Written Statement

of the

NATIONAL ASSOCIATION OF REALTORS®

submitted to the

House Financial Services Committee
Subcommittee on Housing and Community Opportunity

On

"Transforming the Federal Housing Administration for the 21st Century**"**

April 5, 2006

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The NATIONAL ASSOCIATION OF REALTORS® represents a wide variety of housing industry professionals committed to the development and preservation of the nation's housing stock and making it available to the widest range of potential homebuyers. The Association has a long tradition of support for innovative and effective Federal housing programs and we work diligently with the Subcommittee and the Congress to fashion housing policies that ensure Federal housing programs meet their mission responsibly and efficiently.

While the homeownership rate continues to rise, there are still many hard-working families that simply cannot qualify for a conventional mortgage. Minority homeownership rates are significantly lower than the national average—around 50%, compared with nearly 70% for the nation as a whole. The homeownership rate for African American households the first quarter of 2005 was 48.8 percent, while Hispanic households were at 49.7 percent. The homeownership rate for Asian, Native Americans, and Pacific Islanders was 59.4 percent. By comparison, 76.0 percent of non-Hispanic whites were homeowners.

FHA's single-family mortgage insurance program is a valuable government program that has proved highly beneficial in helping low-, moderate-, and middle-income people achieve the dream of homeownership. FHA insurance is available to individuals regardless of their racial, ethnic or social characteristics and its universal availability helps stabilize housing markets when private mortgage insurance is nonexistent or regional economies encounter disruptions. We believe that the FHA program can be empowered with tools to close the minority homeownership gap and keep homebuyers from risky loan products currently being provided by the conventional and sub-prime markets.

It is important to note that FHA is NOT a lender. The argument that FHA will take the market away from lenders is simply false. FHA simply insures safe and fairly-priced mortgages that are made by private lenders. It has also been argued that FHA is a subsidy that the federal government need not provide. FHA is fully self-supporting. The FHA fund is fully paid with insurance premiums paid by borrowers. There is no cost to the taxpayer; in fact FHA generates revenue for the U.S. Treasury.

A growing number of homebuyers are deciding to use one of several new types of specialty mortgages that let them "stretch" their income so they can qualify for a larger loan. Specialty mortgages often begin with a low introductory interest rate or payment plan—a "teaser"—but the monthly mortgage payments are likely to increase significantly in the future. Some are "low documentation" mortgages that provide easier standards for qualifying, but also feature higher interest rates or higher fees. Some lenders will finance 100% or more of the home's value, but these mortgages also present a big financial risk if the value of the house decreases. Mortgages such as interest-only, negative amortization, and options ARMs can often be risky propositions to borrowers. These pose severe risk burdens to consumers who may be unable to afford the mortgage payment in the future because monthly payments may increase by as much as 50% or more when the introductory period ends, or cause their loan balance (the amount you still owe) to get larger each month instead of smaller.

For many of these potential homebuyers, FHA can play a major role in meeting their homeownership aspirations without adverse consequences. FHA typically serves borrowers who have lower annual incomes, make smaller down payments, and purchase less expensive homes. However, FHA's market share has been dropping in recent years. In the 1990s FHA loans were about 12% of the market. Today, that rate is closer to 3%. As the market has changed, FHA must also change to reflect consumer needs and demands. Conventional and sub-prime lenders have been expanding their products and offering more types of loans to more types of borrowers. However, not all of these loans are in the best interest of the borrower. If FHA is enhanced to conform with today's mortgage environment, many borrowers would have available to them a viable alternative to the riskier products that are marketed to them.

In today's market, interest rates are low, home prices are rising, and lenders have expanded their pool of tools to offer borrowers. But will these options still be available during periods of economic uncertainty? FHA has been there for borrowers. When the housing market was in turmoil during the 1980s, FHA continued to insure loans. Following Hurricanes Katrina and Rita, FHA has continued to provide a foreclosure moratorium for borrowers who are unable to pay their mortgages while they recover from the disaster. The universal and consistent availability of FHA is the principal hallmark of the program that has made mortgage insurance available to individuals regardless of their racial, ethnic, or social characteristics during periods of economic prosperity and economic depression. FHA is the only national mortgage insurance program that provides financing to all markets at all times.

To enhance its viability in mortgage markets, the Administration is proposing a number of important reforms to the FHA single-family insurance program that will greatly benefit homebuyers nationwide. FHA is proposing to eliminate the statutory 3 percent minimum cash investment and downpayment calculation, allow for extended loan terms from 30 to 40 years, and increase the loan limits from 87 percent to 100 percent of the conforming loan limit in high cost areas and increase the floor from the current 48 percent to 65 percent of the conforming loan limit across the country.

The ability to afford the downpayment and settlement costs associated with buying a home remains the most challenging hurdle for many homebuyers. Eliminating the statutory 3-percent minimum downpayment will provide FHA flexibility to offer varying downpayment terms to different borrowers. Although housing remains strong in our nation's economy and has helped to increase our nation's homeownership rate to a record 69 percent, many deserving American families continue to face obstacles in their quest for the American dream of owning a home. Providing flexible downpayment products for FHA will go a long way to addressing this problem.

The term of a mortgage insured under the FHA single-family mortgage insurance program has traditionally been 30 years. Increasing the term would reduce the monthly mortgage payment, enable more households to qualify for a mortgage, and increase homeownership. Research conducted by the NATIONAL ASSOCIATION OF REALTORS® (NAR) shows that approximately 41 percent of American households could qualify to purchase the U.S. median priced home of $208,300 with a 30-year mortgage. This amounts to approximately 45.1 million households. Extending the term to 35 years would permit 2.1

million more families to buy a home with an FHA mortgage. Extending the term to 40 years would permit 3.6 million more families to buy a home with an FHA mortgage than they can today.

