M E M O R A N D U M

To: Members of the Committee on Financial Services

From: FSC Majority Committee Staff

Date: May 13, 2013

Subject: May 16, 2013 Housing and Insurance Subcommittee Hearing on "Sustainable Housing Finance: The Government's Role in Multifamily and Health Care Facilities Mortgage Insurance and Reverse Mortgages"

On Thursday, May 16, 2013, at 2:00 p.m. in Room 2128 of the Rayburn House Office Building, the Housing and Insurance Subcommittee will hold a hearing on "Sustainable Housing Finance: The Government's Role in Multifamily and Health Care Facilities Mortgage Insurance and Reverse Mortgages." This hearing will examine the government's role in providing mortgage insurance for multifamily housing, health care facilities, and reverse mortgages, and will examine ways to reform the Federal Housing Administration (FHA).

This will be a one-panel hearing with the following witnesses:

- Mr. Charles Coulter, Deputy Assistant Secretary for Single-Family Housing, Federal Housing Administration, Department of Housing and Urban Development
- Ms. Marie Head, Deputy Assistant Secretary for Multi-Family Housing, Federal Housing Administration, Department of Housing and Urban Development
- Mr. Roger Miller, Deputy Assistant Secretary for Healthcare Programs, Federal Housing Administration, Department of Housing and Urban Development

Background

The FHA is an agency of the Department of Housing and Urban Development (HUD) that provides mortgage insurance for single-family and multifamily home loans. Within the FHA, the Office of Multifamily Housing Programs administers mortgage guarantee programs for market segments other than single-family loans and pays for them from the FHA's General Insurance and Special Risk Insurance (GI/SRI) insurance fund. Specifically, the FHA uses the GI/SRI Fund to provide mortgage insurance for loans to develop, rehabilitate, or refinance multifamily rental housing, nursing home facilities, and hospitals. The available insurance programs for these loans typically guarantee 100 percent of the long-term (up to 40 years), fully amortizing, and non-recourse principal amount of the loan.

Congress sets an annual limit on the notional value of new loans that the FHA can insure in a fiscal year, commonly referred to as the "commitment authority." The commitment authority for the FHA's mortgage insurance programs for multifamily mortgages and healthcare mortgages significantly increased from $4.3 billion in FY 2008 to $21.6 billion in FY 2012, and appears to be increasing still with each passing fiscal year. The FHA's GI/SRI commitment authority for FY 2013 is $25 billion; in HUD's FY 2014 budget request, the Administration requested $30 billion in GI/SRI commitment authority.

As the FHA's mortgage insurance commitments have increased, some have raised concern about the fiscal health of the FHA's mortgage insurance funds because of their current exposures.[1] At the end of fiscal year 2012, the GI/SRI insurance portfolio contained over 514,500 loans with a cumulative unpaid principal balance of $144.5 billion. On February 14, 2013, the U.S. Government Accountability Office (GAO) designated the FHA as a "high risk" agency in its 2013 High Risk Series Report, which is updated at the beginning of each Congress. In its section entitled, "Modernizing the U.S. Financial Regulatory System and Federal Role in Housing Finance," the GAO noted that "a weakening in the performance of FHA-insured mortgages has heightened the possibility that FHA will require funding from the U.S. Treasury to help cover its costs on insurance issued to date."

FHA Mortgage Insurance for the Multifamily Mortgage Market

Section 221(d) of the National Housing Act authorizes the FHA to insure mortgages made by private lending institutions to finance the construction or substantial rehabilitation of multifamily (five or more units) rental or cooperative housing for moderate-income families. Currently, the FHA may insure up to 90 percent of the cost of a new construction or the refinancing of an existing mortgage.

Fannie Mae and Freddie Mac, the two principal government-sponsored enterprises (GSEs) in the mortgage market, also participate in the financing of multifamily housing. While the FHA provides mortgage insurance for multifamily loans, the GSEs purchase or guarantee the multifamily mortgage-backed security, which often results in the GSEs and the FHA competing against each other in the multifamily mortgage finance market. Although multifamily loans make up a relatively small portion of the GSEs' business activities, the GSEs currently own or guarantee one-third of the total $846.3 billion in multifamily mortgages outstanding in the form of mortgage-backed securities.

