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TRANSFORMING THE FEDERAL HOUSING ADMINISTRATION FOR THE 21ST CENTURY

HEARING

BEFORE THE

SUBCOMMITTEE ON
HOUSING AND COMMUNITY OPPORTUNITY

OF THE

COMMITTEE ON FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

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TRANSFORMING THE FEDERAL HOUSING ADMINISTRATION FOR THE 21ST CENTURY

Wednesday, April 5, 2006

U.S. HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON HOUSING AND
COMMUNITY OPPORTUNITY,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The subcommittee met, pursuant to notice, at 9:05 a.m., in the Rayburn House Office Building, Hon. Gary Miller presiding.

Present: Representatives Miller of California, Neugebauer, Fitzpatrick, Waters, Velazquez, Lee, Miller of North Carolina, Scott, and Cleaver.

Ex officio: Representative Frank.

Mr. MILLER OF CALIFORNIA. [presiding] Good morning. The meeting is called to order. The Subcommittee on Housing and Community Opportunity is meeting to consider the Administration's proposal on FHA, single-family mortgage insurance activities. And Commissioner Montgomery, we are glad to have you here today with us.

We welcome you today, and would like to commend you for your work to ensure that the FHA program becomes, once again, a viable option for low- and moderate income home buyers. Leadership and vision has already resulted in many regulatory improvements, and we encourage you to look at this program, and to understand that we wholeheartedly agree with what you're trying to do.

We think that it is underutilized. We think there is an opportunity here to create brokers and lenders in a—where they have the ability to participate in FHA, where we currently think they're pretty much restricted, based on the amounts in the past that we have been able to lend and to guarantee for.

Today, FHA is no longer a useful product for prospective home buyers. Working families such as teachers, police officers, firefighters, nurses, and others are faced with situations where they are unable to own a home in communities where they serve.

While FHA—created more than 70 years ago to meet the needs of those underserved by the private sector—today is not living up to its mission, and working families are left out without an affordable alternative to finance their homes.

Statutory limitations preclude the FHA from adapting to a rapidly changing marketplace. As a private sector mortgage market has become more efficient, the FHA program's inflexible rules and requirements have left it virtually irrelevant to the financing options.

In high-cost areas, this is especially true, where statutory loan limits eliminate the programs as an option for the purchase of the entry-level home. Under the current limits, FHA products are not available for home buyers in high-cost areas of the country because the maximum mortgage limits aren't much more than the housing prices.

Working families who need to qualify for FHA are effectively kept out of the program because of where they live, and where they work. In fact, I introduced H.R. 176 with Barney Frank this past year, which would raise the limits, and, I think, go a long way toward making the program a workable program.

We are looking forward today to hearing your testimony on what the Administration is planning to do. We hope you are open to suggestions. We would like to see this program work. I recognize Mr. Frank, who is not here. Mr. Miller you are recognized for 5 minutes. No opening statement? Mr. Scott?

Mr. SCOTT. Thank you, Mr. Miller. And I certainly want to thank you and Chairman Ney and Ranking Member Waters for holding this hearing on the future of the Federal Housing Administration. We should continue to evaluate the program, and to ensure that it reaches more potential homeowners.

And lenders claim that FHA requirements to obtain FHA loans have created a disadvantage for the loans, compared to conventional markets. It is possible that the reduction of FHA loans has created less competition for predatory lenders. There have also been concerns that FHA has not adapted to the modern condominium market.

In addition to considering policy changes to the FHA, Congress should also be concerned with increases in the cost of the program. The fiscal year 2007 budget proposed by the Administration would increase the current annual loan fee of FHA, multi-family rental housing loans, as well as loans for healthcare facilities. Many housing associations oppose these fees, due to their fears that these costs could inflate the cost of housing.

The FHA programs are designed to help increase home ownership among low-income Americans. And one way to help increase home ownership is to lower the downpayment required for FHA loans.

Congressman Tiberi and I have introduced the Zero Downpayment Pilot Program Act, which would do just that. Last Congress, a similar bill passed this committee, but was not ultimately approved by Congress. I urge my colleagues to move forward and support this important innovation.

While home ownership has increased in the United States, more can be done to help bring the American dream to all segments of our society. I look forward to the hearing from the witnesses today to understand how the FHA can increase its participation in the housing market. Thank you, Mr. Chairman.

Mr. MILLER OF CALIFORNIA. Mr. Frank, you are recognized for 5 minutes.

Mr. FRANK. Thank you, Mr. Chairman. I want to say that I appreciate very much your role in this issue. I know the chairman has taken the lead by introducing the bill, and I have enjoyed

working with him in the housing area, and I look forward to our working together.

I hope that this is a bill that we will, with some changes—not huge ones—be able to pass, and get enacted. I think it is a good piece of legislation. I appreciate the Administration's taking the initiative, listening to some of the suggestions we have had, and I know, given the gentleman from California's commitment here, we have a very good chance on this.

And let me say that, as is often the case, you tend to take for granted the places you agree and focus on the areas of disagreement. So I just wanted to say at the outset, I am in overwhelming agreement with this bill on most of the points. There is just one area that I want to raise, and I am glad that we're moving in this direction, but I would suggest that we move in a little different way, and that is on the risk-based premium for the lower-end people.

I very much applaud this. We have talked about increasing home ownership. And, obviously, you're not going to do that unless we reach out to people who find themselves in some difficulty.

And you know, one of the things I want to stress, when we got the data, people said, "Well, it is true that if you're black or Hispanic, the percentages show you're going to be maybe paying more for a loan, or having more difficulty in getting a loan. But that's not because of racism, it's because of the economic fact."

Well, having said that, we haven't solved the problem. Explaining that racial disparity is, in part, because of economic disparity doesn't mean we can all go home for dinner. It means that we then look at ways of dealing with that economic issue, because having this kind of racial disparity in access to home ownership isn't fair, and it's not healthy for our society and the kind of society we want to continue to build. And FHA, obviously, gives us a chance to deal with that.

My only concern is—and I appreciate when you say, Mr. Secretary, that the risk-based premium we will be charging people in the lower-end would still be lower than they would get in the private market. And as you say on page four, "The higher premiums that FHA will charge some types of borrowers are still substantially lower than they would pay for sub-prime financing," and I think that's a good thing.

But I think that they could be even lower. Here is the deal. Obviously, in extending these loans to people who would otherwise be into the sub-prime market, we are assuming that the great majority of them will be able to pay their loans. Otherwise, you wouldn't get into it. What we are saying is that there will be a higher percentage of default there.

So, the question is, okay, we are going to extend this, and a percentage of the people who get these, we know, will default because of their economic circumstance. But most of them won't. So then the question I would pose in public policy terms is this. Who should subsidize the fact that we are going to be lending money to people where there is a higher rate of default?

And my answer is that we should not ask the people who are not going to default in this stratum to subsidize the people who do. Let's subsidize them from somewhere else.

In other words, let's say to the low-income people, "Okay, we're going to lend you the money, and yes, some of the people who borrow are going to default in higher numbers, and we need to find that somewhere."

But why not cross subsidize? I don't think we need to look at this and say, "Each segment of the market has to be economically self-sufficient," especially since, as I read the budget for this bill, the project is that if we were to pass the bill exactly as is, it would be $845 million per year, I assume, in increased revenue. Although, in our budget terms, revenue is called a negative subsidy. That is, we are—negative subsidy means we are sucking money out of the borrowers, rather than giving it to them.

And I think it's a good idea for us to be able to raise some more money. But it's obviously more than we need. So the one point of difference I have—and I have spoken to the gentleman from California about this—is, look, I think it's a very good idea to try and reach out to this low-end segment, and it will help us in the predatory area.

Actually, we're working on sub-prime lending, and predatory lending, but I'm a great believer in capitalism. One of the best ways that we can get the private market to lower the rates it charges sub-prime people is to compete with them, by having an alternative place where they can go. I am all for that.

The only thing I think is—and I understand why the private market would have to charge the low-income borrowers more than high-income borrowers for interest, because of the risk of default. And let's be clear what we're talking about. We are saying given the way a rental—a loan market works, the poorer you are, the more you're going to have to pay for your house. Not a happy situation. We understand that's unavoidable in the private market; but it's not unavoidable in the public sector.

We, the Federal Government, have the ability, I think, to say, "You know what? We are not going to charge low-income people more for the loans, because some of them are going to default. We are going to find a way to make"—we want to take the risk of that default, and we will find the funds to take care of that somewhere else.

So, with that one difference—and I think we need to work it out, because I don't want to destroy flexibility and the staff of the committee have pointed out there are some broader considerations here. But if we can find a way to protect the low-income borrowers from having to pay more for the loans, then I think we have a bill that will be, I hope, overwhelmingly supported, and I appreciate the Administration's putting a very pro-housing responsible bill together. Thank you, Mr. Chairman.

Mr. MILLER OF CALIFORNIA. Thank you, Mr. Frank. The bottom line is to make the FHA program a viable mortgage option. We must ensure that the program allows for the purchase of entry-level homes.

This includes not only the elimination of the geographic barriers to utilize the program in high-cost areas, but also facilitating the purchase of entry-level homes including condos and manufactured housing. These forms of housing are an affordable option in entry level home ownership, and they should be included under this pro-

gram, if we truly want to make it help families climb the rung on the ladder of home ownership.

