CALIFORNIA ASSOCIATION OF REALTORS®

Issues Briefing Paper

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Real Estate Finance Committee
Federal Issues Committee

Proposed FHA Rescue Legislation

The following is for study only and has NOT been approved by the Real Estate Finance Committee or the Board of Directors.

Issue: C.A.R. staff asked both the REF and FIC leadership to review the issue of allowing the Federal Housing Administration (FHA) and Fannie Mae and Freddie Mac (GSE) to purchase mortgages from lenders that are at risk of defaulting. Staff requested this because Congress was preparing to hear and vote on new legislation which C.A.R. did not have policy addressing. REF and FIC leadership made the following recommendation to the C.A.R. Leadership Team which they approved.

That C.A.R. "Support" allowing the government housing programs to purchase mortgages from lenders that are at risk of defaulting. C.A.R. believes that the government housing programs should not be utilized as a taxpayer funded bailout; but, that lenders and homeowners should share in the responsibility and cost.

Background:
In early and mid 2007, the national housing market was showing signs of a decline with a downturn in housing prices, a slowdown of sales, and an increased rate of foreclosures. The market continued to worsen and eventually led to the subprime market collapse. In August of 2007, Wall Street responded by halting investments in not only subprime mortgage backed securities (MBS) but all non government entity MBS. This immediate drought of capital has contributed greatly to the current housing market conditions that include, record-low home sales, record declines in home prices and record numbers of foreclosures across the country.

Besides the current weak housing market, other factors are placing pressure on Congress to take immediate action to stabilize the housing crisis and avert a national recession. These include constituent complaints and cries for help, lobbying efforts by Wall Street, lenders and other industry parties, and 2008 being a presidential election year.

Summary:
While there are a number of proposals from Congressmen, Senators and federal regulators, the two bills that have the best opportunity of passage are those by Representative Barney Frank and Senator Christopher Dodd. Frank and Dodd jointly announced their bills on March 13, and while there are some differences the primary intention of both proposals is to utilize the FHA to insure troubled mortgages.

Frank and Dodd Side-by-Side Comparison

Concept	Frank	Dodd
Title (The bills are still in draft form and do not yet have bill	FHA Housing Stabilization and Homeownership Retention Act	HOPE for Homeowners Act of 2008

numbers)		
Key Idea	Utilize FHA to insure up to $300 billion in troubled mortgages that would be refinanced at a lower fixed-rate loan and below the appraised value of the property.	Utilize FHA to insure up $300 billion in troubled mortgages that would be refinanced at a lower fixed-rate loan and below the appraised value of the property.
Eligibility	1. Owner occupied principal residence 2. Loan origination between Jan 1, 2005 and July 1, 2007 3. Debt-to-income (DTI) ratio greater than 40 percent as of March 1, 2008 4. Borrower must certify they have not intentionally defaulted on the existing loan	1. Owner occupied principal residence 2. Can't afford current mortgage payments (standards determined by the Board to be set up by the legislation) 3. Originated on or before Jan 1, 2008
Government Involvement	FHA Insurance	A new federal agency governed by a Board of department heads and the chair of the FDIC which will oversee a program utilizing FHA Insurance
New Loan Amount	The principal loan amount will be reduced to 90 percent of the appraised value of the property. Additionally, the single upfront FHA premium will be paid by further reducing the loan value by an amount not to exceed 5 percent. Annual premium is not to exceed 1.5 percent of the remaining insured principal balance	The principal of the new loan will be the lesser of what the borrower can afford to pay (set by the Board) or the amount established at auction, and it may not exceed 90 percent of the appraised value of the property. Additionally, the single upfront FHA premium will be paid by further reducing the loan value by an amount not to exceed 3 percent. Annual premium is not to exceed 1.5 percent of the remaining insured principal balance
New Loan Requirements	1. Underwritten with full income documentation 2. Must remain within current FHA loan limits at time of underwriting 3. Fixed rate loan 4. Borrower can not be denied the loan based on FICO score or default	1. Fixed rate loan 2. 30 year term
Net Equity Sharing	When the property is sold the borrower shall pay FHA the	When the property is sold the borrower shall pay FHA:

