RSC Republican Study Committee
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Legislative Bulletin……………………………………..………September 18, 2007

Contents:

Summary of the Bills Under Consideration Today:

Total Number of New Government Programs: At least three

Total Cost of Discretionary Authorizations: $95 million decrease over five years

Effect on Revenue: $0

Total Change in Mandatory Spending: $16 million increase in one year

Total New State & Local Government Mandates: 0

Total New Private Sector Mandates: 0

Number of *Bills* Without Committee Reports: 0

Number of *Reported* Bills that Don't Cite Specific Clauses of Constitutional Authority: 0

H.R. 1852—Expanding American Homeownership Act (*Waters, D-CA*)

Order of Business: The bill is scheduled to be considered on Tuesday, September 18th, likely subject to a structured rule. Summaries of any amendments made in order under the rule will be provided in a separate RSC document.

Background: The Federal Housing Administration (FHA) was created in 1934 (and became a part of the Department of Housing and Urban Development—HUD—in 1965) to provide mortgage insurance on loans made by FHA-approved lenders throughout the United States and its territories. The FHA insures mortgages on single family, multifamily, and manufactured homes and hospitals. The FHA is reportedly the largest insurer of mortgages in the world, having insured over 34 million properties since its inception. FHA mortgage insurance protects lenders against loss if the homeowner defaults on his mortgage loan.

FHA operates entirely from self-generated income (proceeds from the mortgage insurance paid by homeowners), which is placed in an account that is used to operate the program. The FHA currently has 4.8 million insured single family mortgages and 13,000 insured multifamily projects in its portfolio.

For more information about the FHA, visit its homepage here: http://www.fha.gov/.

Summary: H.R. 1852 would, among other things, authorize the Federal Housing Administration (FHA) to use risk-based pricing for the mortgage guarantees it offers. Highlights of the bill are as follows:

- Raises the FHA maximum loan limits for single-family homes (which are set at the lesser of two benchmarks) from: (1) 95 percent of the median home price for the area to 100 percent and (2) from 87 percent to 100 percent of the GSE conforming loan limit (the size of a loan a government-sponsored enterprise like Freddie Mac may purchase), with an increase in the minimum loan limit (the "floor") from 48 percent to 65 percent of the GSE limit (the limit is $417,000 in 2007). Currently, FHA insurance will not cover loans greater than $362,000 in high-cost areas and $200,000 in low-cost areas. These limits would increase to $417,000 and $271,000, respectively.

- Aligns the loan limits for 2-, 3-, and 4-unit mortgages with the ratios used by GSEs.

- Extends the maximum length for an FHA loan term from 35 to 40 years.

- Retains the current statutory 3% cash downpayment requirement--except for "zero- and lower-down payment borrowers," as defined in the legislation. The FHA could charge upfront premiums for such borrowers in an amount up to 3% of the principal, and annual premiums for such borrowers up to 0.75% of the loan balance.

- Allows the FHA to use a risk-based premium structure for single-family mortgages, insured on or after October 1, 2007, allowing for different interest rates to be charged depending on a borrower's credit history. The bill would specifically allow zero-and-lower-downpayment, as well as higher-risk, borrowers (as defined in the bill) to received FHA loans.

- Establishes procedures for HUD to establish and change premiums, including a list of factors to be considered in establishing such premiums.

- Requires HUD to provide "payment incentives" (i.e. premium reductions) for borrowers who make on-time payments for at least the first five years of the loan, and authorizes HUD to offer such incentives as soon as three years after continuous on-time payments.

- Authorizes HUD to require pre-mortgage counseling for zero- and lower-downpayment borrowers, as well as higher-risk borrowers (i.e. borrowers with poor credit scores) and to require that borrowers be informed of their local counseling options. Borrowers who become 60-days delinquent on their loans would have to be given notice by a housing counseling entity of the availability of foreclosure prevention counseling.

- Requires borrowers applying for zero-down and lower-downpayment loans to be provided written disclosures, either through counseling or at loan application, regarding other mortgage loan options, the additional costs associated with lower down payment loans, the appreciation needed to pay off the loan, including selling costs, disclosures of their payment incentive rights (at the closing), and disclosure of rights to loss mitigation (also at the closing).