There are two differences between the FHA and the GSEs' multifamily books of business. FHA multifamily mortgage insurance is primarily targeted to new construction projects, which are often located in relatively undeveloped areas with market rents higher than the region's average. The GSEs' multifamily book of business has a larger proportion of loans for affordable and specialized projects and does not include lending for new

[1] The concern about the financial health of the FHA stems also from concerns with the solvency of the Mutual Mortgage Insurance Fund, which is used to guarantee mortgage insurance for single-family homes.

construction projects. The FHA takes 100 percent of the credit risk on its multifamily loans, while the GSEs share some of their credit risk with private sector lenders.

The Mortgage Bankers Association reported that the share of outstanding multifamily mortgage debt held or guaranteed by the FHA and GSEs grew from 30 percent ($198 billion) in the first quarter of 2007 to 45 percent ($376 billion) in the fourth quarter of 2012. The FHA and GSEs together either insured or guaranteed over 50 percent of multifamily origination volume in 2011. (Total 2012 origination figures for the multifamily market will be available in the fall of 2013).

FHA Mortgage Insurance for Nursing Homes, Assisted Living Facilities, and Hospitals

The FHA's Office of Healthcare Programs (OHP) administers the FHA's mortgage insurance programs for healthcare facilities, which include the Section 232 Mortgage Insurance for Residential Care Facilities program and the Section 242 Mortgage Insurance for Hospitals program. These mortgage insurance programs enable the financing and refinancing of healthcare facility projects across the country. There are approximately 2,890 insured loans for residential care facilities and hospitals in the FHA's portfolio. According to HUD, the net claim rates are less than one percent in both programs.

Established in 1959, Section 232 of the National Housing Act—also known as "Mortgage Insurance for Residential Care Facilities"—authorizes the FHA to insure mortgages made by private lending institutions to finance the construction or renovation of nursing, assisted-living, intermediate care, or board-and-care facilities. Major equipment needed to operate the facility may be included in the mortgage, and the Section 232 program allows for long-term, fixed-rate financing for new and rehabilitated properties for up to 40 years.

Established in 1968, Section 242 of the National Housing Act—also known as "Mortgage Insurance for Hospitals" —authorizes the FHA to insure mortgages made by private lending institutions to finance the construction or rehabilitation of public or private nonprofit and proprietary hospitals and major movable medical equipment, as well as to refinance existing debt. To qualify for Section 242 mortgage insurance, a hospital facility must be properly licensed, provide community services for inpatient medical care of the sick or injured, and be able to demonstrate its need for construction, refinancing or rehabilitation. To qualify for the program, the hospital's maximum loan-to-value ratio can be no greater than 90 percent, the loan term can be no more than 25 years, and the hospital must maintain a mortgage reserve fund—a fund where the mortgagor (hospital) contributes at least one year of debt service. According to the FHA, the average loan insured under this program is approximately $70 million per hospital, with approximately 10 hospitals constructed through the FHA's mortgage insurance each year.

The FHA's Reverse Mortgage Insurance Program

The Home Equity Conversion Mortgage (HECM) program is the FHA's reverse mortgage insurance program. The HECM program permits borrowers 62 years of age or older to convert the equity in their homes into a monthly income stream (for a fixed term or for life), a lump sum payment, or a line of credit. Unlike a borrower who obtains a traditional mortgage, a HECM borrower makes no mortgage payments and is not required to meet an income or credit qualification. The program's only requirement is that the mortgage balance be paid when the last borrower named on the mortgage moves, refinances, sells, or dies. If the outstanding balance exceeds the property's value when the loan comes due, the borrower's maximum liability is the property's value. Through FY 2008, the HECM program was insured through what is now the GI/SRI Fund. Beginning in FY 2009, however, the HECM program was insured through the MMIF. In FY 2012, the FHA insured more than 54,000 HECM loans for a total of $13.2 billion.

After evaluating the performance of HECM loans in the MMIF's FY 2012 portfolio, an independent actuarial review estimated the economic value of the HECM portion to be negative $2.8 billion. The Administration's FY 2014 budget proposal further underscored the fiscal problems in the HECM portfolio, projecting that the FHA may need a $943 million infusion from the Treasury to absorb losses in the MMIF. HUD Secretary Shaun Donovan testified before the Senate Appropriations Committee on April 11, 2013, that "this potential appropriation is largely due to the existing reverse mortgage (HECM) portfolio."