	greater of 3 percent of original insured principal obligation of the mortgage Or A percentage of the portion of net proceeds described below: 1. 100 percent during the first year of the term of the mortgage 2. 80 percent during the second year 3. 60 percent during the third year 4. 40 percent during the fourth year 5. 20 percent during the fifth year 6. 0 percent after the end of the fifth year	1. 100 percent of net proceeds if sold during the first year 2. 90 percent of net proceeds if sold between 1 year and 2 years 3. 80 percent if sold between 2 years and 3 years 4. 70 percent if sold between 3 years and 4 years 5. 60 percent if sold between 4 years and 5 years 6. 50 percent if sold after 5 years This 50 percent would last in perpetuity until the borrower sells the home.
Where Premiums will Go	Premiums will be placed in the Special Risk Insurance Fund which is separate from the Mutual Mortgage Insurance Fund (which finances most of its single-family mortgage insurance) and the General Insurance Fund (which finances most of its multifamily mortgage insurance). This allows HUD to manage more effectively the greater risk supposed to be inherent in these loans, thus lowering the insurance premiums for the vast majority of borrowers.	Premiums will be placed in a newly created HOPE Fund.
Sunset Dates	Expires after a two-year period; however, the HUD Secretary may extend the program up to four times for periods of no longer than 6 months each.	The program will sunset on December 31, 2012.
Lender Requirements	This is a voluntary program. Lenders may choose to auction loans they believe would qualify for the program but will not be forced to.	This is a voluntary program. Lenders may choose to auction loans they believe would qualify for the program but will not be forced to.
Miscellaneous		
	Authorizes $10 billion in loans and grants for the purchase and rehabilitation of vacant or foreclosed homes with the goal of occupying them as soon as possible. Funds distributed to	HUD and OFHEO shall establish a foreclosure prevention goal for Fannie and Freddie where they would purchase loans at a discount and write down those mortgages. Mortgages would be

	states by the Secretary of the Treasury.	written down using the same criteria from FHA as loans eligible for FHA insurance. OFHEO would be given authority to require GSEs to raise capital commensurate with additional risk this goal poses. Additionally, the GSE's low- and moderate-income housing goals would be suspended.

(The chart above is a compilation of information provided by the Mortgage Bankers Association and C.A.R. staff summaries of the draft bills.)

Pros and Cons

For	Against
Contrary to popular perception, these bills are not a complete bailout. Lenders are forced to take a loss on the loan through a cramdown of the principal below the current appraised value. Homeowners will be forced to pay mortgage insurance and forego a percentage of any appreciation.	There is no overwhelming support for a bailout by Americans. According to a December, 2007, CNN poll, only 51 percent of Americans support using federal dollars to help out struggling homeowners and only 25 percent support bailing out lenders.
The current downturn in the housing market that has led to skyrocketing foreclosure rates has had a devastating impact on many communities across the county as well as in California. These bills present an opportunity for homeowners in trouble to possibly refinance into a safe and affordable loan and stabilize the current market.	Since the program would be voluntary for lenders, this is nothing more than a statutory version of the failed Hope Now program the administration flaunted as the savior of the housing crisis. Lenders have shown little interest in voluntarily participating in programs such as this. With no real teeth these bills are little more than a P.R. effort.
Many inside the beltway are in agreement that Frank and Dodd will "steamroll" these bills through their respective chambers. That is not to say final passage of a bill is a foregone conclusion as the bills differ in a number of areas and these differences would have to be worked out. However, at the core of both bills is utilizing FHA to insure troubled mortgages.	What the market is currently experiencing is nothing more than a correction of the skyrocketing home prices and home sales from the previous five years. This is nothing more than a healthy cycle in the real-estate market and the only real cure is to let it work itself out.
Premiums are deposited in funds separate from the FHA Mutual Mortgage Insurance Fund (MMIF) so it isn't at risk.	By forcing FHA to insure loans already in jeopardy of defaulting Congress is essentially bailing out lenders and homeowners using taxpayer money should the insurance premium payments and principal reductions not be sufficient.
	Is this fair? The majority of subprime loans are fixed rate and are not in danger of foreclosure. Many of these homeowners in fixed-rate subprime loans may have been offered exotic adjustable-rate loans that would have allowed them to purchase a more expensive home then they actuality could have afforded. Instead these homeowners took sensible loans with higher interest-rates that they knew they could afford. Now irresponsible

	homeowners who took out a loan they could not afford may wind up with a lower interest rate and have their mortgage principal reduced.
	While the Frank bill separates the program funds from the MMIF, it does place them in the fund that is used to support other programs and would place them in jeopardy.

Outlook:
The House has passed Frank's bill as part of their Housing Stimulus Package.

When the Senate proposed and passed its housing stimulus package, Dodd's bill was not included in it. Dodd has since included it in a recently introduced GSE Reform bill that has been marked up out of his Senate Banking, Housing, and Urban Affairs Committee.

NAR Policy:
At the NAR May 2008, Business Meetings, the following policy was adopted:
"That NAR support the use of the FHA mortgage insurance program to help homeowners refinance their mortgages. Any such program should include safeguards to protect the original mission and goals of FHA, and the American taxpayer from risk."