In addition to reforming what can be purchased in the program, we must also consider the competitiveness of FHA products are currently structured among the mortgage options available. In other words, we must explore the reasons that the program is being utilized—its available mortgage products for a potential home buyer. The answer is it's inflexible today, and burdensome processes have left many in the industry hesitant or actually unable to offer FHA products to their clients.

Technological deficiencies must be addressed. While the rest of the mortgage industry is electronically driven, the FHA program remains a dinosaur, still trying to convert from a peer-based process to an efficient electronic one. Lack of flexibility and downpayment amounts to tremendous amounts of—FHA used to be the best option for low- and moderate-income home buyers, because it had the lowest downpayment requirement. This is no longer the case.

Although the private market has developed flexible downpayment arrangements to meet the need of borrowers, the FHA programs' downpayment requirements are fixed to 3 percent.

While other mortgage products have recognized that the ability to accumulate enough cash for the downpayment assistance is universally considered to be the greatest single barrier to home ownership, the FHA program does not offer flexibility in the downpayment level. While the private mortgage insurers have adopted a risk-based premium structure, FHA does not set its insurance premiums according to the risk of the loan. As a result, low-risk borrowers pay higher premiums to subsidize the high-risk borrowers.

More Americans could qualify for a mortgage if their monthly payment were lower. To make mortgages more affordable, the FHA should have the flexibility to offer mortgages with longer terms than the traditional 30 years. In this way, borrowers would be able to purchase a home with a mortgage product that is less risky than the interest-only product that has become more popular in the housing market.

Cost-prohibitive and time consuming, financial audits and net worth requirement limits mortgage brokers' participation in the program. This means that FHA is not made available to some borrowers who would get a better deal under the program, under the sub-prime loan.

America is a home of people of different origins and different make-ups, and we need to make sure that this program fits their needs.

Mr. Cleaver from Missouri? You are recognized for 5 minutes.

Mr. CLEAVER. Thank you, Mr. Chairman. I would like to thank the chairman and ranking member for successfully scheduling this hearing today. And I would like to also thank our witnesses for joining us this morning.

We face a tremendous challenge at this moment in our Nation's history. And one of our great challenges is to provide every American a safe and affordable place to call home.

We met last week to discuss the countless deficiencies in the HUD budget proposed by the Administration, and we will see to-

morrow and Friday what happens to the House budget resolution when it is considered on the Floor.

But I believe all of us agree that we have got to be creative in finding additional ways to provide homes to every American who needs one. Revitalizing FHA is a timely undertaking, and I believe that we can provide more housing to low- and moderate income Americans if FHA is in full operation. FHA, created in 1934, at the very height of the Depression, was a very valuable tool then, and I think it can be again.

I met last week with a Missouri brokers association, and they mentioned some of the remarks that you recently made about FHA. And they are concerned today that the FHA program, which once had 40 percent of the market share, now only has 3 percent. I don't know if those numbers are accurate or not. That's what they gave me.

And it seems to me that FHA could help us address some of the pressing housing needs, particularly for low-income Americans. And so, I look forward to your comments today, and for an opportunity to exchange some views with you. Thank you, Mr. Chairman.

Mr. MILLER OF CALIFORNIA. Thank you. For the record, I would like to enter the statements of the National Association of Realtors; the Manufactured Housing Institute; the Manufactured Home Ownership Association for Regulatory Reform; the National Reverse Lenders Association; the National Multi-Housing Council; and the National Association of Real Estate Brokers Investment Division. Without objection, those are entered into the record.

Brian Montgomery is the Assistant Secretary of Housing for HUD. He is the Federal Housing Commissioner at the Department of Housing and Urban Development. Prior to joining HUD, Mr. Montgomery was the Deputy Assistant to the President at the White House.

From 1995 to 1999, he served in the administration of Governor George W. Bush as communications director at the Texas Department of Housing and Community Affairs and the Texas Department of Economic Development. Welcome, Mr. Montgomery.

STATEMENT OF THE HONORABLE BRIAN D. MONTGOMERY, ASSISTANT SECRETARY FOR HOUSING, FEDERAL HOUSING COMMISSIONER, DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

Mr. MONTGOMERY. Thank you very much. Thank you, Chairman Miller and Ranking Member Waters. I would also like to thank Ranking Member Frank for inviting me here today to testify in the Administration's FHA Modernization Act. I ask that my written testimony be entered for the record.

The bill itself is really very simple, the proposal straightforward. It does just what the name suggests. It modernizes the 72-year-old Federal Housing Administration, and restores the agency to its intended place in the mortgage market. Nothing more, nothing less. Yet the impact of this bill, we believe, will be tremendous. And let me explain.

FHA was created in 1934 to serve as an innovator in the mortgage market, to meet the needs of citizens otherwise underserved

by the private sector, to stabilize local and regional housing markets, and to support the national economy. This mission is still very relevant, perhaps now more so than ever. And most of us would agree that FHA can and should continue to play its important role.

Unfortunately, over the last several years, the housing agency that helped bring the Nation out of the Depression, the agency that helped our grandparents and helped our parents buy their first homes, the agency that stood by the oil States and the rust belt States in the 1980's was falling way behind.

For example, over the last 5 years, in Congressman Tiberi's district, FHA volume dropped 44 percent. For Congresswoman Harris, volume dropped 74 percent. And for Ranking Member Waters, volume has all but disappeared, declining 98 percent.

Without a viable FHA, many home buyers, first-time home buyers, minority home buyers, and home buyers with less than perfect credit, were left with fewer safe and affordable options. Many home buyers turned to high-cost financing, and non-traditional loan products to afford their first homes.

All that said, the FHA Modernization Act is part of the solution. FHA reform is designed to give home buyers who can't qualify for prime financing a choice again—we believe, a better alternative.

Now, let me explain the simple changes we're proposing. For one, we are proposing to eliminate the complicated downpayment calculation, and the traditional cash investment.

Last year, 43 percent of first-time home buyers purchased their homes with no downpayment. Of those who did put money down, the majority put down 2 percent or less. The downpayment is the biggest barrier to home ownership in this country, and this Act proposes to permit borrowers to choose how much to put down, from no money down to 1- or 2-, or perhaps even 10 percent.

The bill also proposes to provide FHA the flexibility to set the FHA insurance premiums commensurate with the risk. We would charge lower credit risk borrowers a lower insurance premium and higher credit risk borrowers a slightly higher premium.

With this risk-based premium structure, we can reach hard-working credit-worthy borrowers such as store clerks, mechanics, librarians, bus drivers, and social workers, who, for a variety of reasons, do not qualify for prime financing. The higher premiums that FHA will charge some types of borrowers are still substantially lower than they would pay for sub-prime financing.

Another change proposed in the FHA Modernization Act is to increase our loan limits. The loan limits in the high-cost areas would rise from 87 to 100 percent of the GSE conforming loan limit, and in lower cost areas, from 48 to 65 percent of the conforming loan limit. This change is extremely important, and crucial in today's housing market. Because of rising costs, FHA insured only 5,000 loans in the entire State of California last year, compared to 127,000 in 1999.

We are also proposing some changes to specific FHA products, insuring mortgages on condominiums under its standard single-family product, modernizing the Title I manufactured housing program, and expanding the home equity conversion mortgage program, also known as reverse mortgages.

Let me assure you that the changes we are proposing will not increase the overall risk of the MMI fund, or impose a potential cost on taxpayers. We are proposing to continue managing the fund in a financially prudent manner, beginning with a change in FHA pricing to match premiums with risk.

I know I have talked a lot here today, but I want to convey to you just how passionate I am about the proposed changes. When people ask me, "Why are we proposing these changes," I tell them these exact words: families need a safe deal at a fair price. Families need a way to take part in the American dream without putting themselves at risk. Families need FHA.

I want to thank you again for providing me the opportunity to testify here today on this Act, and I look forward to working with all of you to make these reforms a reality. Thank you.

[The prepared statement of Mr. Montgomery can be found on page 74 of the appendix.]

Mr. MILLER OF CALIFORNIA. Thank you. Would HUD support affordable housing goals for FHA programs similar to Fannie Mae and Freddie Mac?

Mr. MONTGOMERY. Well, certainly, Mr. Chairman, all of our housing products serve families of lower to moderate incomes. If you're asking would we put similar targets on FHA? I'm sorry?

Mr. MILLER OF CALIFORNIA. Yes.

Mr. MONTGOMERY. Okay.

Mr. MILLER OF CALIFORNIA. Yes, similar targets.

Mr. MONTGOMERY. That's—

Mr. MILLER OF CALIFORNIA. California and high cost areas—I know in Barney Frank's area and in mine—FHA doesn't exist. In Maxine Waters area, which is pretty much contiguous with mine, it doesn't exist because the limits are so low, that we just—nobody can buy a house that cheap in the marketplace. So FHA is completely driven out of the marketplace.

We just reformed in last year's bill—if it ever gets out of the Senate—on GSE's, where they can go into high-cost areas like ours, and they can compete up to medium, 150 percent above their normal loan limit, but not to exceed medium. I mean, we need something like that for FHA and high-cost areas, because it just isn't there.

Mr. MONTGOMERY. And certainly, Mr. Chairman, that's what the bill proposes. And probably a really striking example is you look at Ranking Member Waters's district. In the year 2000, we made 2,200 loans in her district. Last year we did 34. We are not a product in the Nation's most populous State.

Alternatively, because of housing prices, we are an extremely viable product in the Nation's second largest State, in Texas. But right now, unless you live in the Midwest, certain parts of the lower East Coast, and in the South, we just can't serve lower to moderate income home buyers.