- Specifically states that these counseling and disclosure requirements yield no right of private action (no ability to sue), yet HUD could establish penalties on mortgagees for noncompliance.

- Requires HUD to report annually to Congress on the rates of default and foreclosure of zero- and lower-downpayment and higher-risk borrowers, as well as on actions HUD has taken to mitigate losses.

- Authorizes an up-to-25% increase in the FHA single-family loan limit for any home that includes space used for a licensed child care facility.

- Allows the FHA to insure manufactured housing and updates and clarifies the existing FHA mortgage insurance procedures for condominiums (mainly to align them with adjustments made above to single-family housing and to the allowance of manufactured housing).

- Makes clarifying adjustments to the Mutual Mortgage Insurance Fund (MMIF) at the Department of Treasury (which was created to consolidate single-family FHA mortgage loan programs under one fund). The Secretary would be directed to ensure that the Fund remains financially sound. If the Fund proves to be actuarially unsound, the Secretary would be allowed to adjust premiums or adjust underwriting standards.

- Makes Homeownership Voucher Program mortgages and Home Equity Conversion (i.e. "reverse") mortgages secured under the National Housing Act the obligations of the MMIF.

- Makes single-family mortgages insured under the National Housing Act on Hawaiian home lands and Indian reservations the obligations of the MMIF.

- Repeals the following "obsolete or little used" programs (as defined by the Democrat staff of the Financial Services Committee): mortgage insurance for outlying areas, certain mortgage insurance on Indian lands, mortgage insurance for servicemen, special mortgage insurance for low income families, and the graduated payment mortgage program. The committee staff note that some of these programs are duplicative, and the benefits to the involved constituencies are available under other portions of the National Housing Act.

- Eliminates the current volume cap (set at 250,000) on FHA Home Equity Conversion Mortgages (HECM) or "reverse mortgages"—whereby homeowners over the age of 62 take out a line of credit on their home—and sets a single nation-wide loan limit tied to the GSE conforming loan limit (thus eliminating the local median home price determination). HUD would have to establish limits on the origination fee that may be charged for a reverse mortgage loan (though not more than 2% of principal) and allows such loans to be used for co-op units.

- Permits mortgage brokers and correspondent lenders to originate FHA loans if they post bond in the amount of $75,000, in lieu of having to meet various financial audit and net worth requirements. GAO would have to report on the effectiveness of this bond option after four years. The bond program would terminate after five years, unless HUD extends it based on determinations that it offers similar or better protections for borrowers.

- Imposes additional requirements for mortgage brokers and correspondent lenders participating in FHA loans, including requiring them to "safeguard and account for any money handled for the borrower; to follow reasonable and lawful instructions from the borrower; and to act with reasonable skill, care, and diligence."

- Gives HUD the authority to increase FHA single family loan limits up to the nationwide GSE conforming loan limit for a period of up to 36 months in presidentially-declared disaster areas—but not in excess of 100% of a home's appraised value plus closing costs.

- Prohibits HUD from insuring any FHA loan unless the borrower provides acceptable personal identification: a Social Security card along with a photo ID issued by the federal or a state government, a driver's license or ID card issued by a state in accordance with the REAL ID Act of 2005, any valid passport, or a photo ID card issued by U.S. Citizenship and Immigration Services.

- Instructs HUD to carry out a five-year pilot program to establish an automated process for providing alternative credit rating information (such as information on rent payments, utilities payments, etc.) for borrowers who have insufficient credit histories for determining their creditworthiness. HUD could not insure a number of mortgages under this pilot that exceeds 5% of the aggregate number of FHA-insured mortgages in the preceding year. GAO would have to report to Congress within two years on the number of additional borrowers assisted by this program and on the impact of this program on safety and soundness of National Housing Act insurance funds.

- Increases the maximum FHA multifamily loan limits in high-cost areas from 140% of the basic loan limit to 170% and raises such maximum loan limits on a project-by-project basis from 170% of the basic limit to 215% of such limit.

