



August 13, 2010

The Honorable David Stevens
Assistant Secretary for Housing and Federal Housing Commissioner
Department of Housing and Urban Development
451 7th Street, S.W.
Washington, D.C. 20410-0500

Re: **Docket No. FR-5404-N-01**
Federal Housing Administration Risk Management Initiatives: Reduction of Seller Concessions and New Loan-to-Value and Credit Score Requirements

Dear Assistant Secretary Stevens:

The Mortgage Bankers Association (MBA)¹ appreciates the opportunity to comment on the proposed guidance for the Department of Housing and Urban Development, Federal Housing Administration (FHA) Risk Management Initiatives: Reduction of Seller Concessions and New Loan-to-Value and Credit Score Requirements. Upon final completion of the rule, FHA will make significant programmatic changes that will affect potential future homeowners.

First, the proposed rule change would reduce the limit on seller concessions from its current six percent to three percent. Second, the change would introduce a minimum decision credit score of at least 500 and reduce the maximum loan-to-value (LTV) for all borrowers with decision credit scores of less than or equal to 579 to 90 percent LTV. Third, the change would be a tightening of manual underwriting standards, including new requirements of at least one month reserves and stricter debt-to-income (DTI) ratios. FHA is proposing these changes to improve risk management of the Mutual Mortgage Insurance (MMI) Fund – the largest of FHA’s insurance funds – and to help improve the capital ratio of this fund.

¹ The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 280,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,200 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mortgagebankers.org.

MBA's Position

MBA supports FHA's efforts to maintain financial stability and to improve risk management. Our members agree that modifications in FHA policy are necessary to ensure the safety and soundness of the MMI Fund and we are willing to work in a partnership with FHA to implement meaningful changes. We caution HUD to ensure policies do not reach too far and needlessly discourage home buying at a time when the housing market is still fragile.

A. Reduction of Seller Concessions

FHA proposes to reduce the six percent limitation of seller concessions to three percent, primarily because FHA's data indicates that borrowers who receive more than three percent in seller concessions had a higher risk of losing their homes than those borrowers with fewer concessions from 2005 to 2008. MBA supports a reduction of the current six percent maximum seller concessions; however, we believe that the maximum should be reduced to four percent, not three percent. FHA should align its cap with the four percent limit of Department of Veterans Affairs (VA) Loan Guaranty Program. VA's delinquency rate is below FHA's rate, despite the fact that most VA borrowers do not make a down payment.

MBA recognizes the difficulty in establishing robust risk management protocols that do not unnecessarily impede access to credit by responsible borrowers. Therefore, MBA believes the seller concession limit should be considered within the context of other risk management-related policy changes implemented by FHA during the past year. These changes include hiring a chief risk officer, limiting cash-out refinances, clarifying appraisal practices, and tightening condominium policies. Moreover, within the next 60 days, FHA will implement a new premium structure that raises the annual premium from 55 basis points (bps) to 85 bps or 90 bps, depending on the loan-to value ratio. MBA believes these changes, coupled with a four percent seller concession limit, strike the right balance between protecting the MMI Fund and serving as a credit source for responsible borrowers.

At a time when the housing market is slowly showing signs of recovery, MBA does not think that it is appropriate to make policy changes that could negatively impact the purchase market, especially the first-time homebuyer segment, which serves as a catalyst for the overall market. According to MBA's August 4 Weekly Application Survey, the unadjusted Purchase Index increased 1.5 percent compared with the previous week, was up 7.1 percent relative to four weeks previous, but was 33.7 percent lower than the same week one year ago. This data indicates that while the market is showing signs of progress, it has a long way to go before it reaches a full recovery.

FHA highlights that conventional mortgage lenders have capped seller concessions at three percent of the sales price on loans with LTV ratios similar to FHA. MBA however

believes that mirroring conventional standards, for this policy, is not appropriate. The core population that FHA serves is minorities, low-to moderate income families, and first-time homebuyers. Given its mission, FHA has a responsibility to ensure that its programs have reasonable flexibilities that do not exist in the conventional market. MBA believes that having a slightly higher seller concession cap is reasonable, since FHA's core population generally has limited resources to allocate towards settlement costs, the difference between three percent and four percent can be substantial to first-time or low-to moderate- income homebuyers who may have saved for years in order to purchase homes. For example, if the seller concession limit was three percent, a borrower who purchased a \$192,750 home would be limited to a maximum concession of \$5,782.50. (See Attachment A.) If the limit was four percent, this borrower's maximum concession would be \$7,710 - a sizeable difference of \$1,927.50 to homebuyers within FHA's borrower demographics. Homebuyers with FHA insurance still must have a down payment of 3.5 percent for their "skin in the game," thus requiring additional funds is not necessary and could prevent some homebuyers from purchasing a home, or could deprive cash-strapped homebuyers of the opportunity of increasing their reserves.