Mr. MILLER OF CALIFORNIA. Yes.

Mr. MONTGOMERY. And we just think it's time to reform the conforming loan limits.

Mr. MILLER OF CALIFORNIA. There are some who have tried to make the argument that what we're trying to do will hinder the

ability of the conventional marketplace to work with minimal competition from FHA. I disagree with that. What's your opinion?

Mr. MONTGOMERY. Well, again, we are a mortgage insurance product. We don't loan money.

Mr. MILLER OF CALIFORNIA. No, you don't, but you guarantee, which enables people to be able to get into a low-cost loan.

Mr. MONTGOMERY. Absolutely. We have a 100 percent iron-clad guarantee. Some people have said that we're trying to compete more with the conventional market. Our Congressional mandate from the 1930's is not obsolete. We think it's more important today than it was even back then. We just think the product is a little obsolete and needs to be modernized.

Mr. MILLER OF CALIFORNIA. Well, the jumbo marketplace, or conventional marketplace, has grown tremendously, because they're picking up a sector that you're not in, GSE's were not in.

And what practical impact do you think that the loan limit increase will have on home buyers in high-cost areas to be able to purchase an entry-level home? Do you see a tremendous benefit by your changing your way of doing business?

Mr. MONTGOMERY. Yes, Mr. Chairman. I will give you a good example. And I will use California and even Massachusetts again. If you can't—by the way, if you can qualify for prime financing, God bless you, that's a great thing. And we want everyone to do that. But if you can't do that right now, if you're in a high-cost State, and if you—if you're a lower income home buyer with a few blemishes on your credit, your only option is sub-prime lending.

Mr. MILLER OF CALIFORNIA. Yes.

Mr. MONTGOMERY. Which, inherently, is not a bad product.

Mr. MILLER OF CALIFORNIA. More expensive—

Mr. MONTGOMERY. The way that it was used is bad. So that leaves what is a very safe product, which has one of the best loss mitigation programs around, out of the playing field in the Nation's most populous State.

Now, if you look at Marin County in the Bay Area last year, we did a total of six loans. Five of those were reverse mortgages. You go to Webb County, Texas, which most people have never heard of, unless you're from Texas. We did over 1,500 loans.

That, to me, says we need to do something. And it doesn't matter whether I'm visiting with a Democrat Member or a Republican Member. If you're in a high-cost State, they all tell me, "Do something about the loan limits," and that's what this bill proposes.

Mr. MILLER OF CALIFORNIA. And there is a perception out there that somehow the Federal Government is subsidizing individuals with these loans. Would you please address that? Because this turns revenue into the general fund.

Mr. MONTGOMERY. Well, and there are no taxpayer funds used in that. In fact, other than working capital fund monies and salary and expenses money, FHA doesn't receive any appropriation. We're a self-supporting entity. It's supported by the people who pay the insurance premiums, and that's the way it's been for 72 years.

Mr. MILLER OF CALIFORNIA. What's the current health of the FHA mutual mortgage insurance fund?

Mr. MONTGOMERY. Well, Congress has a mandated 2 percent capital reserve. Right now it's a little over 6 percent. So we are finan-

cially sound. We have had clean audits the last 12 years, and the fund is financially sound.

Mr. MILLER OF CALIFORNIA. How do you ensure proper underwriting?

Mr. MONTGOMERY. Well, we have some of the best underwriting standards around. And bear in mind, since we are an insurance premium, we guarantee the product. It allows families to have a more affordable interest rate. And it's a very transparent product, unlike what you see in some predatory lending. And we think it's a darn good product. It's just time to modernize.

Mr. MILLER OF CALIFORNIA. So you can justify what we're attempting to do here?

Mr. MONTGOMERY. Yes, sir, absolutely. We feel very passionate about this, and believe it's good public policy, and long overdue.

Mr. MILLER OF CALIFORNIA. Thank you, sir. Mr. Frank, you are recognized for 5 minutes.

Mr. FRANK. Thank you. Mr. Secretary, I really appreciate your elaboration on the high-cost situation, because we have people, I think, quite ignorantly—maybe out of good faith, but ignorantly—criticizing the increase in the loan limits, and saying, "Well, you're moving away from the segment you're supposed to serve."

And I think you made it very clear that if we don't increase the loan limits in much of the country, you cannot serve that segment, that we are talking not about getting to a higher-end in the income spectrum, but reaching precisely the part of the spectrum that FHA is supposed to reach in places where it is now priced out of the market.

I was particularly struck by your comments about our colleague from California, Ms. Water's, district, the fact that FHA has virtually disappeared. So that when we talk about raising the limits, we're still not going to hit Santa Monica. You're still not going to hit, you know, much of the Bay Area.

We are not talking about reaching the high-end areas in California or in Massachusetts. There are parts of my district, the City of Newton, where I live myself, where I don't think the limit is going to come close, even at the higher level, to them. But there are other parts of my State, and of California, where it will. So I really appreciate that, and I hope we will hold firm on this.

And there are some competitors who don't like the idea. But again, we want to be clear that we are not changing the mission of FHA.

And is it also the case, by every projection we have, that if you are able to do that, if you are able to go with a higher loan limit based on the house price, that this will increase the negative subsidy, i.e., make money for us?

Mr. MONTGOMERY. Well, as you know, Ranking Member Frank, we're required to operate in a negative subsidy environment. And we think by, again, spreading the risk out, we can continue to operate in this environment. And we just think that it's time to price the product, which we think is a good product, commensurate with the risk, and that's what this bill does.

Mr. FRANK. I appreciate that. The other thing I would say is this. You know, some of what we favor is, I think, going to increase the return to the Treasury, just by increasing the amount of volume.

But we have a fund that is now in an actuarially sound position. Is that correct?

Mr. MONTGOMERY. Yes. Yes, sir, it is.

Mr. FRANK. All right. And it is returning over and above what's needed to be actuarially sound, some surplus to the Treasury?

Mr. MONTGOMERY. That is correct.

Mr. FRANK. Okay. Well, in that case, that's why I think the gentleman from California and I are somewhat skeptical that you need all of the increases that are in this bill.

I mean, when we have got an actuarially sound fund, and it's already making money, an additional $845 million seems to me to be more than we need on this program. And that's why, in particular, I will be working to try and—I don't want to take away the flexibility for pricing.

We don't want to have a situation where things could go bad and we would be in some trouble. But particularly at the low end, I want to stress again that I think this is a very good forum now in which we, the Federal Government, can help low-income people.

And again, we are agreeing that when you extend the loans downward, you are going to hit people who are higher risk, not because of any moral deficiency on their part, just because they have less money, they have less margin, etc. And then the question becomes, for public policy, who should subsidize them?

And again, I think that's the way to focus it. And I think the answer should be we that do not expect the majority of lower income people who would be reached here to have to bear a lot of the burden of the subsidy for the minority who aren't going to pay up. Let's find another way to do that. We have budgetary flexibility here, because we're in the FHA structure. And I am pretty sure there is no requirement that any particular class of loans has to bottom out, has to be in overall balance. So I would look very closely at that.

And yes, it would be nice if you made a little bit more money. Frankly, some of us believe that the surplus that is generated, while in budget terms it's not a free gift to use it for housing, it justifies housing.

That is, when you look at the housing budget of America, as you look at the amount we expend from the Treasury and HUD, we ought to keep in mind that we are making some money as an offset to that in the housing area from FHA. And while it doesn't make it a free gift of money in the pay-go sense, it does, I think—it should have some public policy goals.

So, I again want to thank the Administration. This is a very good bill, and I hope we can move forward on it with the one change that I discussed. And as I said, I particularly appreciate—and we will be talking more about—your helping us justify the high-end.

I guess the best way to put it—to go back to the high-end thing—if you believe that there ought to be economic guidelines for where the FHA can lend, then you ought to believe that we adjust those for region. The notion that you would set a limit based on the cost of housing, and ignore the very wide variations in the cost of housing, just doesn't make any sense economically. Thank you, Mr. Chairman.

Mr. MILLER OF CALIFORNIA. Thank you. Mr. Frank, when this program changes, there are areas of San Francisco, like the Bayview Area Redevelopment Sector, that are going to tremendously benefit from this program. Ms. Lee, you are recognized for 5 minutes.

Ms. LEE. Thank you very much. Good to see you. And let me just ask you, going to the Bay Area, of course my area is Oakland, the East Bay, across from San Francisco. And right now, the median price of an existing single-family detached home, just in California in general, is about $551,000. That's a 13 percent increase.

And of course, the median price of homes in my county, in Alameda County, during January of 2006 was $570,000. Now, that's $570,000 for a small house. The FHA loan limit, I believe, in my district for a one unit house is about $362,000. So, I think we all agree that these loan limits need to be raised.

But I'm not sure, with that big of a gap between the median price and even the loan limit being raised, what in the world are we going to do to ensure that people who deserve to purchase and participate with FHA will be eligible?

I also wanted to know just—I believe in this legislation you presented—and this is the second question—that there is no provision for fair housing and non-discrimination reforms in the FHA program. And I'm wondering what you're doing to ensure that all lenders are in compliance with fair housing laws, and if you have a breakdown of the demographics of FHA homeowners, specifically African American, Latino, and Asian Pacific American homeowners, under the FHA program.

Mr. MONTGOMERY. Thank you very much for your question. And I will answer the last part first.

We work very closely with Assistant Secretary Kim Kendrick in fair housing issues, and I think FHA is a leader in that area, and especially as we're celebrating Fair Housing Month in the month of April.

