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SENATE REPUBLICAN POLICY COMMITTEE

Legislative Notice

No. 42 December 14, 2007

S. 2338 – FHA Modernization Act of 2007

Calendar No. 481

On November 13, the Banking Committee reported S. 2338; S. Report 110-107.

Noteworthy

- Under a unanimous consent agreement reached December 13, 2007, the Senate will take up S. 2338, the FHA Modernization Act of 2007 on December 14, 2007, with two amendments pending, a Dodd/Shelby amendment and a Coburn amendment. There will be a total of 90 minutes of debate, equally divided.

- As of press time, the Dodd/Shelby amendment was adopted by unanimous consent. The only remaining amendment to be considered is a Coburn amendment dealing with reverse mortgages.

- S. 2338 makes changes to the National Housing Act of 1934, thereby reforming the Federal Housing Administration's (FHA) single-family insurance program.

- S. 2338 raises loan limits, modifies downpayment requirements, and expands the access to FHA programs.

- S. 2338 also removes the current cap on the number of reverse mortgages made through the Home Equity Conversion Mortgage program (HECM) and raises the current loan limit for this program to a single national loan limit. HECM is currently a demonstration project; S. 2338 makes HECM permanent.

- On September 18, 2007, the House passed H.R. 1852, legislation similar to S. 2338, by a vote of 348-72.

Background

FHA was created in the National Housing Act of 1934 to stimulate the housing market at a time when homeownership was low. Over the past 73 years, FHA programs have helped over 34 million low- to moderate-income families become homeowners.

FHA does not make (originate) direct loans but rather guarantees that the total mortgage will be paid to a lender if a buyer defaults. Its Single Family programs insure mortgage loans to purchase new or existing homes, condominiums, manufactured homes, and houses needing rehabilitation, as well as reverse equity mortgages to elderly homeowners.[1] FHA-insured mortgages are an attractive option because these mortgages do not require more than a 3-5 percent down payment and tend to have lenient credit history requirements.

Since 2005, the Administration has called on Congress to modernize FHA because its "outdated statutory authority has left the agency out of synch with the rest of the lending industry."[2] In recent years, FHA's market share of the number of insured loans has dropped from 19 percent in 1996 to 6 percent in 2006 as conventional mortgage lenders have offered new options for low- to moderate-income families.

Currently, FHA programs are administered through two program accounts—the Mutual Mortgage Insurance Fund/Cooperative Management Housing Insurance fund (MMI) and the General Insurance/Special Risk Insurance fund account. The MMI is currently solvent and adequately capitalized. However, FHA's FY08 budget request indicated that because of expected adverse loan performance and improved estimation techniques, total costs may exceed receipts. Therefore, FHA may require additional appropriations of credit subsidy budget authority to continue operation to avoid an expected $143 million shortfall in FY08.

As a mortgage insurer, FHA must pay the cost of loans when borrowers default on their loans. FHA seldom recovers the costs of the loans when they resell the properties to the public. The agency loses an average of 30 percent of each insurance claim it pays.[3]

Bill Provisions

Title I – Building American Homeownership Act

Section 102: Maximum principal loan balance

Current Law: The maximum insurable mortgage loan limit amount for a single-family residence is set on an area-by-area basis. The amount is the lesser of (a) 95 percent of the local median

[1] Reverse mortgages are the opposite of traditional mortgages in the sense that the borrower receives payments from the lender instead of making such payments to the lender. Reverse mortgages are, in general, designed to enable elderly homeowners to remain in their homes while using the equity in their homes as a form of income.
[2] See testimony from Federal Housing Commissioner Brian D. Montgomery: http://banking.senate.gov/_files/ACFCE6.pdf
[3] For more information on FHA, see CRS report RS20530, FHA Loan Insurance Program: An Overview.

home price or (b) 87 percent of the nationwide government-sponsored entity (GSE) conforming loan limit.

S. 2338: This section raises the loan limit to the lesser of (a) 100 percent of the local median home price, or (b) the nationwide GSE conforming loan limit, which is currently $417,000.

Section 103: Cash investment requirement and prohibition of seller-funded downpayment assistance

Current law: In general, an FHA-insured loan requires a minimum of 3-percent cash investment or downpayment. Mortgage insurance premiums and closing costs may be financed into the loan.

S. 2338: This section simplifies the calculation to require a minimum 1.5-percent cash investment of the appraised value of the property for all FHA-insured loans. The Committee-passed bill does not allow for a zero downpayment, as proposed by the Administration. This section also prohibits seller-funded downpayment entities from providing any of this required cash investment.