MBA believes that a four percent maximum seller concession covers most closing costs and prepaids for most borrowers. For example, for an average FHA purchase price of \$192,750 (\$190,188 loan amount), the estimated closing costs and prepaids total \$6,599.95, or approximately 3.42 percent (see Attachment A). With MBA's proposed limit, most borrowers' costs can be absorbed by the four percent cap and there is not room to add extraneous costs, which is a prime concern for FHA.

Notably, decreasing the seller concessions disproportionately negatively impacts the homebuyer with the lower loan amount and MBA requests special consideration by FHA on implementing any new policy in lower-cost geographic areas. As shown in Attachments B and C, despite a reduction in loan amount, closing costs are generally fixed and thus represent a greater percentage of lower loan amounts than higher loan amounts. For example, in Attachment B, the borrower's purchase price is \$100,000 and the estimated closing costs and prepaids total \$5,053.03, or 5.05 percent of the home price. Attachment C is a more extreme example, where a home that costs \$75,000 has estimated closing costs of \$4,427.84, or 5.9 percent of the purchase price. Lower-cost areas and the ones hardest-hit by the recession, such as Pittsburgh, Pennsylvania (median sales price of \$116,000), Akron, Ohio (median sales price of \$95,000), Grand Rapids, Michigan (median sales price of \$91,000), Chattanooga, Tennessee (median sales price of \$113,000), and Las Vegas, Nevada (median sales price of \$137,000)² will experience the most severe impact of the policy change. Although specific costs vary by market, capping the seller concession limit at four percent instead of three percent would help provide additional support for lower loan amounts, where closing costs often exceed three percent of the sales price or appraised value of the home.

² *Median Sales Price of Existing Single-Family Homes for Metropolitan Areas*, National Association of Realtors. 2010.

The FHA proposed rule includes data that claims to show a correlation between borrowers who received more than three percent in seller concessions and high claim rates between 2003 and 2008. FHA uses this data to support why three percent should be the cap for seller concessions. MBA, however, believes that it is important to note that the highest claim rates for loans with concessions above three percent were in years 2003 through 2006, when seller-funded down payment assistance (SFDPAs) was permitted and, thus those loans are included in the high claim rates.

FHA and the industry are well aware that some unscrupulous “charity” organizations offered SFDPAs as “zero-down” FHA loans. Through a seller “donation” to the SFDPAs charity, typically the amount equal to the then-required three percent down payment, the homebuyer had the funds for the down payment via a “gift.” In most cases the gift was added to the sales price, requiring repayment by the borrower. The default rate on SFDPAs loans is notoriously high and the independent auditor in the Fiscal Year (FY) 2009 Actuarial Report notes that “if the FHA had not insured any loans with seller-funded down payment assistance, the net capital ratio today would still be above the statutory required two percent.” FHA ended SFDPAs in 2008, which is also when the claim rate for the loans with concessions above three percent dramatically decreased. To compare, in 2003 for loans with concessions above three percent the claim rate was ten percent; in 2008 the claim rate for these same types of loans was 1.7 percent. MBA believes that FHA should not penalize future borrowers for a past policy that no longer exists.

Also, MBA requests FHA to clarify its definition of “third party contribution.” Lender-paid closing costs should be excluded from any seller concession limit. MBA agrees with the current definition of “interested parties” in Handbook 4155.1 section 9.1, which only includes real estate agents, builders, and developers – not lenders.

MBA wants to emphasize that policy changes that require systems modifications do require a significant amount of preparation time for lenders. If FHA issues a final version of this proposed rule, we request a minimum of 90 days to implement any changes.

B. New LTV Ratio and Credit Score Requirements

MBA agrees that a minimum credit score is necessary to support responsible lending and the FHA proposed minimum score of 500 is acceptable. Moreover, MBA supports FHA’s proposal to reduce the maximum LTV to 90 percent, if the borrower’s credit score is equal to or below 579.

