Statement
of the
Mortgage Bankers Association of America
before the
Subcommittee on Housing and Community Opportunity
House Financial Services Committee

May 3, 2001

Madam Chairman and members of the subcommittee, my name is John A. Courson. I am President and Chief Executive Officer of the Central Pacific Mortgage Company, Folsom, California. I am appearing before you today in my capacity as Vice President of the Mortgage Bankers Association of America (MBA)*. Accompanying me is Howard Glaser, Senior Staff Vice President for Government Affairs. MBA is grateful to have the opportunity to testify before the Subcommittee on Housing and Community Opportunity on the important subject of the crisis in affordable housing in the United States. We look forward to working with members of the subcommittee on initiatives that will help to alleviate this serious and deepening problem.

Today, in spite of a decade of economic growth and a still strong, but slowing economy, there is a crisis in affordable housing. As would be expected, this crisis certainly affects the poorest of the poor, but it is not limited to low-income families. This is a crisis that is deepening, and that is affecting more and more of America's working families. It is hurting people in many walks of life, including teachers, police officers, municipal workers and even people who work here in Congress. It is felt in every area of the country, although it is most severe in older cities that have limited supplies of housing stock. It affects renters, those who are trying to achieve the American dream of homeownership, and even those who already own their homes.

There are many statistics that document the problem. Last year, the National Housing Conference published a groundbreaking report entitled ***Housing America's Working Families***. This report states that, in the midst of unprecedented economic prosperity, one out of every seven American families, or 13.7 million households, faces a

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*MBA is the national association representing the real estate finance industry. 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 home ownership prospects through increased affordability; and to extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters excellence and technical know-how among real estate finance professionals through a wide range of educational programs and technical publications. Its membership of approximately 2,800 companies includes all elements of real estate finance; mortgage companies, mortgage brokers, commercial banks, thrifts, life insurance companies and others in the mortgage lending field. For additional information visit MBA's Web site: www.mbaa.org.

critical housing need. A "critical housing need" is defined as paying more than 50 percent of household income for housing, or living in severely dilapidated housing. As stark as this statistic is, it is not the entire story. The number of moderate-income families facing critical housing needs is significant and growing. In 1997, 1.2 million working families with moderate incomes were in this group. By 1999, the number had grown to 1.7 million, an increase of 38 percent. Between 1997 and 1999, the number of moderate-income families at the higher end of the income scale—earning 80 to 120 percent of median income—facing critical housing needs increased by 74 percent. Every year, more and more American families, often families with one or even two full-time wage earners, cannot find or afford decent housing.

Why is there a crisis in affordable housing?

What are the causes of this crisis? Why is it getting worse? There are a number of reasons. For one thing, there is simply not enough housing stock. This is particularly true in older, more established cities, such as Boston, San Francisco and Newark. The lack of existing housing, especially multifamily housing, has made cities, such as these, virtually unaffordable for many of the people who work in them. New Jersey ranks as the least affordable state in the country, and Massachusetts ranks as number four. A minimum wage worker making $5.15 in New Jersey would have to work 131 hours *per week* to earn enough to afford the fair market rent for an average two-bedroom rental.

Although the situation is dire in cities, such as Newark, New Jersey or Boston, other parts of the country are not immune. In Green Bay, Wisconsin, a full-time worker being paid the federal minimum wage would have to work eighty-one hours a week just to pay the rent on a two-bedroom apartment. In fact, there is not a single jurisdiction in the country where a full-time minimum wage worker can afford the HUD-defined fair market rent for a two-bedroom apartment. Further, there is evidence that housing prices are continuing to rise. According to Harvard University's Joint Center for Housing Studies, rents have been rising faster than inflation for each of the last three years.

One of the basic laws of economics—supply and demand—is at play in this crisis. Rents and home prices are high, and are continuing to rise, because supply is low. There are a number of reasons why there is a shortage of affordable housing. Production of new housing, particularly that built through private/government partnerships, such as those utilizing Federal Housing Administration (FHA) programs, is very low. Existing housing that is severely dilapidated or in disrepair is not being rehabilitated, and there is not enough preservation of older multifamily and single family units.

