MORTGAGE BANKERS ASSOCIATION

April 2, 2014

The Honorable Shaun L.S. Donovan
Secretary
Department of Housing and Urban Development
451 7th Street SW
Washington, DC 20410

Dear Secretary Donovan,

The Federal Housing Administration (FHA) plays an essential role in the U.S. housing finance system, especially for first-time, minority, and low- and moderate-income homebuyers. We appreciate your ongoing efforts to restore the FHA's Mutual Mortgage Insurance Fund (MMIF) to its required reserve ratio. The performance of the recent vintages validates these efforts.

However, at this stage of the Fund's recovery, we are concerned that recent increases and changes to FHA's annual mortgage insurance premium (MIP) are leaving too many creditworthy families without affordable access to credit.

From 2008 to 2013, HUD raised FHA's Single Family annual MIP five times. For a 30-year fixed-rate FHA-insured mortgage, the annual MIP increased from 0.50 percent to 1.35 percent. With these changes, a family receiving a $100,000 FHA loan today will pay over $600 per year in additional premiums than would have been required in 2008. Furthermore, in June 2013, HUD extended the requirements for MIP payments to the entire life of most loans. Previously, borrowers would stop paying the MIP once the loan-to-value (LTV) ratio on their home reached 78 percent. Together, these changes have greatly increased the cost of an FHA-insured loan for all borrowers.

In the near term, the current premium structure is pricing many creditworhty first-time buyers out of the market. Over the long run, high premiums on relatively low-risk business expose FHA to the risks of adverse selection. Recent data indicate that FHA 's recapture rate on refinances has declined since the imposition of the life-of-loan MIP. In addition, a high premium structure will over time result in higher risk borrowers – those with lower credit scores and the inability to meet downpayment requirements of other programs – turning to FHA as the "lender of last resort." Together, these trends could have a detrimental effect on the fiscal health of the Mutual Mortgage Insurance (MMI) Fund.

FHA's current risk management practices are moving the Fund toward financial health. These efforts have led to a significant improvement in the performance of 2010-2013 books of business, with those books adding approximately $31.3 billion in economic value to the Fund. However, as the fiscal standing of the Fund continues to improve, MBA urges you to consider options to help restore balance between FHA's affordability and actuarial soundness, including:

1. **Creating a "step down" for the annual MIP after a loan reaches a certain loan-to-value threshold.** MBA analysis shows that if FHA were to adopt a policy which stepped

down the MIP in year ten of the loan, reducing it to 60 bps for the balance of the life of the loan, the net present value of cash flow to FHA would remain positive under conservative assumptions. This could stem some of the early prepayments by FHA's lowest risk borrowers.

2. **Analyzing a rebalancing of the upfront and annual MIP.** MBA urges you to conduct an analysis of whether shifting some premium payments from an annual basis to an upfront premium can improve FHA affordability while still protecting the Fund. We believe that rebalancing the premium structure could make FHA-insured loans more attractive to borrowers with stronger credit profiles and reduce the threat of adverse selection to the Fund.

As you know, there is long lag time before pricing and underwriting changes show up in the performance of the fund. For this reason, it is important to anticipate the impact of current pricing and underwriting standards on the future performance of the MMIF. We think it is important for HUD to explore options for improving FHA affordability in ways that also support long-term actuarial soundness. We welcome the opportunity to discuss these ideas further with you and your staff.

Thank you for the careful consideration of our request. Please call Pete Mills (202-557-2878) or Steve O'Connor (202-557-2867) at MBA if you have any questions

Sincerely,

E.J. Burke
Chairman
Mortgage Bankers Association