- Authorizes appropriations, in the amount equal to the net increase in negative credit subsidy (i.e. excess FHA funds from premiums and fees charged under the mortgage insurance programs) created by this bill's provisions, for diversion to an **affordable housing fund** (created by the GSE reform bill—H.R. 1427), for grants to provide affordable rental housing and homeownership opportunities for low income families. NOTE: in current law, excess FHA funds—i.e. savings—are deposited in the U.S. Treasury as a benefit to taxpayers.

  The amount diverted to an affordable housing fund would be the amount of FHA savings after first deducting all of the following: 1) the amount, if any, needed to avoid a credit subsidy appropriation for the FHA single family loan program in that year, 2) the amount needed to increase nationwide funding for housing counseling grants from the current level of $42 million to $100 million a year for each of fiscal years 2008-2012, and 3) $25 million for each of fiscal years 2008-2012 to increase funding for improving FHA technology, procedures, processes, program performance, and salaries.

  No negative credit subsidies (i.e. FHA savings) from the single family loan program could be used to fund expenditures under this section.

  NOTE: RSC Chairman Hensarling submitted an amendment to the Rules Committee to strike the diversion of FHA savings to an affordable housing fund. See "Possible Conservative Concerns" below.

- Prohibits HUD from increasing any FHA premiums above the level in effect at the beginning of FY2007, unless HUD determines that, absent such increase, a program would require a credit subsidy appropriation (i.e. a taxpayer bailout).

Additional Background: In the 109th Congress, a related bill (H.R. 5121, sponsored by Rep. Bob Ney, R-OH), passed the House on July 25, 2006, by a vote of 415-7. To see the RSC Legislative Bulletin on H.R. 5121, see page 17 at this webpage: http://www.house.gov/hensarling/rsc/doc/LB_072506_suspensions.doc.

RSC Bonus Fact: The FHA was created to shore up a floundering construction industry in the 1930s. http://www.fha.gov/about/index.cfm#history

Committee Action: On March 29, 2007, the bill was referred to the Financial Services Committee, which, on May 2nd, marked up, and ordered it reported to the full House 45-19. All the no votes were Republicans, including Ranking Member Spencer Bachus (R-AL) and RSC Chairman Jeb Hensarling (R-TX).

Possible Conservative Concerns: Conservatives have expressed numerous concerns about this legislation, including the following:

- Loan Limits Increases. The bill would increase various loan limits and thus make more people eligible to receive FHA mortgage insurance. Such increases seem to conflict with the mission of the FHA—to help low-income and other people get mortgages. By raising loan limits, FHA insurance could presumably be obtained by more people who are not the true targets of FHA.

- Zero Downpayments. The bill would allow FHA insurance to cover loans on which the borrower has made no downpayment. Conservatives may be concerned that this program expansion allows FHA insurance to cover people who received their homes without investing any equity into it.

- Mandatory Refunds. The bill would essentially mandate refunds to borrowers who have made on-time payments for five years. This provision would reduce revenues to the FHA (making it more likely to need appropriations support from general taxpayers) and would remove flexibility for FHA in its incentive programs.

- Affordable Housing Fund. The bill would divert certain FHA savings to an affordable housing fund (for the distribution to housing non-profit entities). Conservatives have opposed an affordable housing fund in the past because, since money is fungible, it would allow liberal activist groups, like ACORN and La Raza, that perform some housing-related activities to use taxpayer dollars to indirectly subsidize their big-government, anti-conservative advocacy nationwide. Furthermore, FHA savings currently get returned to the Treasury as a benefit to taxpayers. This legislation would siphon away FHA savings for this fund, as well as for additional activities detailed above.

- Crowding Out the Private Market. Some conservatives may be concerned that H.R. 1852 would expand FHA's ability to guarantee mortgages and therefore increase a federal subsidy for homebuyers. In addition, some may be concerned that this expansion may crowd out the private market. For instance, according to CBO, "FHA's basic insurance is directed at a segment of the market that is shrinking and becoming less dependent on the government for access to mortgage financing. In part, that situation has arisen because private lenders have increased their offerings for low-downpayment and higher-risk mortgages."