One significant cause of the current shortage in rental housing has been FHA's recent absence from the rental housing market in many high cost areas. FHA insurance is one of the most productive tools for motivating the market to increase affordable rental housing. However, in many cities across the country, FHA has not insured any new multifamily development in several years. A recent study by the Coalition for Affordable

Rental Housing, of which MBA is a founding member, found that in 2000, in fifteen large cities the FHA failed to insure a single new development. *Last year, no new developments were funded in Baltimore, Birmingham, Boston, Cincinnati, New York City, Providence, Salt Lake City, San Francisco, Syracuse or Tampa.* In over half of these cities, including Boston, New York and Syracuse, no new units have been insured for the *past four years*. In 2000, only one project was funded in Dallas, Los Angeles and Washington, D.C. Altogether, over the past four years, fewer than 130,000 units in the entire country have been insured by the FHA. This is due to certain program constraints that will be discussed in this testimony.

On the homeownership side, while the nation's overall homeownership rate has reached an all-time high of 67.5 percent, minorities have unfortunately not achieved an equal level of homeownership. In the final quarter for which we have numbers, an impressive 74 percent of white families owned their own homes, compared to only 48 percent of African-American families and 47 percent of Hispanic families. More has to be done to help minority families achieve the dream of homeownership.

Clearly, the crisis in affordable housing is real, and it affects every congressional district in the country. The crisis has deepened during the last decade, and as the economy slows, unless Congress and the administration take action, a growing number of families will be unable to find a decent place to live.

What are some of the solutions to the crisis in affordable housing?

MBA believes that the federal government has a critical role to play in both increasing the supply of affordable rental housing and expanding home ownership. Earlier this year, MBA released *A Blueprint for Reform from the Real Estate Finance Industry: Building Communities, Expanding Homeownership, Improving Access to Credit*. This document lays out an agenda to increase affordable housing and expand homeownership. Many of the steps outlined in this *Blueprint for Reform* require only small legislative changes. Some can be achieved through simple regulatory adjustment. If implemented, we believe that these measures will have a positive impact on attracting investment to build neighborhoods, and will go a long way toward making housing more affordable and available. The recommendations contained in MBA's *Blueprint for Reform* include improving and strengthening FHA programs, increasing HUD's efficiency, enacting brownfields legislation and more.

Strengthen FHA as a source of credit for affordable homeownership. FHA was created in 1934 to increase affordable homeownership opportunities for American families, improve housing conditions in America and provide a stabilizing force for the American economy. Over the years, FHA has made capital available for the nation's single family housing market by providing government insured financing on a loan-by-loan basis. Today's FHA single family mortgage insurance program helps to provide mortgage credit to families who are underserved or not served at all by the private mortgage insurance market. The FHA program is a stabilizing influence in the nation's housing markets at times and in places where private mortgage insurance is not in sufficient supply.

Increase the FHA multifamily mortgage insurance loan limits. FHA multifamily mortgage insurance has traditionally been a key financing mechanism for the production of housing in urban areas, but the maximum mortgage limits have not been increased since 1992, making the programs unworkable in most areas. An increase in the FHA multifamily loan limits would be a first step in addressing part of this problem. MBA is pleased that both Department of Housing and Urban Development (HUD) Secretary Martinez and Chairman Roukema favor a 25 percent increase in the loan limits. MBA supports HR 1629, "The FHA Multifamily Housing Mortgage Loan Limit Adjustment Act of 2001", which was introduced by Chairman Roukema and Representative Barney Frank on April 26. FHA maximum mortgage limits should be indexed to reflect future cost increases, and maximum high cost percentages should be increased to allow for production in extremely expensive markets such as New York City, Boston and San Francisco. During an April 26 hearing on the HUD budget, Secretary Martinez, in response to a question from a member of the subcommittee, stated that he would consider indexing any increase to allow for inflation and market differences.