FHA mortgages are used most often by first-time homebuyers, minority buyers, low- and moderate-income buyers, and other buyers who cannot qualify for conventional mortgages because they are unable to meet the lender's stringent underwriting standards. Despite its successes as a homeownership tool, FHA is not a useful product in high cost areas of the country because its maximum mortgage limits have lagged far behind the median home price in many communities. As a result, working families such as teachers, police officers and firefighters are unable to buy a home in the communities where they work. Prospective homebuyers in high cost states should not be left behind just because of their geographic location. Increasing FHA loan limits in high cost areas will address these problems.

Under the Administration's proposal, FHA's limits for single unit homes in high cost areas would increase from $362,790 to the 2006 conforming loan limit of $417,000. Research conducted by the National Association of REALTORS® indicates that this will result in 28% more FHA originations in California and 19% more originations in Massachusetts. In non-high cost areas, the FHA limit (floor) would increase from $200,160 to $271,050 for single unit homes. The high cost increase would bring FHA loans on par with loan guarantees provided by the Department of Veterans Affairs. In 2004 President Bush signed legislation authorized by Congress to increase the Veteran's loan guarantee to 25% of the conforming loan limit. This means veterans can purchase homes using the VA loan product for up to $417,000, the current conforming loan limit.

Increasing the FHA loan limits will stimulate homebuying opportunities in all segments of the country and provide an important benefit to thousands of average income families seeking to purchase modest homes throughout all regions of the country. Increasing the high-cost maximum mortgage limit constitutes basic regional equity allowing qualified moderate-income homebuyers in high cost areas to share the benefits of FHA homeownership that FHA users in other regions of the country now enjoy. Increasing the base loan limit will enhance FHA's ability to assist homebuyers in areas not defined as high-cost, but where home prices still exceed the current maximum of $200,160. This includes states like Arizona, Colorado, Florida, Georgia, Illinois, Maine, Minnesota, Nevada, North Carolina, Ohio, Oregon, Pennsylvania, Utah, Vermont, and Washington. None of these states is generally considered "high cost" but all have median home prices higher than the current FHA loan limit.

The Administration also proposes to combine all single-family programs into the Mutual Mortgage Insurance Fund. The FHA program has four funds with which it insures its mortgages. The Mutual Mortgage Insurance (MMI) Fund is the principal funding account that insures traditional 203b single-family mortgages. The fund receives upfront and annual premiums collected from borrowers, as well as net proceeds from the sale of foreclosed homes. It is self-sufficient and has not required taxpayer bailouts.

For accounting purposes, the MMI fund is linked with the Cooperative Management Housing Insurance Fund (CMHI). The CMHI finances the Cooperative Housing Insurance program (Section 213), which provides mortgage insurance for cooperative housing projects of more than five units that are occupied by members of a cooperative housing corporation. FHA also operates Special Risk Insurance (SRI) and General Insurance (GI) Funds, insuring loans used for the development, construction, rehabilitation, purchase, and refinancing of multifamily housing and healthcare facilities, as well as loans for disaster victims, cooperatives and seniors housing.

Currently, the FHA condominium loan guarantee program and 203k purchase/rehabilitation loan guarantee program are operated under the GI/SRI Fund. NAR strongly supports inclusion of these programs in the MMIF. In recent years programs operating under the GI/SRI funds have experienced disruptions and suspensions due to funding commitment limitations. Because the multifamily housing programs are under the GI/SRI funds and thus susceptible to future funding expirations, maintaining the single family programs under the GI/SRI funds would expose these programs to possible future disruptions. Thus, from an accounting standpoint, it makes sound business sense to place all the single-family programs under the MMIF.

Besides combing the 203(k) and condominium programs under the MMIF, NAR also recommends key enhancements to increase the programs' appeal and viability. Specifically, NAR recommends restoring investor participation in the 203(k) program. We also recommend that HUD lift the current owner-occupied requirement of 51 percent before individual condominium units can qualify for FHA-insured mortgages. The policy is too restrictive because it limits sales and homeownership opportunities, particularly in market areas comprised of significant condominium developments and first-time homebuyers. In addition, the inspection requirements on condominiums are burdensome. HUD has indicated that it would provide more flexibility to the condo program under the MMIF. We strongly support loosening restrictions on FHA condo sales and 203k loans to provide more housing opportunities to homebuyers nationwide.

The NATIONAL ASSOCIATION OF REALTORS® recognizes that homeownership is a primary goal of American families. Housing has always been and continues to be one of the highest personal and social priorities in America with study after study affirming that a large proportion of Americans would rather own than rent a home. Homeownership directly benefits society by fostering pride and participation in one's community, encouraging savings and promoting social and political stability. Homeownership has been emulated on television, romanticized in literature, and coveted in the popular social consciousness. It is advocated by private enterprise and encouraged by government policy. Clearly, it is the proud achievement of most American families, the ultimate assimilation for generations of immigrants to this country, and the pinnacle for Americans generally as they climb the ladder of economic success.

The NATIONAL ASSOCIATION OF REALTORS® applauds the private sector for the recent development of innovative and affordable housing products that are providing housing opportunities for many deserving families. However, not all needs are being met, and some homeowners may not be in a loan that is appropriate for them. Consequently, the NATIONAL ASSOCIATION OF REALTORS® steadfastly maintains that government mortgage programs in general and the Federal Housing Administration in particular represent the most important source of homeownership for many American families. FHA provides a homeownership tool that provides security and stability to homeowners. We urge you to seriously consider these reforms to the FHA single-family home loan guarantee program to ensure all homeowners are afforded the true dream of homeownership.