Relative to the conforming loan limit cost, we—

Ms. LEE. Let me just ask you though, Mr. Secretary, in this legislation, in the legislation that's being proposed, shouldn't there be some provision reaffirming that?

Mr. MONTGOMERY. We will make sure it is. The intent—and I will go back and look a the legislation—is not to supplant what is in there now, but we will certainly—and I give you my word—to make sure that is in there.

Ms. LEE. Great. And we will work with you on that also.

Mr. MONTGOMERY. Thank you.

Ms. LEE. Thank you. Okay, continue.

Mr. MONTGOMERY. But relative to the conforming loan limits, I am often struck by the fact that in the Nation's most populous State, the median home price is north of $550,000. In the second most populous State, Texas, it's only about $175,000.

Now, there are plenty of homes—right now we can't exceed $362,000—but by going to 100 percent, we can go to $417,000. And while we may not be able to get parts of the Bay Area, there are certainly other parts of California and other high-cost States. There are a lot of homes being built between $362,000 and $417,000, which is a 100 percent limit.

It's difficult for us, speaking for FHA, to address beyond that. But we certainly recognize that it's a concern in many parts of the country.

Ms. LEE. But let me ask you. It is a concern. And you just laid out what the issue is, and what the problem is, and what we're going to see, of course, is de facto segregation.

You're going to see areas such as the Bay Area become upper middle income white areas. You're going to see people moving, which we're seeing now, out of places such as Oakland and San Francisco, primarily minority potential homeowners, minority constituencies and populations leaving. And we're going to have a major crisis on our hands, in terms of the further segregation of America, based on, now, the fact that people cannot qualify because we know, historically, income levels are lower in communities of color, and they can't afford these houses.

And so, it's a vicious cycle. And how do we break that cycle, is what I'm asking you.

Mr. MONTGOMERY. Well, speaking for FHA, it's difficult for us to address people who—where home prices exceed what we are required by law to stick to.

And I certainly agree with your premise, that there is a concern about construction of affordable housing in many parts of the country. And I would say that's most pronounced, unfortunately, and probably, in your district, that what sort of incentive is there for people to build homes of more moderate cost, versus higher-cost homes.

There are certainly regulatory barriers, local codes that certainly drive up the cost. Real estate values just continue to increase in many cases out of sight, to be very blunt.

But we think, relative to low- to moderate-income home buyers, by making this step at least to 100 percent, that we can at least serve more families who are not being served right now, or at least serve them with a much safer product.

Mr. MILLER OF CALIFORNIA. The gentlelady's time is up. One of the largest originators of loans we have out there is the mortgage brokers. Yet, in many cases, they are not allowed to offer FHA type of loans. Are you addressing that in any way?

Mr. MONTGOMERY. We have been working very closely with the mortgage brokers and other groups.

In fact, my first day on the job, when we realized we needed to fix FHA, we sat down and met with every group, from low-income housing advocates to realtors, home builders, brokers, and bankers.

And I know some of them have concerns about the audit requirements, and we are in communication with them to see if we can resolve that, because they are originating between 60 and 67 percent of all loans right now, and I don't like using this term, but they are, in effect, our sales force.

Mr. MILLER OF CALIFORNIA. Yes, they are.

Mr. MONTGOMERY. And—

Mr. MILLER OF CALIFORNIA. We had a hearing last year when the bankers came forth and testified that they are one of their major resources in processing loans, and yet they are not really able to work in the FHA arena.

Mr. MONTGOMERY. Well, there were some rather onerous process requirements, Mr. Chairman, that from day one we immediately began to modernize. And those were roundly applauded by the mortgage brokers and by the mortgage bankers, just streamlining our procedures.

Also, we had some fairly onerous appraisal requirements. And we were even, as you know, one of the last entities requiring thick case binders full of home documents to be mailed back and forth between our home ownership centers and brokers and lenders.

Mr. MILLER OF CALIFORNIA. Yes.

Mr. MONTGOMERY. And if there was one little error, we had to FedEx it back, and it got very expensive. We are now requiring them to do that—or saying that they can do it electronically.

So, a lot of those have been applauded by the industry, including the mortgage brokers.

Mr. MILLER OF CALIFORNIA. Well, in the vein of what Ms. Lee was talking about, about low-income families having an opportunity to go and buy a home in the marketplace, many—in many cases, mortgage brokers have more time and the ability to represent a low-income family, representing them in a lending environment. And I think that that would go a long way toward addressing these concerns.

Mr. MONTGOMERY. Yes, sir.

Mr. MILLER OF CALIFORNIA. Ms. Velazquez, you are recognized for 5 minutes.

Ms. VELAZQUEZ. Thank you, Mr. Chairman. Commissioner Montgomery, this committee approved zero downpayment legislation last year that included mandatory counseling. Although this legislation has not passed Congress, does HUD plan to take the advice of this committee and require housing counseling for loans that require no downpayment?

Mr. MONTGOMERY. Well, we certainly think home buying counseling is a very good concept, and a very good program. As you know, this Administration has increased home buying counseling funds exponentially over the last 5 years.

Now, as you know, this legislation—I haven't used the term zero down, because zero down would now become one of several options that we could offer low- to moderate-income home buyers. And again, if we could price it commensurate with the risk, look at the borrower's portfolio, they may qualify for zero down, and maybe a half percent down, and maybe 1-, 2-, or 3 percent.

So, we're not zeroing in on just zero down, because there may be, again, a whole range of products that family—and some families may not want to put down more money. They may want to save it to furnish the home, or something of that manner. The key thing here is flexibility.

Ms. VELAZQUEZ. But even if you don't want to call it zero down, my question to you is whether you're going to take the advice of this committee and include or require housing counseling for those borrowers, especially if we want to tackle the issue of foreclosure, predatory lending in our communities, low-income communities, we need to educate those consumers.

Under this proposal, would you intend in any way to make sure that borrowers will be connected to that type of housing counseling?

Mr. MONTGOMERY. Well, that is certainly something that we can consider, now that we have moved away just from a zero down. It wasn't our intent to not offer families advice on the home buying process. But certainly it's something we can look at.

And I want to add to that, we also did not have a separate FHA website or a call center, which we now have. And we think, to the degree that we can't sit down and do one-on-one counseling, it is about time that FHA had the ability for people to access information on the Internet, or pick up the phone and—

Ms. VELAZQUEZ. But in low-income communities, people might not have access to technology.

Mr. MONTGOMERY. And that's a very good point. We have, I should add, begun a marketing campaign designed specifically at Latino and African American communities in 60 communities across the country, and we are starting the effort, Representative. And we hope with this legislation, to do even more.

Ms. VELAZQUEZ. Okay. The FHA is generally targeted for minority, low-income, and first-time home buyers. These borrowers will likely be charged higher premiums under a differential mortgage premium system.

Can you explain how changing to this system, and imposing higher rates, will not push some borrowers out of the program, and you will be then defeating the purpose?

Mr. MONTGOMERY. I think it's important to put into context the amount between the varying percentages of the mortgage insurance premiums.

I will use an example, a $100,000 home, which while not readily available up here, it is in other parts of the country. The payments on that home would be about $674 a month for a family that pays a 1.5 percent FHA mortgage insurance premium and a .5 percent monthly premium. If we charge that family the maximum of 3 percent, again with the .5 percent annual premium, the payment only goes up $19 a month.

Now, compare that to what that family would pay with a standard 9.5% sub-prime loan. The payment is $160 more a month. So, even by going up—again, we have to keep a capital reserve that Congress mandates—even going to the extreme example of 3 percent, which is the cap we have been working with—it's still a far, far better product, a safer product with no pre-payment penalties, than that family would get versus the sub-prime product.

Ms. VELAZQUEZ. I understand that. But for some, and too many families in this country, $20 is a lot. It will make the difference between purchasing a prescription drug or putting food on their table. So that's my point. Thank you.

Mr. MILLER OF CALIFORNIA. Thank you. FHA proposals contain many options, but condominiums seem to be one that is, often times, overlooked. And one of the types of housing especially attractive to first-time home buyers, is the condominium. Can you please explain how the proposal would make it easier for buyers to use FHA to buy a condo?

Mr. MONTGOMERY. Well, condominiums have been in the FHA on the multi-family program side for a number of years. And we think it's time to move them into the single-family side, and to put all the single-family programs, including condominiums, under the MMI fund.

Mr. MILLER OF CALIFORNIA. So they will all be single-family, attached and detached, under one category, then?

Mr. MONTGOMERY. That's correct. It will all go under single family, including condominiums, and be operated under the MMI fund, instead of the—

Mr. MILLER OF CALIFORNIA. So the loan, then, would be pretty much pushed by FHA as you would single-family detached?

Mr. MONTGOMERY. That's correct. And as many condominiums now are springing up in areas closer to city centers, they become more viable options for a lot of families. And again, we just think it's time to modernize it, and make condominiums a part of the single family product side.

Mr. MILLER OF CALIFORNIA. Great, thank you. Mr. Scott, you are recognized for 5 minutes.

Mr. SCOTT. Thank you, Mr. Chairman. Mr. Montgomery, the FHA is a product of the Franklin Delano Roosevelt Administration. It was birthed during the Depression to serve those needs that were not met by the private sector, correct? And recently, the FHA loans have started to decline. Is that—when did that decline start?

Mr. MONTGOMERY. Well, FHA volume has always ebbed and flowed, depending on factors, certainly to include economic factors. But the percentage of our market share has been steadily declining for about the last 6 years.