Section 104: Mortgage insurance premiums

Current law: The maximum mortgage insurance premium is 2.25 percent of the insured principal balance of the loan.

S. 2338: This section allows FHA to charge up to 3.0 percent.

Section 107: Insurance of condominiums and manufactured housing

Current law: Condominiums in the form of manufactured housing units are not eligible under current FHA rules.

S. 2338: This section adds a definition of condominium mortgage with the intent to insure condominium mortgages and to provide that condominiums may be in the form of manufactured housing units.

Section 108: Mutual Mortgage Insurance Fund (MMIF)[4]

S. 2338: This section clarifies that the MMIF is subject to the provisions of the Credit Reform Act of 1990 and directs HUD to ensure that the MMIF remains financially sound. This section

[4] MMIF income comes from insurance premiums, interest earnings, and proceeds from the sale of foreclosed homes; and from cash flows out of the MMIF to cover administrative costs, claims on foreclosed mortgages, and refunds of mortgage insurance premiums. In recent years, FHA has faced increased competition from conventional mortgage lenders; the resulting decrease in FHA loan volume coupled with the poor performance of FHA loans has reduced the income traditionally generated by the program.

also requires an annual independent actuarial report to Congress on the financial status of the Fund.

Section 112: Home Equity Conversion Mortgages (HECMs)

Current law: The Housing and Community Development Act of 1987 authorized the HECM program as a demonstration project and limited FHA from insuring no more than 275,000 HECMs. HUD has already reached this limit. The loan limit for HECMs is similar to FHA-insured loans set on an area-by-area limit.

S. 2338: This section eliminates the current cap on the number of HECMs FHA may insure. This section also provides for a uniform nationwide mortgage loan limit on FHA reverse mortgage loans equal to the GSE conforming loan limit of $417,000. This section also limits the origination fee on such mortgages to 1.5 percent subject to a minimum allowable amount. This section also allows the FHA Commissioner the authority to increase or lower the fee cap, depending on market conditions.

Section 113: Energy Efficient Mortgages

Current law: There is an energy efficient mortgages pilot program which provides for a maximum of 5 percent of the value of the property up to $8000.

S. 2338: This section raises the cap on the value of energy efficient improvements to 5 percent of the single-family loan limit.

Section 114: Pilot program

S. 2338: This section requires HUD to carry out a pilot program to establish an automated process for providing alternative credit rating information for borrowers who have insufficient credit histories for determining their creditworthiness.

Section 115: Homeownership preservation

S. 2338: This section requires the Secretary of HUD and FHA Commissioner to improve FHA's loss mitigation process. Recent data from HUD show that there is still a significant number of FHA borrowers who are never contacted to mitigate losses. This section directs HUD and FHA to work with the housing industry to develop and implement a plan to limit losses.

Title II – Manufactured Housing Loan Modernization

Section 203: Exception to limitation on financial institution portfolio

S. 2338: This section changes from a lender portfolio system to a loan-by loan insurance system and retains the 10 percent lender co-insurance.

Section 204: Insurance benefits

S. 2338: This section requires FHA to pay claims on a loan-by-loan basis, absent fraud or misrepresentation.

Section 205: Maximum loan limits

Current law: This current limit for the manufactured housing repair program is set at $17,500. The limit for the home-only program is set at $48,600 and the limit for the land and home program is set at $64,800.

S. 2338: This section raises the loan limits for various Manufactured Housing Loans. These limits have not been adjusted since 1992.

Section 209: Prohibition against kickbacks and unearned fees

S. 2338: This section applies certain provisions of the Real Estate Settlement Procedures Act (RESPA) to the purchase of manufactured homes financed with FHA-insured loans. This section also gives the Secretary of HUD broad authority to apply this section. This section also gives the Secretary the authority to prohibit unfair or deceptive practices in connection with the purchase of manufactured homes with a loan insured under this title.

Administration Position

At press time, there is no White House Statement of Administration Policy.

Cost

The Committee, in consultation with the Congressional Budget Office, estimates that the bill would result in a net cost of $22 million in 2008 and a net increase in offsetting collections of $1.6 billion over the 2008-2012 period.

Possible Amendments

Per a unanimous consent agreement, two amendments will be in order, a Dodd/Shelby amendment on setting a moratorium and a Coburn amendment on reverse mortgages. The Coburn amendment would delay making changes to the cap on HECMs until GAO submits a report on the program.