice of refunding the unearned portion of the Up-front Mortgage Insurance Premium (UfMIP) to borrowers who prepay their FHA-insured mortgage early and go to another product. MBA was hopeful that the removal of the refund (which admittedly was an administrative cost for FHA and servicers) would have been followed by a correlated lowering of the UfMIP. This did not happen. The net effect was to actually raise the cost of the FHA program. MBA would not want to see the same thing happen under a risk-based premium structure.

Raising Maximum Mortgage Limits for High Cost Areas

MBA supports the proposal to raise FHA’s maximum mortgage limits to 100 percent of an area’s median home price (currently pegged at 95 percent) and to raise the ceiling to 100 percent of the conforming loan limit (currently limited to 87 percent) and the floor to 65 percent (currently 48 percent).

There is a strong need for FHA financing to be relevant in areas with high home prices. MBA believes raising the limits to conforming limits in these areas strikes a good balance between allowing FHA to serve a greater number of borrowers without taking on additional risk. The CBO scored this provision in H.R. 5121 as a net revenue generator for the Treasury, indicating that it will improve FHA's performance.

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.

Lengthening Mortgage Term

MBA supports authorizing FHA 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. We believe FHA should have the ability to test products with these features, and then, based on performance and homebuyer needs, to improve or remove such a product.

Improvements to FHA Condominium Financing

MBA supports changes to FHA's condominium program that will streamline the process for obtaining project approval and allow for greater use of this program. 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.

Improvements to the Reverse Mortgage Program

MBA unequivocally supports all of the following proposed changes to FHA's Home Equity Conversion Mortgage (HECM) program: the removal of the current 250,000 loan cap, the authorization of HECMs for home purchase and on properties less than one year old, 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, 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. A senior homeowner living in a high-cost area will be 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.

In addition to the above proposed legislation, MBA is aware of three pieces of legislation which have been introduced in the Senate that would positively affect FHA. These are S. 2123 the "FHA Manufactured Housing Loan Modernization Act of 2005," S. 2597 "The Federal Housing Fairness Act of 2006," and S. 3173 the "21st Century Housing Act." MBA would like to highlight each of these bills.

The FHA Manufactured Housing Loan Modernization Act of 2005 – S. 2123

On December 16, 2005, Senator Allard (R-CO) introduced S. 2123, the *FHA Manufactured Housing Loan Modernization Act of 2005*. The proposals outlined in S. 2123 would help make FHA a leader in promoting sound financing of manufactured housing. MBA understands that the provisions of S. 2123 will be included in the proposed Senate companion legislation to H.R. 5121.

MBA supports revitalizing FHA's Title I manufactured housing mortgage insurance program. Manufactured housing is an important source of affordable housing but FHA's current program to insure mortgages of manufactured housing needs to be updated in order to be relevant to this market.

The Federal Housing Fairness Act of 2006 – S. 2597

On April 7, 2006, Senator Hillary Clinton (D-NY) introduced S. 2597 "The Federal Housing Fairness Act of 2006." MBA strongly supports S. 2597, which would facilitate homeownership in high cost areas.

The sole provision of this bill would amend the National Housing Act by raising FHA loan limits to 100 percent of an area's median home price, not to exceed the conforming loan limit. Currently, FHA loan limits are set at 95% of an area's median home price not to exceed 87% of the conforming loan limit.

21st Century Housing Act – S. 3173

On May 25, 2006, Senator Clinton introduced S. 3173, the "21st Century Housing Act." MBA supports S. 3173 which has a number of provisions that would significantly modernize FHA and its programs. The bill contains the following positive provisions:

Investment in FHA Infrastructure – Human Resources

MBA supports authorizing the Secretary of HUD to appoint and fix the compensation of FHA employees and officers. The bill calls on the Secretary to consult with, and maintain comparability with, the compensation of officers and employees of the Federal Deposit Insurance Corporation. This provision can be carried out by excess revenue derived from the operation of FHA's insurance funds, beyond that which was estimated in the Federal budget for any given year.

While MBA has some questions as to the funding mechanism detailed in the bill for this provision, we firmly believe that giving FHA greater flexibility in investing in its human capital is critical if it is to attract and retain the talent it needs to become a stronger and more effective program serving the needs of our nation's homeowners and renters.

