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"Promoting Bank Liquidity and Lending Through Deposit Insurance, HOPE for Homeowners, and other Enhancements"

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Chairman Frank, Ranking Member Bachus, and members of the Committee, thank you for the opportunity to speak to you today about your proposal to modify the HOPE for Homeowners Program.

My name is Meg Burns and I am the Director of Single Family Program Development for the Federal Housing Administration (FHA), and I am here representing the Secretary of the Department of Housing and Urban Development (HUD), Shaun Donovan. This past August I was appointed to serve as the Executive Director of the Board of Directors of the HOPE for Homeowners Program. As you know, the Board is composed of designees the Secretary of HUD, the Secretary of the Treasury, the Board of the FDIC, and the Board of Governors of the Federal Reserve. In my capacity as Executive Director, I am responsible for day-to-day oversight of the program. Given my direct involvement in all aspects of the program – from development of the policy guidance to industry outreach to program delivery – I am very pleased to be here today to share HUD's perspective on the HOPE for Homeowners section of your bill, HR 703. I want to emphasize that this testimony represents HUD's and not the HOPE for Homeowners Board's perspective

All of us at HUD welcome and applaud that you are proposing to make changes to the HOPE for Homeowners Program. As you are well aware, the initial program data, which we have shared with the committee each month since the program's inception, clearly indicates that changes are not only appropriate, but necessary. Furthermore, changes are needed as quickly as possible.

<u>Status of Program</u>

Let me start by reviewing the most current program data, which certainly makes the case for your proposed changes. To date, FHA has insured no loans under the program; FHA-approved lenders have taken 451 applications and 25 loans have closed. To put these figures in perspective, according to the Congressional Budget Office's original projection that the program would assist 400,000 families over three years, FHA should have insured approximately 40,000 loans by this point in time.

From my personal experience and that of my colleagues, collectively speaking to literally thousands of representatives from servicing, originating, and counseling organizations – programmatic restrictions and high costs have contributed to low participation rates.

Since the law passed, on July 30, 2008, we have conducted more than 100 outreach sessions in communities across the nation. We have a very extensive web site devoted to the program, which includes information for consumers, lenders, and counselors. We've posted comprehensive written training materials and a special webcast-webinar developed by Neighborworks America, so that people can simply listen and learn about the program. Between this aggressive educational campaign and the tremendous amount of publicity the program has received from the press, there is no doubt that homeowners in need of help are fully aware that it is available. In fact, since last September, the FHA call center has received more than 66,000consumer and industry inquires regarding the program, which represents about 45 percent of all incoming calls.

The other conjecture for low program participation is that lenders are not willing to accept losses on the existing liens – which are required to put the borrower into the new HOPE for Homeowners loan, which carries a maximum loan-to-value ratio of 96.5 percent. Even those lenders willing to accept principal write-downs report that they are having tremendous difficulty fitting borrowers into the program due to the severely restricted eligibility criteria. Moreover, we have heard an outcry from many, many counselors and consumer advocates that they cannot, in good conscience, recommend the program to struggling homeowners because the immediate and future cost to consumers is simply too high.

Support for Changes

The HOPE for Homeowners changes, proposed in HR 703, cut to the heart of the problems with the program – overly restrictive eligibility standards and extremely high costs to consumers.

We believe that modifications to the program, including the elimination of a number of the eligibility criteria could result in significant program uptake. The program restrictions have proven to be more and more difficult over time, as economic conditions have worsened.

Of particular note, the March affordability test, in particular, prevents families who have suffered financial hardship since that time from participating, unless they have an adjustable rate mortgage. Under the terms of the existing HOPE for Homeowners law, families with fixed-rate mortgages who were capable of making their mortgage payments last March, but who have lost some source of income during the past year and are now unable to afford their mortgage payments, are not eligible to participate in the program.

To the extent that the criteria were originally proposed as measures to prevent fraudulent practices from slipping into the HOPE for Homeowners program or persons who committed fraud from participating in the program, there are better ways to effectively identify and address the problem. At this stage in the mortgage crisis, program standards that effectively shut out large numbers of families in trouble may only perpetuate the foreclosure crisis. Clearly, HOPE for Homeowners is a product that is intended to help as many families as possible retain homeownership with the larger goal of breaking the cycle of foreclosures and home price depreciation affecting communities all across the nation.