Reform credit subsidy. Effective for FY1992, the Federal Credit Reform Act changed the budgetary treatment of credit programs, including loan guarantee programs. In addition to estimating the losses from anticipated defaults on loans in its current portfolio, FHA is required to estimate the net costs to the government of insuring new mortgage loans. Also, agencies must have budget authority to cover the projected costs of a program to the government, before new loan guarantee commitments are made. The act requires FHA to determine, on an annual basis, an appropriate loan loss reserve—known as credit subsidy—for each of its programs. FHA management must accumulate sufficient, relevant and reliable data that provide a sound basis for the agency's estimates of future loan performance.

HUD and OMB have maintained that the FHA new construction programs required an annual appropriation of credit subsidy based on the prior default experience of the programs. It has become increasingly difficult to accurately project the amount of credit subsidy needed each year. The critical nature of the credit subsidy appropriation became apparent last month. Due to increased demand for the programs, a backlog of unfunded projects at the beginning of the fiscal year and an inadequate appropriation to cover this need, HUD ran out of credit subsidy for FY 2001 on April 19 and shut down the programs in the General Insurance and Special Risk Fund (GI/SRI Fund) that require credit subsidy.

This is a critical situation. Unless some action is taken the new construction or substantial rehabilitation of over 55,000 apartments with a total mortgage amount of over $3.75 billion will not take place. Without these funds, these projects will not be built and developers who have invested hundreds of thousands of dollars in up-front costs for land options, plans and specifications and other pre-development costs will lose those investments. In addition, this opportunity to provide an immediate economic stimulus will be lost. MBA estimates that the 55,000 units would generate over 80,000 new jobs, $3.4 billion in new income to workers and business owners, over $400 million in new local taxes and fees and over $850 million in new federal taxes. All of this would result from an appropriation of only $155 million.

There are several steps that can be taken to ensure that both the current and long-term problems with the FHA multifamily credit subsidy are resolved. First, we urge the administration to comply with the restrictions placed on the appropriation of $40 million in credit subsidy included in the "Legislative Appropriations Act, 2001" passed last December. Release of these funds would result in the immediate reopening of the multifamily new construction and substantial rehabilitation programs. This $40 million, which has already been appropriated, will provide for the new construction or substantial rehabilitation of over 15,000 units of rental housing with a mortgage amount of over $1 billion. Second, MBA believes that an additional appropriation of $115 million for FY 2001 would provide sufficient funds to keep the programs operational for the entire fiscal year.

Finally, with regard to credit subsidy, MBA seeks the support of members of the subcommittee for legislation that would allow the use of the profits generated by programs in the GI/SRI Fund—negative credit subsidy—to fund programs that experience a shortfall in credit subsidy. Representatives LaFalce and Frank have introduced "The FHA Shutdown Prevention Act" (HR 1481) that would allow negative credit subsidy made by programs within the GI/SRI Fund to be used in the event of a future shortfall in credit subsidy. This legislation presents one alternative to the current credit subsidy appropriations procedure.

Delay any increase in the Mortgage Insurance Premium. The administration has proposed a 60 percent increase in the annual mortgage insurance premium for its basic new construction and substantial rehabilitation program so that this program will not require an appropriation of credit subsidy. MBA believes that such an increase is unjustified and unnecessary. The Section 221 (d)(4) program has had an excellent track record over the past thirteen years. Even with the housing recession in the early 1990s, the claims rate on these loans has been less than 5 percent. MBA is working with OMB and HUD to ensure that the assumptions used in their credit subsidy calculations reflect the types of loans currently being underwritten, as required by the Federal Credit Reform Act. Once the assumptions are accurate, if they demonstrate a need for an increase in the mortgage insurance premium to make the program break even, we will not object to an increase. However, with the current formula and assumptions, the 30 basis point increase in the Mortgage Insurance Premium (MIP) from .50 to .80 percent will, we believe, have the unintended consequences of increasing rents and making many projects unfeasible.

Expand FHA's adjustable rate mortgage (ARM) product line. The Fiscal Year 2002 budget for HUD authorizes a new ARM product—hybrid ARMs—for FHA. MBA fully supports this action.