Investment in FHA Infrastructure – Information Technology

MBA strongly supports this provision of S. 3173, which would fund investment in FHA's information technology. This provision contemplates that excess funding derived from the operation of FHA's insurance funds, beyond that which was estimated in the Federal budget for any given year, would be used to carry out this provision.

While MBA has some questions as to the funding mechanism detailed in the bill for this provision MBA believes that upgrading FHA's technology is critical to improving FHA's management of its portfolio and lowering its operational costs. MBA also believes that such an investment will allow FHA to reach farther down the risk spectrum to borrowers currently unable to achieve homeownership.

Extension of Mortgage Term Authority

MBA supports an extension of FHA's mortgage term authority. S. 3173 would amend the National Housing Act by extending FHA's mortgage term authority to 50 years. MBA believes this flexibility would allow FHA to develop products that lower monthly costs and make homeownership a more viable option for many families.

Downpayment Flexibility

*S*ince the downpayment is one of the primary obstacles for first-time homebuyers, minorities, and low- and moderate-income homebuyers, MBA supports this provision that would allow for flexible downpayments. In many cases, the downpayment itself is not as important a factor in determining risk as are other factors, such as credit scores.

MBA believes that a flexible downpayment will allow borrowers to have a cash reserve that may be necessary for the upkeep and maintenances of their homes, as well as for other unforeseen life events.

Mortgage Insurance Flexibility

S. 3173 would allow the Secretary of HUD to establish the cost of a mortgage insurance premium payment, based on factors determined by the Secretary and commensurate with the likelihood of default of the borrower.

MBA supports this provision, as we recognize that FHA may be able to serve more borrowers and do so with lower risk if they are able to adjust premiums based on the risk of each mortgage it insures.

Increasing Maximum Mortgage Limits for Multifamily Housing in High Cost Areas

MBA supports the provision in S. 3173 that would increase loan limits from 140 percent to 170 percent of the basic statutory limits in high cost areas, and from 170 percent to 215 percent of the basic statutory limits to allow for higher than typical costs for individual projects. MBA recognizes that homeownership is not necessarily appropriate for every American, and it is important that there are affordable rental housing options as well as adequate healthcare facilities in communities.

Multifamily concerns

Additionally, I must voice MBA's strong opposition to the proposal in the Administration's budget to increase the insurance premiums on multifamily projects far above that necessary to operate a financially sound program. The net effect of this proposal will be to cause many affordable rental properties not to be built or rehabilitated and to raise rents on those families and elderly households on the projects that still go through.

There is no rationale for this fee increase except to generate additional revenue for the Federal government as these programs are already priced to cover their costs. We urge the committee to prohibit FHA from implementing this fee increase.

Conclusion

FHA's presence in the single-family marketplace is smaller than it has been in the past and its impact is diminishing. Many MBA members, who have been traditionally strong FHA lenders, have seen their production of FHA loans drop significantly. This belies the fact that FHA's purposes are still relevant and its potential to help borrowers is still necessary.

I would like to conclude my testimony highlighting two issues which make passing FHA legislation particularly urgent this year.

First, hurricane season is 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.

Secondly, without Congressional action this year, many families face a serious risk of being unable to access FHA financing due to a recent ruling passed down by the Internal Revenue Service (IRS). On May 4, 2006, the IRS released Revenue Ruling 2006-27, which will likely lead the IRS to rescind the nonprofit status of a large number of nonprofits 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 this ruling to have a dramatic effect on FHA's purchase production. Currently, more than one-third of FHA purchase loans have the type of downpayment assistance that will be affected by the IRS ruling. Such programs currently serve tens of thousands of FHA's primary clientele: first-time homebuyers, low- and moderate-income families and minorities.

MBA does not dispute the ruling by the IRS but we are concerned about the families that will find affordable financing unavailable to them and implore Congress to give FHA the authority to serve these families through a flexible downpayment program this year.

MBA has taken great efforts to inform our membership about the impact of the IRS ruling, and the responses of our members have been strong. Mortgage lenders want to be able to serve these families directly with an FHA product that allows for flexible downpayments. On May 15, 2006, MBA, along with nine other trade associations, sent a coalition letter to members of the House, urging them to co-sponsor H.R. 5121. We have heard that over 12,000 mortgage industry professionals contacted their Representatives during May urging them to support H.R. 5121. Clearly, Congressional action on FHA reform this year is vital.

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