The proposals to reduce consumer costs are worthwhile as well, and HUD agrees that the shared appreciation feature has been very problematic, though notes that any reduction to shared appreciation will increase the costs to the government. The way the existing law is written, borrowers are being asked to pay the Federal government for the benefit of program participation in an amount that could exceed the principal write-down they received. Under the existing HOPE for Homeowners law, there is no cap on the amount of shared appreciation, either in terms of dollars or time; a borrower can only pay off the shared appreciation mortgage by selling the home. The payment is based solely on the increase in value from the time of origination of the HOPE for Homeowners loan until the sale. If the borrower remains in the property for 20 years and the value increases by $70,000 (which is very feasible over that period of time) the obligation to the Federal government is $35,000 – even if the original principal write-down the borrower received was for, say, $20,000. In light of these concerns, HUD supports some significant change to this shared appreciation feature.

Finally, FHA appreciates and welcomes the proposed language requiring the HOPE for Homeowners program to be run in accordance with existing FHA practices. One of the comments that we at HUD made early on in implementing the program cycle was that lenders need to feel comfortable with the program to offer it and that the fewer changes they need to make to their own origination, underwriting, processing, and closing practices, the better. Every minor deviation from FHA's existing standards requires that large lenders train staff, modify systems, and establish new quality control measures. Any disparities within the loan operations of a large institution require a great deal of time and resources, both of which hinder program uptake and certainly slow lender implementation timeframes.

Appropriate Proposals that Could Benefit from Additional Modification

While HUD fully supports program changes, there are a few that could benefit from some additional consideration.

Upfront Mortgage Insurance Premium

Regarding consumer costs, again, the shared appreciation is only one expense to the consumer. Under current law, the borrower also pays an upfront mortgage insurance premium of 3 percent and an annual premium of 1.5 percent. They also pay a shared equity mortgage, which generally equals a percentage of the difference between the value of the home and the new HOPE for Homeowners loan.

The new proposal would retain the shared equity arrangement, but eliminate the upfront mortgage insurance premium altogether, and reduce the annual premium by 55 percent of the principal balance of the mortgage not to exceed 75 percent as based upon the credit risk of the mortgage.

As a guarantee program, upfront premium reduces the subsidy cost from potential losses from foreclosures and claims on the insurance fund.   The upfront premium helps to defray subsidy expenses in a way that stretches the insurance authority farther, enabling FHA to help more families in need.

HUD agrees that the upfront and annual fees are too high and that reductions are appropriate. However, additional evaluation of the impact that the complete elimination of the upfront fee would have on the total costs of the program is warranted.

Subordinate Liens

One of the key features of the HOPE for Homeowners program is the mandatory principal write-down, a feature that FHA supports in theory, but that has proven more difficult in practice. In particular, many subordinate lienholders are not willing to accept the losses that are necessary to put borrowers into a HOPE for Homeowners loan. The program currently permits an immediate payment - now set at 3 or 4 cents on the dollar – to release their liens. In markets where recovery is fairly likely, it's not clear that this incentive is sufficient.

Moreover, the mechanism by which FHA can make payments to subordinate lienholders is cumbersome, making this component of the program a real disincentive for lenders. HUD would suggest that additional discussion and consideration of this element of the program is appropriate. Clearly, HUD supports the overarching Congressional objective to reduce the borrowers' debt loads and put them into sustainable situations, but it may be possible to accomplish the objective with a stronger incentive for subordinate lienholders.

Federal Pre-Emption for Shared Equity Mortgage

Finally, the lending community has expressed tremendous concerns that the shared appreciation and shared equity mortgages, which serve as contracts between HOPE for Homeowners borrowers and HUD, may violate state laws. They are reluctant to engage in the program in states like Texas where the state laws seem to prohibit these types of loans. Some lawyers representing the lending community have suggested that FHA should develop model shared equity and shared appreciation documents for every state in the nation or Federal pre-emption of state laws. We at HUD believe that additional discussion on this issue is certainly worthwhile, to ensure that HOPE for Homeowners can be a vehicle to help struggling homeowners in every state in the nation.

Conclusion

Again, I'd like to thank you for the opportunity to participate in today's Hearing on the proposed legislation, HR 703, and commend the Committee for proposing changes to the HOPE for Homeowners Program. We look forward to discussing with you HOPE for Homeowners Program changes as well as other tools to address the mortgage crisis. I'd be happy to answer any questions you may have.