Hybrid ARMs have an initial fixed interest rate period of at least three years and thereafter the interest rate adjusts annually. These are commonly referred to in the industry as 3/1, 5/1, 7/1, 10/1 ARMs and are common conventional loan products. Hybrid ARMs carry interest rates that are lower than fixed rate loans, but are less risky than the current one year adjustable rate mortgage offered by FHA. Thus, hybrid ARMs strike a more appropriate balance between affordability and risk than do one-year ARMs. The current 30 percent limit on the percentage of FHA business that can be ARMs should be increased to 40 percent to accommodate the hybrid ARM program.

MBA also supports the following changes to FHA:

- The establishment of a uniform, nationwide loan limit for FHA home equity conversion mortgages (HECM) that is equal to the FHA high cost mortgage limit.

- Transfer the HECM program to the mutual mortgage insurance fund.

- Reform the treble damages penalty. Current law authorizes HUD to impose a penalty in the amount of three times the amount of an insurance claim, referred to as treble damages, for a lender's failure to engage in loss mitigation. MBA believes the treble damages penalty is excessive and could seriously jeopardize the attractiveness of servicing and originating FHA-insured loans. MBA believes that a more appropriate penalty is application of existing penalties for technical infractions or a maximum penalty of three times the amount of HUD's loss caused by the lender's willful pattern and practice of failing to engage in loss mitigation.

- Provide FHA with the authority to develop and insure new loan products, on a limited basis, as the marketplace dictates, without requiring FHA to have specific legislative authority for each loan product. This change would foster innovation and allow FHA to respond to a rapidly changing marketplace.

- Make the FHA simplified downpayment calculation permanent. Several years ago, the Congress enacted, as a pilot program, provisions to streamline and simplify the complex downpayment calculation used for FHA home mortgage loans. This simplification made it easier for FHA borrowers to understand how much of a downpayment was needed to obtain an FHA mortgage and made FHA mortgages more affordable. This simplified downpayment pilot program expires on December 31, 2002. By all accounts, the pilot program has been very successful and MBA urges Congress to make this program permanent.

Initiate a new multifamily production program. At the end of the last Congress, there was a growing consensus that the federal government should support programs that produce housing for families with critical housing needs. Many of these programs, however, are targeted to families whose incomes are below 60 percent of area median income. There is currently no program that is designed to provide rental housing for working families earning from 60 percent to 100 percent of median income who are unable to find decent, affordable housing near their work places. It is clear that there is a need for a federal program to address the housing needs of this segment of the population.

Partnering FHA mortgage insurance with an interest rate subsidy will, in most markets, encourage private production of rental housing at rents that would be within the reach of families at 60 percent to 100 percent of median income. Such a program could be used in conjunction with the low income tax credit program or vouchers, where appropriate, to meet the needs of lower income families in a percentage of the units.

Pursue brownfields development. The Environmental Protection Agency (EPA) defines brownfields as abandoned, idled or underutilized industrial or commercial facilities where expansion or redevelopment is complicated by real or perceived environmental contamination. Brownfields can present excellent redevelopment opportunities. They are an underutilized asset that could help communities address a number of issues, including revitalizing urban areas, increasing tax revenues and promoting sustainable growth.

On April 26, by a vote of 99 to 0, the Senate passed S 350, the “Brownfields Revitalization and Environmental Restoration Act of 2001”, opening the door for the clean up and redevelopment of contaminated sites. Introduced by Senator Lincoln Chafee (R-R.I.) and supported by a bipartisan group of senators, the bill seeks greater private-sector involvement in brownfields cleanup by providing certain liability protections for prospective purchasers, landowners and contiguous property holders. The bill also would increase federal brownfields remediation funding and allow states to assume greater cleanup responsibilities. The proposal now moves to the House of Representatives. MBA supports S 350, which is the first significant legislation to address the cleanup of an estimated 500,000 brownfields across the country. Passage of this legislation would significantly advance the economic prospects for recycling such properties into a broad range of productive uses, including affordable housing.

Madam Chairman, MBA appreciates the opportunity to testify, and we are happy to answer any questions you and members of the subcommittee may have. We are also happy to provide additional information in writing.