Mr. SCOTT. Was there any given—up to the last 6 years, it's been going on since 1934. So from 1934 to about 2000, we're moving along pretty good, up and down, ebbing and flowing, but pretty good. What happened 6 years ago? Was there some economic activity, some event that happened that started this downward slip?

Mr. MONTGOMERY. Sir, I would say a lot of our traditional borrowers that would have gone with FHA, if you look at the data and statistics, they moved toward sub-prime loans.

And I can't speak for the past, but I can say you've got a perfect storm, sadly, of an outdated FHA product, and not a lot of consumer awareness of the product. You had onerous requirements. You had outdated technology that we were using. And a lot of realtors and lenders didn't want to use FHA. We were cumbersome and unwieldy, and we're working to change that. I didn't blame them for not wanting to use the product. We didn't make it easy on them.

And between other products marketing themselves well, that we weren't able to do, a lot of families made decisions, they wanted to buy a home—God bless them for doing that—but our concern is that some of those families made poor decisions.

Mr. SCOTT. And you believe passage of this legislation you're proposing and supporting would help put us back on the right track, moving upward?

Mr. MONTGOMERY. Absolutely, sir.

Mr. SCOTT. Would moving FHA to a risk-based pricing formula make it closer in nature to the sub-prime market?

Mr. MONTGOMERY. Sir, just about the entire mortgage industry, and other forms of insurance—which is what we are—price based on risk.

One thing I think it's important to note is that, yes, for some, the premiums will go up. But for a lot, they will go down. And we will look at the totality of a borrower's profile: their income; their debt; their FICO score. You have a lot of immigrant families who don't have a lot of credit, but perhaps have a lot for a downpayment. Now we can price a product to their risk, and it may be, based on their downpayment, they pay very little insurance premium.

Right now, it's a one-size-fits-all that drives away many borrowers. And we think it's just time to modernize it, and bring it into this century.

Mr. SCOTT. Do you and your Administration support the Tiberi-Scott bill for zero downpayment? It is that downpayment that is the most cumbersome, difficult stumbling block to home ownership. And Congressman Tiberi and I have been working on this bill, and it has got some good movement. Do you all support this bill?

Mr. MONTGOMERY. We absolutely support the concept of zero down. And this legislation, though, goes a little step further, in that, again, pricing it to a family's risk or profile, it may be that they can qualify for a half percent. And as I mentioned previously, maybe a family who could go zero down decides, "Well, we would rather keep some of the money to furnish the home, or buy a refrigerator," or whatever. And again, we can have that flexibility that we don't have today.

So, we certainly support that concept, Congressman. But I also think that by implementing this bill, we can have a whole range of downpayment scenarios, again, to match a family's profile

Mr. SCOTT. Okay. Let me just, for—go back for a minute on the condominiums, because that is a big issue. Can you give us a little bit more information on the demographics served by the condominium market?

Mr. MONTGOMERY. Well, sir, I can get you more specific information after this as to the demographics. But we think it's time to modernize, since condominiums are increasing dramatically as an option for families, especially those who want to continue to live near city centers. We just think it's time to modernize, to be able to offer a more affordable product to many families who choose to live in condominiums. But we can get you the demographic—

Mr. MILLER OF CALIFORNIA. The gentleman's time is expired. Thank you.

H.R. 4804, sir, a bill introduced to modernize FHA Title I manufactured housing program, was recently referred to this committee. The Administration's proposal also contained a number of Title I reforms, with the goal of making the purchase of a manufactured home more affordable and increasing Ginnie Mae's participation in Title I programs. What Title I reform does the proposal address?

Mr. MONTGOMERY. Well, for one, we think moving away from the 10 percent portfolio—right now, a lot of—we can't pay claims that exceed the 10 percent of a lender's portfolio. We think it's time to move away from that, to make it more mirror Title II.

We think by raising the prices—right now, for a manufactured home, you are limited to $48,000. The median price for a manufactured home today is a little more than $58,000. So we would propose to raise the conforming loan limits for manufactured homes on a lot, or separate, or even for property improvements. And we just think it's time to modernize Title I, as well.

Mr. MILLER OF CALIFORNIA. And you don't think this creates a greater risk for FHA?

Mr. MONTGOMERY. No, sir. We don't. As a matter of fact, we think that the more it could mirror Title II, the less risky it would be.

Mr. MILLER OF CALIFORNIA. Okay.

Mr. MONTGOMERY. I mean, volume right now we're doing on Title I, because interest rates are so high, that there is no definite guarantee that we're going to pay the claim, and—

Mr. MILLER OF CALIFORNIA. I agree. I just wanted to hear you say it, that's all.

Mr. MONTGOMERY. We're doing less than 2,000 loans now. The volume has all but disappeared.

Mr. MILLER OF CALIFORNIA. Yes.

Mr. MONTGOMERY. And 22 million Americans live in manufactured homes. That's 8 percent of our population. We think we need to make it a more affordable product, especially for families who live in rural communities.

Mr. MILLER OF CALIFORNIA. I agree. Mr. Cleaver, you're recognized for 5 minutes.

Mr. CLEAVER. Thank you, Mr. Chairman. Mr. Montgomery, first, if you could, tell me, please, what the FHA share of the market is, presently.

Mr. MONTGOMERY. It's somewhere between 3.25 and 3.75 percent.

Mr. CLEAVER. Well, are the mortgage folks accurate that FHA once held 40 percent of the market?

Mr. MONTGOMERY. That would probably seem a little high to me. Historically, over the last 20 years, it has fluctuated. But I don't recall, in the last 20 years at least, it's been higher than about 19 percent.

Mr. CLEAVER. So, if this legislation is approved, do you think that FHA would get a larger share of the market?

Mr. MONTGOMERY. I—as a public servant, I hate using the term market share, because it seems like we're a corporation, but it is a good descriptive term.

If we help one more family, sir, with a safer product at a fair price, then we will be satisfied. If that increases the so-called market share, great. But we are doing this to position it as a product, to modernize it, and to make it a more viable option for lower-income families. And we think by doing that, sir, our percentage of the market will more than likely increase.

Mr. CLEAVER. Well, the purpose of the question actually is designed to find out—there are some on this committee and in this Congress who believe that Fannie Mae and Freddie Mac's portfolio has grown too large, that it's too large. I'm not one of them, but there are those who believe that.

And so, I'm wondering whether or not the FHA revitalization would relieve Fannie Mae and Freddie Mac of this—or reduce the size of their portfolio. I mean, if you're going to revitalize and capture a larger share of the market—and I can see that you're trying to stay away from a percentage that you think you might capture of the market—but I'm also interested in whether or not a not-intended consequence of this legislation might be to reduce the portfolios.

Mr. MONTGOMERY. Well, we will certainly not change the housing goals for the GSE's, affordable housing goals, sir. We have a legislative mandate to do those, and those wouldn't change. FHA traditionally serves a lower-income/higher-risk borrower than the GSE's do. And I don't—while there could be some minimal overlaps there, I don't see that being an unintended consequence.

Mr. CLEAVER. Well, yes. I'm not making a judgement on whether it's good or bad, I'm simply wondering if we can reduce the portfolios of the GSE's. I mean, if you're going to—you expect the market to—your market share to rise, right?

Mr. MONTGOMERY. Yes, sir. That's our goal, to serve more borrowers.

Mr. CLEAVER. Okay. So if it rises, do you think that that would reduce the GSE's portfolio?

Mr. MONTGOMERY. More than likely not, sir. But I would say that more families, if you look at the data over the last several years, most of the traditional FHA borrowers—by the way, if some of them went conventional, great; that's what we all want—but looking at the data, most of them were steered toward sub-prime products. And that market, as you know, has exploded, exponentially.

Mr. CLEAVER. Well, what do you—is there—what do you consider to be—I mean, somewhere in your comments you made a statement about some home—oh, okay, I'm sorry. The primary concern with the risk-based pricing approach, or that "FHA will target people who shouldn't be homeowners."

When you say, "shouldn't be homeowners," are you speaking to their income level? To their credit? What are you—who are the people who should not be home buyers?

Mr. MONTGOMERY. Sir, one of the biggest concerns we have are the amount of mortgages that are going to reset later this year and into next year. It's just shy of $2 trillion. And as many arms reset, or other variables occur, we are concerned that some families who got into a loan on day one at "X" number of dollars per month, can now no longer afford the home, once that interest rate resets. And that is something of great concern to us.

And perhaps, if this legislation goes through, we may be able to be an option for many of those families to refinance into an FHA product.

Mr. MILLER OF CALIFORNIA. The gentleman's time has expired.

Mr. CLEAVER. Thank you, Mr. Chairman.

Mr. MILLER OF CALIFORNIA. A good question, Mr. Cleaver. I think part of the problem we have is that the conventional market has grown dramatically, and GSE's have not participated in that growth, because they have been limited on the percentage of loans

they can make, especially like in high-cost areas. They're just not there today.

So, as the market grows, I think GSE participation will also grow at the same percentage it should have in the past. So I don't have that concern.

But on your first page of written testimony, you stated that FHA made significant changes, streamlining and realigning it for procedures. Could you describe those significant changes that have been streamlined in the process, and how it is affecting consumers?

Mr. MONTGOMERY. We are not a retail operation. We rely on realtors and lenders, if you will, to sell and promote FHA. And if we are difficult to deal with, with unique and onerous requirements—for example, if you had a cosmetic problem with a home, might have been a wobbly handrail or a cracked windowpane, we required appraisers to go back and forth, to make sure cosmetic items were taken care of.

