

# As the Industry Turns

Know what major changes come from July's housing act and September's GSE takeover

By **Ruth Lee**, vice president of sales, Titan Lenders Corp.

**I**N RESPONSE TO THE MORTGAGE CRISIS, the Housing and Economic Recovery Act of 2008 became law this past July. Most of the act focuses on statutory amendments that authorize the federal government to have a more direct regulatory role over the mortgage industry.

The changes didn't end there. The Federal Housing Finance Authority (FHFA), an agency created by the act to oversee Fannie Mae and Freddie Mac, placed the government-sponsored enterprises (GSEs) under conservatorship five weeks after the housing bill was signed.

Here's what you should know about the different parts of this new law, as well as the takeover of Fannie Mae and Freddie Mac.

## FHA modernization

The housing bill increased the Federal Housing Administration (FHA) loan limit from 95 percent to 110 percent of the median home price in most areas and to 150 percent of the agency limit for high-cost areas (\$625,500). This will open FHA-insured loans to the largest markets in the country, many of which were hardest hit by nonprime and Alt-A loans.

On the other hand, borrowers in lower-income areas may struggle with new FHA downpayment requirements, which have increased from 3 percent to 3.5 percent. With declining incomes, higher food and fuel prices, and reduced savings ability, this will be harder for lower- to middle-income homebuyers.

In addition, the act eliminates seller-funded downpayment assistance. The Department of Housing and Urban Development has long argued that seller-funded downpayment assistance results in higher default rates. Although nonseller-funded gift funds from nonprofits, employers, churches or family members are still acceptable, as of Oct. 1, the FHA no longer insures loans using seller-funded downpayment assistance.

The day after the housing bill was signed, legislation to reinstate the FHA's ability to insure loans with seller-funded downpayment assistance was introduced. Supporters argue that many viable borrowers will be excluded from

homeownership based on past abuses that aren't relevant to the current lending environment. As of press time, legislation to reinstate seller-funded downpayment assistance has not been passed.

## H.O.P.E. for Homeowners

Another aspect of the housing act is a program designed to help an estimated 400,000 distressed homeowners. The Home Ownership Preservation Entity (H.O.P.E.) for Homeowners program offers FHA-insured mortgages with as much as 90-percent loan to value of current market value to borrowers at risk of losing their homes.

With this temporary program, lenders must agree to reduce affected borrowers' principal balances to 90 percent of market value voluntarily and forgive any subordinate liens to qualify. Some lenders will have markets where this option is significantly more attractive than taking on foreclosures and real estate owned properties.

H.O.P.E. also requires that the borrowers can repay the loan with a 31-percent debt-to-income ratio.

Finally, homeowners will have to pay for the program by sharing their "new" equity and future appreciation with the FHA at sale or refinance on a sliding scale.

## Foreclosure relief and counseling

For communities hardest hit by foreclosures, the act allocates \$3.92 billion. These community-development block grants will allow local governments to purchase foreclosed homes at a discount for future rehabilitation or re-development.

The bill offers \$180 million to help connect distressed borrowers with their lenders to work out some plan for keeping their home.

The act also outlines help for veterans return-

ing from overseas. Returning veterans at risk of losing their homes will receive an extension on the time before foreclosure proceedings can be initiated, ranging from three to nine months. In addition to financial counseling provided for active-duty personnel and veterans, this will give those returning from abroad the time to resolve a financial crisis.

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Further, veterans with ARM loans will receive a one-year moratorium on rate adjustments when they return. Disabled veterans will receive benefits to assist in refitting their homes to serve their accessibility needs.

Military personnel who rent their homes will benefit from a moving cost if they are forced to move because of a landlord foreclosure. Finally, the U.S. Department of Veterans Affairs loan-guarantee cap was increased to help more veterans purchase homes.

## Enhanced mortgage disclosures

The housing act proposes enhanced ARM disclosures to spell out the maximum monthly payments possible under the caps and margins. The bill requires that disclosures are delivered to borrowers within the traditional three days and that the borrowers receive disclosures no later than seven days prior to closing.

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To add new teeth to Truth in Lending Act violations, the statutory penalty was increased tenfold.

### Tax credits and deductions

The housing act offers a tax credit on the lesser of 10 percent of purchase price or \$7,500 for eligible first-time homebuyers who buy their homes between this past April 9 and this coming July 1. The tax credit must be paid back in 15 years or upon sale.

Further, under current tax rules, only homeowners who itemize deductions are eligible to deduct property and state taxes. The act creates a new standard deduction of \$1,000 for married homeowners and \$500 for single homeowners, which will be available for the 1040EZ tax form.

### Licensing changes

The mortgage-reform bill also addresses originator regulation. Many offenders in the industry took advantage of the vagaries of licensing — or lack of it — among different states and markets.

Anyone that originates mortgages, including depository originators, will require licensing, registration and a unique identifier number assigned by the National Mortgage Licensing System.

The law will not pre-empt state-licensing laws, but it will establish minimum standards that states must achieve within two years. For states without current licensing or registration regulations, the legislation provides for management through the licensing system.

### GSE oversight

The housing bill included creation of the FHFA to corral regulatory oversight of the GSEs. This “new” regulator would establish minimum and risk-based capital requirements to ensure that the GSEs remain sufficiently leveraged. This agency’s takeover of the two companies has significant impact on the mortgage and housing industries.

Pre-conservatorship, the GSEs enjoyed positions as “quasi-governmental” corporations with shareholders and dividends, yet they were backed by the federal government. They owned or guaranteed nearly half of all U.S. mortgages — \$5 trillion worth. They had huge executive salaries, huge shareholder dividends and a huge lobbying budget: \$117 million over the past 10 years. Lobbying is proscribed for actual government agencies.

The quasi-governmental side of the GSEs enjoyed a qualifier for investors, inferring that the companies were “backed” by the U.S. government,

allowing them to maintain inflated investment ratings unsupported by their financials. The corporation side of the GSEs was dividend-driven, taking greater risks with investment.

Those risks were compounded by the wave of foreclosures, plummeting stock value and home depreciation, leaving both companies insolvent or close to it.

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Under the FHFA’s authority, the U.S. Department of the Treasury will guarantee the net worth of the former GSEs and open an “ultimate liquidity backstop” line of credit to them and the federal home-loan banks through the Fed until those authorities expire in December 2009. In addition, the Fed will guarantee the financial and operation solvency of Fannie and Freddie through massive purchases of “special” preferred stock.



With all its changes, only time will tell if the Housing and Economic Recovery Act has gone far enough or perhaps too far in creating a remedy for the mortgage credit crisis. For now, mortgage professionals are all probably best-served by watching closely and educating themselves on the emerging new world of the mortgage industry. 