MBA appreciates that FHA recognizes that borrowers with lower credit scores have substantially higher risk than borrowers with better payment histories and thus, the risk to lenders is significant. Some lenders have taken necessary precautions by instituting their own requirements to ensure responsible underwriting and to prevent having to

indemnify FHA for loans in the future. Indemnification is a serious issue. Lenders incorporate sophisticated quality control systems to minimize their exposure to these liabilities. MBA believes that lenders may be more flexible with their requirements if FHA assures them that indemnifications will only be incurred for egregious errors, such as substantiated fraud, and not for standard material findings or life events.

Moreover, with current FHA policies, originators and servicers will be negatively impacted if they originate and service these higher-risk loans. Given the poor creditworthiness of these borrowers and the predictive quality of the credit scores, the risk of the loan defaulting in the future is great, thus impacting the originator's Credit Watch score and causing the servicer to incur unnecessary costs and losses. Without a change in both Credit Watch and servicer borne costs (such as amending the curtailment of debenture interest and partial reimbursement of foreclosure expenses rules) in the event of a default and foreclosure, mortgage companies will not find it prudent to make these loans. Servicers will not be inclined to purchase the servicing for this product. MBA would welcome the opportunity to talk about ways to avoid negatively impacting originators and servicers that may assist in increasing the number of low-credit score refinances with principal writedowns.

Additionally, MBA requests the following clarifications of the policy to facilitate implementation:

1. Make clear the definition of a "valid credit score," specifically in regards to trade lines?
2. Provide additional information on how to treat nontraditional credit scores. For example, is a zero credit score eligible for a 96.5 percent LTV?

C. Manual Underwriting

MBA supports FHA's proposed policy of reducing the number of, and defining specific, compensating factors. We request the following clarifications of the policy to facilitate implementation:

1. Clarify what FHA considers "significant" additional income in regards to its second compensating factor.
2. Make clear whether "documented cash reserves in the amount of 3 total monthly mortgage payments" considered the third compensating factor?

FHA also requested feedback on a policy for borrowers whose housing expense exceeds requirements, but who have no, or minimal debts, for example a borrower with a 36/36 DTI ratio. In these cases, MBA recommends that FHA consider allowing the option of two out of the following three compensating factors:

1. A 24-month housing history with decrease or minimal change;
2. Revolving and installment usage pattern should support history of limited use; and,

3. DTI ratios not to exceed 40/43.

Conclusion

MBA appreciates the effort of FHA in providing increased risk management policies to ensure the future financial security of its insurance funds. We look forward to working with you to advance this goal. Please contact Tamara King at (202) 557-2758 or tking@mortgagebankers.org if you have any questions.

Sincerely,

A handwritten signature in black ink that reads "John A. Courson". The signature is written in a cursive style with a large initial "J" and "C".

John A. Courson
President and Chief Executive Officer
Mortgage Bankers Association

Attachments

Attachment A

COST ESTIMATE

Date: Tuesday, August 10, 2010

Borrower(s): Sample Buyer		Subject Property: TBD	
Loan Program: FHA Fixed			
Interest Rate: 4.500%	Annual Percentage Rate: 5.399%	Term: 360 months	
Purchase Price: \$ 192,750.00	Down Payment (%): 3.50%		
Loan Amount: \$ 186,003.75	Down Payment (\$): \$ 6,746.25		
Total Loan Amount: \$ 190,188.00			
LTV: 98.67%	CLTV: 98.67%		
Costs Associated with the Loan:		Costs Associated with Title:	
Loan Origination Fee 1 pts: \$ 1,860.04	Settlement of Closing Fee \$ 305.00	Loan Discount Fee 0 pts: \$ -	Lenders Title Policy \$ 562.00
Appraisal Fee \$ 400.00	Owners Title Policy* \$ 1,049.00	Credit Report \$ 13.00	*Typically paid by seller \$ -
Lender's Inspection \$ -	Endorsements \$ 150.00	Lender Loan Fee \$ 1,450.00	Courier Fee \$ -
VOE/VOD \$ -	Email Document Fee \$ -	Appraisal Review Fee \$ -	Notary Fee \$ 50.00
	Signer Fee \$ -		Misc. Fees \$ 150.00
	Recording Fee \$ 65.00		
	Total Estimated Closing Costs: \$ 5,005.04		
Fees Associated with Property:			
HOA Transfer Fee \$ -			
Home Warranty \$ -			
Pest Inspection \$ -			
Septic Inspection \$ -			
Items Required by Lender in Advance:		Reserves Deposited with Lender:	
Interest for 15 day(s) \$ 351.75	Hazard Insurance 1 month(s) \$ 5 5.47	Hazard Insurance Prem. \$ 665.64	Mortgage Insurance \$ -
Flood Insurance Prem. \$ -	City Property Insurance \$ -	Mortgage Insurance Prem. \$ 3,255.07	Property Taxes 5 month(s) \$ 5 22.05
VA Funding Fee \$ -	Flood Insurance \$ -		
	Total Estimated Reserve/Prepays: \$ 4,849.98		
Total Estimated Monthly Payment:		Total Estimated Funds Needed to Close:	
Principal & Interest \$963.65	Purchase Price/Payoff \$ 197,750.00	Other Financing \$ -	Total Estimated Closing Costs \$ 5,005.04
Hazard Insurance \$ 55.47	Total Estimated Reserve/Prepays \$ 4,849.98	Real Estate Taxes \$ 104.41	Total Costs: \$ 202,605.02
Mortgage Insurance \$ 85.04	Loan Amount \$ 186,003.75	HOA Dues \$ -	FHA UFMIP/VA FEE Financed \$ 4,185.00
Other \$ -	Seller Paid Closing Costs \$ -		Earnest Money (Need to Verify) \$ -
	Total Credit: \$ 190,188.75		
Total Monthly Payment: \$ 1,208.57	Cash from/to Borrower: \$ 12,416.27		
<i>Total Estimated Closing Costs + Total Estimate Prepays – Upfront Mortgage Premium = Settlement Costs.</i>			