Now, certainly, we're not, you know, cutting any corners on something structural in nature, or impacting the safety and health of the occupants. That was one concern: onerous appraisal requirements. We did away with those. We adopted what the conventional market does, and that's accept the Fannie Mae appraisal form.

We also had the unique requirements as sending the case binders back and forth. We came into the late 1990's, so to speak, from a technological standpoint, and said, "Can we be doing this electronically?" mirroring what the Veterans Administration home buying program has been doing since 1999. Very, very successful. We also just are generally trying to make FHA much easier to deal with.

But we all agree to meeting with our industry partners, while they roundly applauded—and all of them did, I might add—our process improvements, they also seconded what we had realized, that it was time to make long-overdue product improvements, as well.

Mr. MILLER OF CALIFORNIA. Thank you for your testimony. Would you like to say anything in conclusion?

Mr. MONTGOMERY. Just thank you very much for the opportunity to testify today.

Mr. MILLER OF CALIFORNIA. Thank you, sir. I would like to welcome our second panel now. We have Stella Adams, who is a board member of the National Community Reinvestment Coalition. Members of the coalition seek to increase the flow of private capital into traditionally underserved communities.

Jerry Howard is executive vice president and chief executive officer of the National Association of Home Builders. Welcome, Jerry. The Association is a Washington, D.C.-based trade association, where the mission is to enhance the climate for housing in the building industry.

Regina Lowrie is the president of Gateway Funding Diversified Mortgage Service, located in Horsham, Pennsylvania. She is testifying today as a board member of the Mortgage Bankers Association.

And A.W. Pickel is president and CEO of Lender One Financial Corporation, located in Lenexa, Kansas. Lender One is a full service mortgage banking operation approved to underwrite conven-

tional and government loans. Mr. Pickel is testifying today on behalf of the National Association of Mortgage Brokers. Welcome. Ms. Adams, we would recognize you first, for 5 minutes.

STATEMENT OF STELLA ADAMS, BOARD MEMBER, NATIONAL COMMUNITY REINVESTMENT COALITION

Ms. ADAMS. Thank you, Mr. Chairman, and Ranking Member Waters. It is an honor to be here today, as the voice for over 600 community organizations from across the country that comprise the National Community Reinvestment Coalition.

Mr. Chairman and other distinguished members of the committee, we applaud your efforts to modernize FHA and update programs that have become antiquated. It is important that these programs remain relevant in today's lending market.

Nonetheless, we are concerned with some of the proposed reforms that will move FHA more towards private sector pricing patterns. The mission of FHA is to serve low- and moderate-income families with affordable home loans. In general, we believe that FHA should be modernized, but these proposals would move FHA away from its original purpose.

NCRC believes that FHA must provide an alternative to sub-prime lending, in order to provide a competitive impetus for pricing to be reduced for borrowers with impaired credit. The proposal to adopt a risk-based pricing mechanism for mortgage insurance would move FHA closer to the risk-based pricing in the sub-prime market.

In other words, FHA pricing would more closely resemble sub-prime pricing. This move would be the opposite of what is needed. We need to retain and expand upon alternatives to sub-prime pricing, in order to maintain competitive pressure on the sub-prime market to lower its pricing.

An example illustrates how the proposed risk-based pricing mechanism would move FHA pricing toward sub-prime pricing. Imagine two borrowers, Josh and Monica. Josh has seriously impaired credit, and is a B-minus sub-prime borrower. Monica has a few nicks on her credit, and is an A-minus sub-prime borrower. Right now, both Josh and Monica get charged roughly the same FHA mortgage insurance premium. Monica cross-subsidizes Josh's premium.

On the other hand, if Josh and Monica were to go to the private sector market, Monica could probably get a near-prime loan, perhaps around 7 percent. Josh's APR would be much higher, possibly 9 to 10 percent. In contrast, the FHA program reduces the pricing disparity between Monica and Josh's prices for loans. While this may not be the greatest deal for consumers like Monica, it protects consumers like Josh from onerous and high-cost loans in the private market.

FHA's program has lost market share to sub-prime lenders in recent years. While a number of sub-prime lenders are responsible, predatory lending is a subset of sub-prime lending.

Moreover, abusive lending is particularly prevalent at the lower ends of the credit scoring spectrum, since the more credit-impaired borrowers are precisely the ones with the fewest alternatives.

Currently, FHA loans are an important source of an affordable loan for traditionally underserved borrowers. NCRC's data analysis shows that a greater percentage of lower income and minority borrowers receive FHA loans than conventional loans. Moreover, the level of sub-prime lending, as a percent of loans, sub-prime loans were 1.4 percent of government-insured loans. In contrast, sub-prime loans were 11.5 percent of conventional home loan purchases.

As illustrated by the data, a move to risk-based premium pricing could seriously undercut the current affordability of FHA loans for traditionally underserved borrowers. We cannot move dramatically away from FHA's vital place in the market, as an affordable alternative.

Significant policy questions are whether a move to risk-based premium pricing is necessary to shore up the competitiveness of FHA lending, or the safety and soundness of FHA lending.

NCRC is not convinced that a move to risk-based pricing is necessary to offer flexible and affordable mortgages. We have had discussions with a number of large lenders offering conventional mortgage loans with very minimal downpayments, without private mortgage insurance, and to borrowers with low credit scores—below 600 FICO.

We ask HUD to more fully explore these types of products, and additional credit counseling that may be needed as a component to some of these products. Enhanced home buyer counseling and careful underwriting appear to be a more promising path than moving toward a sub-prime pricing structure.

By making FHA loans more costly for credit-impaired borrowers, the chances increase that these borrowers will default, making the FHA program less safe and sound.

Mr. MILLER OF CALIFORNIA. The gentlelady's time has expired. Would you like to wrap up?

Ms. ADAMS. We thank Mr. Chairman for holding this hearing of great importance for the ability of minority and low-income borrowers to buy affordable homes. We urge the committee not to move FHA towards a risk-based pricing system, and not to raise maximum loan amounts.

As demonstrated above, NCRC believes it is critically important to preserve FHA as an affordable alternative to the sub-prime market. On the other hand, if FHA remains an affordable alternative, it serves as an important check and balance on the private market, keeping pressure on sub-prime lenders to lower their prices. Thank you, on behalf of NCRC and our members.

[The prepared statement of Ms. Adams can be found on page 47 of the appendix.]

Mr. MILLER OF CALIFORNIA. Thank you. Mr. Howard, you are recognized for 5 minutes.

STATEMENT OF GERALD M. HOWARD, EXECUTIVE VICE PRESIDENT AND CEO, NATIONAL ASSOCIATION OF HOME BUILDERS

Mr. HOWARD. Good morning, Chairman Miller. Good morning, Mr. Cleaver. It's great to be before this subcommittee again. I am

Jerry Howard, the CEO of the National Association of Home Builders.

Over the past 2 decades, the popularity and relevance of the FHA's single family programs has waned, as they have failed to keep pace with the market. This is due partially to statutory and regulatory constraints that have limited the FHA's ability to respond to the needs of the borrowers. The differences between FHA's requirements and those for conventional mortgages are a disincentive to the use of the FHA programs.

Further, the FHA's lack of responsiveness to market needs has created opportunities for predatory lenders. Nevertheless, important strides have been made to revitalize FHA under the leadership of Commissioner Montgomery, and with the support of Secretary Jackson.

The benefits of these efforts are already being seen. The FHA has aligned its appraisal requirements with market practices. Additionally, FHA's new policies increase the allowable loan to value ration for cash-out refinancing transactions. And revisions to the 203(k) rehabilitation program have made this program more user friendly.

Despite these steps, several requirements still seriously constrain FHA's ability to deliver a range of mortgage products needed for FHA to fulfill its mission.

Accordingly, NAHB believes that Congress should grant the FHA the broader authority outlined in the Administration's budget request, and detailed in the draft authorizing legislation. NAHB is pleased that several reform proposals are included in the Administration's position. I will outline them here.

First, the current limit for FHA mortgages is too low to enable deserving potential home buyers to buy homes in many high-cost areas. The artificially low limit restricts choices for home buyers who use FHA-insured mortgage loans. They are pushed to the lowest echelon of available homes throughout much of the country. And in many areas, there are no homes available.

NAHB supports the Administration's proposal to recalibrate local loan limits to 100 percent of the area median, up to the conforming loan limit, and to increase the minimum FHA mortgage amount to a more meaningful level.

Second, one of the most common factors keeping potential home buyers from achieving their dream of home ownership is the lack of financial resources to pay downpayment and closing costs. FHA's current statutory requirement of a cash contribution of 3 percent by a home buyer was considered innovative years ago, when downpayments of 10 percent or more were the norm for conventional loans.

However, recent strides in underwriting make it possible to predict with reasonable certainty, the likelihood that a borrower will or will not default on a loan, rendering the downpayment a far less critical variable in the underwriting process.

NAHB has long supported efforts by this committee to implement the new zero downpayment program, and we support the Administration's request to provide FHA the flexibility to establish a range of downpayment program requirements for its single family pro-

grams, as long as the programs operate on an actuarially sound basis.

Third, NAHB is pleased that the budget request includes an initiative for a risk-based mortgage insurance premium. Such a premium would temper the current structure for better performing loans, or cross-subsidizing weaker loans in the FHA insurance fund, allowing the FHA to support a broader menu of mortgage markets.

