

# FHA Must Balance its Commitment to its Single-Family Mission, Risk Management, and the Assistance to the Housing Recovery as the Housing Market Transforms

## MBA Recommends

The Federal Housing Administration (FHA) and Ginnie Mae are vital components of the housing finance system and provide an indispensable service to the underserved, low-to-moderate income, and minority homebuyer and renter. It is imperative that Congress support these entities through this housing finance transition period so that they remain viable, relevant and sustainable for the long term.

## Background

For many years, FHA and Ginnie Mae have been the government's primary programs for making homeownership accessible and affordable to America's middle-income families. FHA's business is clearly focused on first-time homebuyers, particularly among minorities. Recent data shows that first-time homebuyers accounted for more than 75 percent of FHA's purchase mortgages, and minorities accounted for more than 30 percent of this business.

The Mortgage Bankers Association (MBA) is a strong supporter of FHA and Ginnie Mae. Our members understand the value of the FHA's programs to homebuyers, especially those who may need the features of FHA-insured loans to purchase their first homes, and we appreciate the market liquidity that Ginnie Mae provides.

In the early 2000s there were discussions among policymakers about whether FHA was truly necessary, or if the private sector could assume its functions. The significance of FHA and Ginnie Mae in the housing finance system has been underscored, however with the recent mortgage crisis that began in late

2006 and resulted in the retreat of the private sector and an illiquid mortgage market. FHA's counter-cyclical role has proven invaluable to maintaining liquidity in the mortgage market and has helped buttress the country's unstable housing finance system. With the contraction of the private sector, FHA's market share has grown to almost 30 percent of all loan originations and has reached as high as 50 percent in some geographic locations in 2010, and almost 50 percent of all purchase mortgages in the country. Temporary higher maximum loan limits of \$729,500 in high-cost areas helped to increase this market share.

In this time of crisis and increased defaults, FHA had to make efforts to protect the Mutual Mortgage Insurance (MMI) fund, which supports the main single-family programs. FHA has made a series of single-family risk management and lender oversight and enforcement changes over the last two years designed to protect the financial stability of FHA. Single-family changes included, restructuring the mortgage insurance premiums, eliminating FHA's approval of loan correspondents, and raising its lender net worth requirements. MBA commends the Department of Housing and Urban Development's (HUD's)

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and FHA's leadership for taking proactive measures in order to ensure that "a taxpayer bailout" is not necessary. The most recent Actuarial Report released in November 2010 shows the MMI Fund at 0.50 percent, with the capital reserve ratio requirement of two percent expected to be met in 2014, and exceed the requirement in 2015.

As the housing market begins to stabilize and the debate intensifies over the new configuration of the country's housing finance system, policymakers are now faced with the question of how to transition FHA back to a state of normalcy without dramatically disrupting the housing recovery. Recommendations for how to scale back government involvement range from a dramatic and immediate reduction to a gradual phase-out of the country's dependence on the public sector. While both positions have merit, supporters of a phase-out approach recognize that the foundation of the housing market is still not strong and that the return of the private sector and regulatory certainty for lenders are keys to a smooth transition.

Because of the potential detrimental consequences of any drastic action, MBA supports a gradual reduction of government involvement. MBA is committed to supporting FHA through this transition time and providing it with the support it needs to remain a viable, relevant component of the housing finance system and continue to provide housing opportunities for millions of Americans.

Throughout this transition, FHA should ensure that it balances appropriate risk management, sustainable homeownership and support for the housing market recovery. Policies that are too constricting over too short a period of time would not allow businesses the flexibilities that are necessary in loan originations and may hinder the availability of credit to responsible borrowers.

## Action Needed

MBA believes FHA's importance to the housing finance market make it imperative that policymakers act thoughtfully to preserve the agency's strength and viability now, and over the longer term, without hindering the progress of the housing recovery. It is in the spirit of partnership that MBA makes the recommendations below that are intended to fortify the financial foundation of FHA, continue its affordable housing mission, and assist in a smooth transition to a normalized housing market.

## Program Support

1. Support the current single-family loan limit cap of \$729,750 until the markets are further stabilized, at which time the limit should be re-examined.
  - MBA believes it is important for Congress to consider the stabilization of the economy and the return of adequate liquidity to the marketplace, as it debates whether to maintain the current higher loan limits. Reducing the single-family loan limits at this time could leave middle-income homeowners, especially in high-cost areas, without affordable financing options.
2. Maintain the current 3.5 percent minimum downpayment requirement for single-family borrowers with credit scores of 580 or greater.
  - A critical component of FHA's mission is to maintain the affordability of homeownership. The current minimum downpayment permits borrowers to have appropriate "skin in the game" while providing affordable homebuyers with an option for entering the home buying market.
  - Maintaining the existing minimum downpayment requirements, while requiring strong underwriting standards, such as full documentation, allows affordable homebuyers to responsibly become, and stay, homeowners.

## Capacity and Resources

1. Give FHA and Ginnie Mae the needed resources to hire new staff with current mortgage market skills.
  - FHA should be given flexibility and financial resources to hire the appropriate number of qualified staff for its current and future needs.
  - FHA and Ginnie Mae should be given the ability to recruit and pay staff at a higher federal pay scale on par with other "professional-grade" cabinet, regulatory and independent agencies that require specialized expertise, such as the Federal Deposit Insurance Corporation and the Securities and Exchange Commission.
  - MBA recommends FHA and Ginnie Mae also have the ability to more broadly utilize retention allowances,

recruitment bonuses and superior qualifications appointments.

2. Provide FHA with the resources to develop and implement updated information technology systems and processes including the use of anti-fraud tools. Furthermore, FHA should continue implementation of business process re-engineering within select programs, and refine the FHA TOTAL Scorecard.
  - FHA should employ a fraud monitoring and reporting tool as early in the origination process as possible and before consummation.

## Operations and Delivery of Services

1. Promote a fair indemnification process that includes justifiable cause or materiality for the request and a well-defined, clear and transparent lender appeals process.
  - Many of the proposed policy changes are extremely subjective and provide FHA with the authority to apply rules with the most rigid interpretation, at the administration's discretion.
  - HUD should note that increasing lender risk could discourage participation and cause lenders to tighten

their own guidelines. MBA is concerned about the layering of additional risk management requirements that significantly increase compliance costs and lead to fewer responsible borrowers qualifying for FHA loans.

2. Give the FHA Commissioner the authority, with concurrence from the HUD Secretary, HUD General Counsel and Ginnie Mae President, to temporarily suspend problem lenders. The Commissioner should secure the concurrence of the HUD Secretary, General Counsel and Ginnie Mae President before taking this action.
  - The FHA Commissioner should have the authority to temporarily suspend a lender, pending a more expansive review and on-site visit, if FHA knows a lender's portfolio is experiencing a dangerous level of stress. Currently, the Mortgage Review Board is the only vehicle available to FHA to suspend lenders.
  - FHA must establish a fair, clear and transparent due diligence process for lenders before the suspension, including, but not limited to, quality control audits and loan performance reviews.
  - FHA should establish a reasonable cure period for lenders and a process for contesting any suspension decision.