Attachment C

COST ESTIMATE

Date: Wednesday, July 28, 2010

Borrower(s): Sample Buyer		Subject Property: TBD	
Loan Program: FHA Fixed			
Interest Rate: 4.500%	Annual Percentage Rate: 5.399%	Term: 360 months	
Purchase Price: \$ 75,000.00	Down Payment (%): 3.50%		
Loan Amount: \$ 2,375.00	Down Payment (\$): \$ 3,625.00		
Total Loan Amount: \$ 73,003.44			
LTV: 98.67%	CLTV: 98.67%		
Costs Associated with the Loan:		Costs Associated with Title:	
Loan Origination Fee 1 pts: \$ 723.75	Settlement of Closing Fee \$ 218.00	Loan Discount Fee 0 pts: \$ -	Lenders Title Policy \$ 341.00
Appraisal Fee \$ 375.00	Owners Title Policy* \$ 625.00	Credit Report \$ 13.00	*Typically paid by seller \$ (625.00)
Lender's Inspection \$ -	Endorsements \$ 150.00	Lender Loan Fee \$ 1,450.00	Courier Fee \$ -
VOE/VOD \$ -	Email Document Fee \$ -	Appraisal Review Fee \$ -	Notary Fee \$ 50.00
	Signer Fee \$ -		Misc. Fees \$ 150.00
	Recording Fee \$ 65.00		
Fees Associated with Property:			
HOA Transfer Fee \$ -			
Home Warranty \$ -			
Pest Inspection \$ -			
Septic Inspection \$ -			
		Total Estimated Closing Costs:	\$ 3,535.75
Items Required by Lender in Advance:		Reserves Deposited with Lender:	
Interest for 15 day(s) \$ 136.80	Hazard Insurance 1 month(s) \$ 34.78	Hazard Insurance Prem. \$ 417.36	Mortgage Insurance \$ -
Flood Insurance Prem. \$ -	City Property Insurance \$ -	Mortgage Insurance Prem. \$ 1,628.44	Property Taxes 5 month(s) \$ 303.15
VA Funding Fee \$ -	Flood Insurance \$ -		
		Total Estimated Reserve/Prepays:	\$ 2,520.53
Total Estimated Monthly Payment:		Total Estimated Funds Needed to Close:	
Principal & Interest \$374.96	Purchase Price/Payoff \$ 75,000.00	Other Financing \$ -	Total Estimated Closing Costs \$ 3,535.75
Hazard Insurance \$ 34.78	Total Estimated Reserve/Prepays \$ 2,520.53	Real Estate Taxes \$ 60.63	Total Costs: \$ 81,056.28
Mortgage Insurance \$ 32.93	Loan Amount \$ 72,375.00	HOA Dues \$ -	FHA UFMIP/VA FEE Financed \$ 1,628.00
Other \$ -	Seller Paid Closing Costs \$ -		Earnest Money (Need to Verify) \$ -
	Total Credit: \$ 74,003.00		
Total Monthly Payment: \$ 503.30	Cash from/to Borrower:		\$ 7,053.28
<i>Total Estimated Closing Costs + Total Estimate Prepays - Upfront Mortgage Premium = Settlement Costs.</i>			