Fourth, by extending the maximum loan maturity to 40 years, FHA will enable borrowers' monthly loan payments to be reduced. Unlike current popular interest-only loans, an FHA-insured mortgage loan with a 40-year maturity will ensure that some part of the borrower's monthly payment is used to reduce the outstanding loan balance, and to build up equity in the home.

Finally, in many communities, condominiums represent the most affordable path to home ownership. Unfortunately, FHA's requirements for condominium loans are burdensome, differing significantly from the requirements for mortgage loans that are secured by detached single family housing. The net result is a severe limitation on the availability of FHA-insured mortgages for those attempting to purchase a condo unit.

NAHB is pleased that the Administration has requested to consolidate all of the single-family mortgage insurance programs under one section of the National Housing Act. This would be a major step in reopening FHA-insured financing in this critically important market segment.

Mr. Chairman, we thank you for the opportunity, and we look forward to working with you, and with the ranking member and the other members of the committee in this important issue.

[The prepared statement of Mr. Howard can be found on page 52 of the appendix.]

Mr. MILLER OF CALIFORNIA. Thank you, Mr. Howard. Mr. Fitzpatrick, you are recognized for the purpose of an introduction.

Mr. FITZPATRICK. Mr. Chairman, I am very proud indeed to welcome to the House of Representatives, and this committee, an outstanding Pennsylvanian, Regina Lowrie, who is the chairman of the Mortgage Bankers Association.

Ms. Lowrie is a woman entrepreneur who, in 1994, founded Gateway Financial Diversified Mortgage Services in Horsham, Pennsylvania, which is part of the greater Philadelphia area, with just 8 employees, which she has helped to grow today to a company of over 800 employees with 58 offices, and is greater Philadelphia's largest independent mortgage company. I am very proud to have her testify to the committee today. Thank you, Regina.

Mr. MILLER OF CALIFORNIA. Ms. Lowrie, you are recognized for 5 minutes.

STATEMENT OF REGINA M. LOWRIE, CHAIRWOMAN, MORTGAGE BANKERS ASSOCIATION

Ms. LOWRIE. Thank you, Congressman Fitzpatrick. And good morning, and thank you for holding this hearing, and inviting me to share MBA's views on reforming the FHA.

As Congressman Fitzpatrick said, in 1994, I founded Gateway Funding Mortgage with 7 employees and $1.5 million in capital.

We now have over 800 employees working in more than 58 offices, and originating over $3 billion in loans. I am proud of our work at Gateway, and of my entire industry, in providing home ownership opportunities for American families.

When I started Gateway, FHA programs helped to serve many borrowers who would otherwise not get a loan. Ten years ago, FHA comprised 40 percent of our volume. We worked hard to be a good partner with FHA. And together, FHA and Gateway served tens of thousands of people.

Today, however, this story is very different. While Gateway has grown significantly, our use of the FHA program has dropped precipitously. While Gateway has been able to adapt to changes in the market, FHA has not. While the needs of low- and moderate-income home buyers, of first-time home buyers, and of senior home owners have changed, FHA has not followed its historic path of adapting to meet borrowers' changing needs.

We support FHA, and we believe that it plays a critical role in today's marketplace. Most of FHA's business is directed towards low- and moderate-income and minority borrowers, the very strata that is most challenged to be part of our ownership society.

At the same time, we have watched, with growing concern, as FHA has steadily lost market share over the last decade, potentially threatening its long-term ability to help underserved borrowers. FHA was founded in 1934, and many of the laws, regulations, and traditions that govern its operations have not kept pace with the rapidly changing and dynamic marketplace. As the market continues to innovate around FHA, the great fear is that many aspiring home buyers will either be left behind, or forced into higher cost alternatives.

We believe that Congress should empower FHA to incorporate private sector efficiencies that will allow it to meet today's needs and anticipate tomorrow's. MBA believes that changes should be made in three areas: FHA needs more flexibility to innovate new products, and introduce them; invest in new technology; and manage their human resources.

MBA supports the Administration's proposals to help FHA achieve these goals. MBA supports changes to the FHA downpayment requirements, including the elimination of the complicated downpayment formula, and the rigid cash investment requirements.

The downpayment is one of the primary obstacles for first-time, minority, and low-income home buyers. FHA may be able to serve more borrowers, and do so with lower risk to their funds, if they are able to adjust their premiums, based on the risk of each mortgage insured.

MBA would caution, however, that creating a risk-based premium structure will only be beneficial to borrowers if there is a lowering of current premiums.

Finally, MBA supports all of the proposed changes to the current home equity conversion mortgage program. MBA's surveys show that FHA's HECM product comprises 95 percent of all reverse mortgages, and is thus tremendously important to our senior homeowners.

In conclusion, FHA has an important role to play in the market in expanding affordable home ownership opportunities for the underserved, and addressing the home ownership gap. But the loss of market presence means we are losing FHA's impact. The result is that some families are either turning to more expensive financing, or giving up.

MBA applauds the leadership and commitment of HUD Secretary Jackson and FHA Commissioner Montgomery in calling for FHA reform. And I urge Congress to enact legislation to reform FHA to increase its availability to home buyers, promote consumer choice, and ensure its ability to continue serving American families. Thank you.

[The prepared statement of Ms. Lowrie can be found on page 61 of the appendix.]

Mr. MILLER OF CALIFORNIA. Thank you, Ms. Lowrie. Mr. Pickel, you are recognized for 5 minutes.

STATEMENT OF A.W. PICKEL, III, PAST PRESIDENT, NATIONAL ASSOCIATION OF MORTGAGE BROKERS

Mr. PICKEL. Good morning, Chairman Miller, Ranking Member Waters, members of the subcommittee, and Mr. Cleaver. It's always good to see a fellow Kansas Citian.

My name is A.W. Pickel, III, and I am the past president of the National Association of Mortgage Brokers. Thank you for inviting NAMB to testify today on transforming the Federal Housing Administration for the 21st Century. As the voice of the mortgage brokers, NAMB speaks on behalf of more than 25,000 members in all 50 States and the District of Columbia.

I want to commend this subcommittee for its leadership when addressing the much-needed reforms to the FHA program. America enjoys an all-time record rate of home ownership today, an achievement to which mortgage brokers have directly contributed.

NAMB appreciates the opportunity to address the need to: one, increase FHA loan amounts for high-cost areas; two, develop risk-based pricing for mortgage insurance on FHA loans; and three, reform the FHA program to reduce the barriers to mortgage broker participation.

NAMB supports many of the proposed reforms to the FHA program, but believes the Administration should also first make certain that the FHA loan program is a real choice for prospective borrowers. Regardless of how beneficial a loan product may be, it requires an effective distribution channel to deliver it to the marketplace.

Unfortunately, many prospective borrowers are denied the benefits offered by FHA loans, because mortgage brokers, the most widely used distribution channel in the mortgage industry today, are limited in their ability to offer such products.

Current FHA requirements impose cost-prohibitive, time consuming, and unnecessary annual audit and net worth requirements on mortgage brokers that want to originate FHA loans. These requirements seriously impeded mortgage brokers' ability to bring FHA loans to the marketplace. A stated objective of HUD and FHA is to increase origination of FHA loan products, and expand home

ownership opportunities for first-time, minority, and low- to moderate-income families.

NAMB supports increased access to FHA loans, so the prospective borrowers who have blemished or almost non-existent credit histories, or who can only afford minimal downpayments, have increased choice of affordable loan products, and are not forced by default into a sub-prime loan.

The solution to increasing FHA loan production is simple. Allow more mortgage brokers to offer FHA loan products directly to consumers. This can be accomplished by eliminating the audit and net worth requirements for mortgage brokers. At a minimum, bonding requirements offer a better way to ensure the safety and soundness of the FHA program, rather than requiring originators to submit audited financial statements.

Congress and this Administration have made home ownership a priority in this country. Unfortunately, today, the demand for homes continues to outpace new housing development and sales of existing homes, causing escalation of home prices. In an environment of rising interest rates, many first-time, minority, and low- to moderate-income home buyers need the safer and less expensive financing option that the FHA program can provide.

For this reason, NAMB uniformly and unequivocally supports increasing FHA loan limits in high-cost areas. Congress should also create the ability for FHA loan limits to be adjusted up to 100 percent of the local area median home price in all communities, thereby providing a logical loan limit that will benefit both the housing industry and the consumer. This approach allows the FHA loan limits to respond to changes in home prices, and reflect a true home market economy.

The benefits of the FHA program should belong equally to all taxpayers, especially those residing in high-cost areas that often are most in need of affordable mortgage financing options. NAMB also believes that FHA risk-based premiums are needed in the current mortgage finance system to drive competition and lower cost for borrowers.

Private mortgage insurers have already demonstrated the ability to balance risk with the premiums charged. FHA should be afforded the same opportunity. The proposed reforms simply bring FHA into parity with what has already proven to be a reasonable assumption of risk for the marketplace. With risk-based premiums, FHA will have the ability to enter the sub-prime market safely, and still offer significant savings to prospective borrowers.

Because FHA's share of the market is approaching marginal levels, any risks to the program are likely to be greater under the status quo than with the proposal. Making FHA more competitive will improve the services and products provided by other lenders and insurers in the industry, and help to restore FHA loan product origination to levels of previous years.

NAMB also supports eliminating the downpayment requirement, and granting FHA the flexibility to offer 100 percent financing to aid in the effort to increase home ownership for first-time, minority, and low- to moderate-income families.