  Given that the private marketplace is offering many different, affordable homeownership opportunities, one might question whether now is the proper time to expand and perpetuate a government program that was created in 1934 to broaden homeownership and increase employment in the building industry.

Administration Position: The Statement of Administration Policy (SAP) for H.R. 1852 generally supports the bill, but includes concerns about certain provisions, including:

- "the Administration strongly opposes the establishment of a new Affordable Housing Grant Fund linked to increased FHA receipts;
- "the provision for mandatory refund of "excess" premium to borrowers with FICO credit scores below 560 whose loans survive more than five years undercuts the insurance principle on which FHA is based;

- “the Administration also has concerns with the two percent limitation on HECM loan origination fees proposed in the legislation; and
- “the Administration is also concerned about a provision that would make it possible for correspondent lenders to use FHA without meeting audit and net worth requirements, which could allow participation by brokers who are inadequately capitalized or have internal control difficulties.”

Cost to Taxpayers: According to CBO, H.R. 1852 would increase mandatory spending by $16 million in FY2007 and would reduce authorization levels by $12 million in FY2008 and by $95 million over the FY2008-FY2012 period.

It is worth noting that, in a study requested last year by Congressman Jeb Hensarling, CBO stated that current budget rules understate the cost of federal credit programs, such as FHA loan programs, in part by failing to account for market risk and separately listing administrative expenses:

> [Current budget rules] understate the cost of FHA guarantees relative to that of other federal spending programs….For example, a proposal to spend $2 billion per year for vouchers to permit high-risk first-time home buyers to purchase private mortgage insurance would have a budget cost of $10 billion over a five-year period, whereas the fiscally equivalent alternative of operating the [FHA] program under current policy would be shown in the budget as having net savings of $1.8 billion for that same period.
>
> Source: http://www.cbo.gov/ftpdocs/74xx/doc7412/07-17-FHA.pdf

As a result, while the CBO cost estimate may suggest “savings” from expanding the FHA loan programs, H.R. 1852’s actual burden to the taxpayer may be far greater.

Does the Bill Expand the Size and Scope of the Federal Government?: The bill would expand federal loan programs, as detailed above.

Does the Bill Contain Any New State-Government, Local-Government, or Private-Sector Mandates?: CBO confirms that the bill contains no mandates.

Does the Bill Comply with House Rules Regarding Earmarks/Limited Tax Benefits/Limited Tariff Benefits?: The Financial Services Committee, in House Report 110-217, reports that Section 28 of the underlying bill, regarding the clarification of the disposition of certain properties, is essentially an earmark requested by Rep. John Dingell (D-MI). The request letter from Rep. Dingell submitted to the committee is included in the committee report:

> DEAR GENTLEMEN: I am requesting the legislative language found in Section 28 of H.R. 1852 for the City of Ypsilanti, Michigan in fiscal year 2008. The entity that would benefit from this provision is the City of Ypsilanti, located at City Hall, One South Huron Street, Ypsilanti, MI 48197. The provision would allow HUD to sell the Parkview Apartments, located at 596 S. Hamilton Street, Ypsilanti, Michigan 48197, at a below market rate. I certified that neither I nor my spouse has any financial interested in this project.

House Rule XXI, Clause 9(d) defines “earmark” as “a provision or report language included primarily at the request of a Member, Delegate, Resident Commissioner, or Senator providing, authorizing or recommending a specific amount of discretionary budget authority, credit authority, or other spending authority for a contract, loan, loan guarantee, grant, loan authority, or other expenditure with or to an entity, or targeted to a specific State, locality or Congressional district, other than through a statutory or administrative formula-driven or competitive award process."

Constitutional Authority: The Financial Services Committee, in House Report 110-217, cites constitutional authority in Article 1, Section 8, Clause 1 (relating to the congressional power to promote the general welfare of the United States) and Clause 3 (relating to the congressional power to regulate interstate commerce).

Outside Organizations: The Mortgage Bankers Association is supporting this legislation.

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