Therefore, under the leadership of Mr. Montgomery, I would like to say that FHA has made great strides, most recently with the

adoption of the 95 percent cash-out refinances, and the appraisal changes. We would encourage Congress to seize this opportunity to revitalize the FHA program with this proposal, so that we can increase minority home ownership by 5.5 million by 2010.

Borrowers underneath this will see better loan programs at lower interest rates. We strongly urge the subcommittee to accept this proposal. NAMB appreciates the opportunity to offer our views on transforming the FHA program for the 21st century. We want to thank you for your consideration. We look forward to working with you, and I am happy to answer any questions.

[The prepared statement of Mr. Pickel can be found on page 80 of the appendix.]

Mr. MILLER OF CALIFORNIA. Thanks, Mr. Pickel. Ms. Waters, you are recognized to make an opening statement.

Ms. WATERS. Thank you very much, Mr. Chairman. I would like to thank Mr. Ney, who is not here this morning, for his interest in this subject matter, and for agreeing to hold this hearing on this issue. And I would like to thank you for sitting in for him.

Historically, the Federal Housing Administration and its mortgage insurance programs were available to insure lenders against loss from loan defaults by borrowers. However, this hearing is really long overdue, because of the decline of the use of FHA-insured mortgages making an otherwise valuable source of mortgage insurance unavailable for an important segment of the mortgage market.

Some might even say that the FHA had lost touch with reality, because its programs were no longer reaching their intended targets: low- and moderate-income persons and first-time home buyers. Today we have an opportunity to explore FHA mortgage insurance programs to determine what is best for first-time home buyers and low- and moderate-income persons, as well as the many borrowers who feel that the sub-prime lending market is their only option.

The relationship between affordable housing and the availability of mortgage insurance is an important issue for me. Without the availability of mortgage insurance choices, those pursuing the American dream of wanting a home find it next to impossible to overcome the many obstacles to home ownership. Government-backed mortgage insurance should not be seen as one of those obstacles.

The growth in risk-based mortgage activities has been accompanied by a rise in predatory lending activities, predatory lending activities that inflate the cost of owning a home, and increasingly, erode the equity in the very home that the individual purchases. Predatory mortgages are estimated to cost $9.1 billion each year. The FHA proposal is, in part, an alternative to help buck this trend. It is welcomed.

According to the FHA, between 2003 and 2005, non-prime loans grew from 118 billion to 650 billion in mortgages, while FHA went from insuring 9.2 percent to 4.1 percent of the Nation's mortgages. According to a Mortgage Banker's Association survey, non-prime loans are far riskier, with foreclosure rates twice that of prime loans. And non-prime foreclosures will only grow with pre-payment penalties, balloon mortgages, and rising interest rates.

For minorities, the situation is even more frightening. Non-prime targets minorities with 40 percent of African Americans and 23 percent of Hispanic home buyers paying interest rates that are 3 percent over market rates. Between 2001 and 2003, the shared non-prime mortgages for African Americans almost doubles. And with Hispanic, the rate went up two-and-a-half times.

I am just happy that the FHA has decided to finally address the shortcomings of the current FHA mortgage insurance programs. Some of the problems are being driven by changes in technology, while other problems represent the reluctance of some to take on this issue, because of criticism about FHA entering the predatory lending market.

It would be premature and unfair for any of us to conclude anything about the FHA mortgage insurance proposal until we have heard from the Commissioner and the other witnesses. I understand that they have been here this morning; they have had their say.

Many of you know that I have worked with Mr. Ney and some others, not only to make sure that those of us who live in States like California could raise the loan limits to include more people, but increasingly we have been watching as the mortgage brokers and others come up with more and more products to be able to accommodate the low-income home buyers, and the minority home buyers. Unfortunately, FHA has just sat there, watching this market without being able to impact it in any appreciable way.

Now, I think with this hearing, all of our members can learn a lot more about what is possible with FHA. I am excited about no downpayments; I am excited about a product that can finally reach the market that so desperately needs some attention.

So, with that, Mr. Chairman, I thank you and I yield back the balance of my time.

Mr. MILLER OF CALIFORNIA. Thank you, Ms. Waters. I appreciate the testimony today, Mr. Pickel, Ms. Lowrie, Mr. Howard. You have all expressed support for raising these limits.

But Ms. Adams, I noticed your opposition to that. And how is this increase harmful to low-income and minority families who live in places such as New York, California—where Maxine and I are from—and Washington, D.C.? How does that impact them in a negative fashion?

Ms. ADAMS. Thank you, Mr. Chairman. The concern that we have at NCRC is that while, in those high-priced markets, it certainly would make it affordable, unlike the GSE's affordable housing goals, the FHA does not have an affirmative public obligation, outside of its intended mission, to serve low- and moderate-income persons.

And so, if we expand it to high—to the high-cost markets where it would meet the needs of low- and moderate-income persons, it would also expand their ability to reach out in other markets, in markets like mine, where it's very affordable to go into upper middle-income—

Mr. MILLER OF CALIFORNIA. No, it doesn't do that. It only impacts high-cost areas. And what are the alternatives if these loan limits are not increased in high-cost areas? It deals with it up to a percentage to median. If your median is down to $150,000, it

doesn't increase it there. But you can't buy a $300,000 home in Maxine's district, nor in my district. And we're trying to create more opportunity in the marketplace.

But what you're expressing does the opposite. It eliminates people from having the opportunity to have an FHA loan. So what are the alternatives to these loan increases, in your opinion?

Ms. ADAMS. We believe that there are a number of factors that are playing into those markets that may need to be addressed outside of the FHA. Forty percent of those markets are really investors, and not really first-time home buyers, and their second home markets that are driving up the costs in those areas.

Mr. MILLER OF CALIFORNIA. What do you consider underserved populations, then?

Ms. ADAMS. I clearly consider minority and low-wealth populations to be underserved.

Mr. MILLER OF CALIFORNIA. That would be predominantly San Francisco, Oakland, Los Angeles—

Ms. ADAMS. But I will tell you that housing prices at $300,000 and $400,000, the populations that I consider low-wealth and underserved, won't even be able to afford an FHA loan at $300,000.

Ms. WATERS. Would the gentleman yield?

Mr. MILLER OF CALIFORNIA. Yes, I am just about through, and then I would be happy to yield.

Ms. WATERS. Yes.

Mr. MILLER OF CALIFORNIA. We have to look at areas other than just less expensive areas. FHA needs to be relevant in low- and moderate-income families throughout this country.

Ms. WATERS. I think that's correct, sir.

Mr. MILLER OF CALIFORNIA. And low- and moderate-income families in many areas are having to pay $400,000, $450,000 for a home. And FHA is not there to serve them. And then that puts them in a situation where, like Maxine Waters was concerned about, where are we forcing these people to go to? And in many cases, they are forced to go to lenders that we consider predatory, in some cases.

Sub-prime, I'm not talking about, because I think there is an absolute market for that. But to take FHA and take it out of these marketplaces, puts people in a very difficult situation when we're trying to provide an opportunity for low- and moderate-income home buyers in high-cost areas. Would you like to respond to that?

Ms. ADAMS. I agree with you, sir. I think it's a complex issue. I don't know how people who make $40,000, $50,000, or $60,000 are going to be able to afford a $300,000 loan, even with FHA—

Mr. MILLER OF CALIFORNIA. Different issue. Different issue. Maxine, I yield to you.

Ms. WATERS. Yes. I'm sorry, Mr. Chairman, I have to run over to the Judiciary Committee for an amendment that I have. But I wanted to say to our witness here that I appreciate her concern, and certainly that is a legitimate question to raise.

When you look at our market in California, and you look into what is supposed to be the poorest areas where these homes have just shot up to unimaginable prices, what you find in many cases are two and three families going in together to buy homes. And it works very well.

What happens is if you get, you know, two or three families who are working that can share the space, and then what they do is they build up equity. And when they build up the equity in the home, and then they are able to refinance, often times they can bring down the price of the interest rates, etc.

And in addition to that, with the appreciation and the equity that they have in the home, it gives them even more money, and they buy up even more. So I know it's kind of tricky, but believe me, they need the opportunity to have access, even with these spiraling costs that we have in places like California.

Ms. ADAMS. Ms. Waters?

Ms. WATERS. Yes?

Ms. ADAMS. It is the desire of the National Community Reinvestment Coalition that every American have the opportunity and access to affordable housing, and to home ownership, and to safe and sound products, such as the FHA mortgage, as opposed to the—some of the products that are in the sub-prime market.

Ms. WATERS. Well, I know your mission, and what your goals are. But I also have to tell you that I find that you are getting some of your support from predatory lenders. And if you can work with them, you can work with FHA.

Ms. ADAMS. We strongly—I only had 5 minutes, and I only wanted to highlight the risk-based—

Ms. WATERS. No, but I want to let you know I know a lot.

Ms. ADAMS. Yes, ma'am. But—

Ms. WATERS. And so when you start to tell me about what your mission is, I probably know it as well as anybody.

Ms. ADAMS. Yes, ma'am. We support FHA—

Ms. WATERS. I know where much of your money comes from. So they need the same opportunity that the predatory lenders that you work with have, okay?

Ms. ADAMS. We're trying to reform those predatory lenders—

Ms. WATERS. I know what you're trying to do, but I also know who is at your banquets, and what they do, all right? You're talking to me, now.

Ms. ADAMS. We support FHA. We believe that FHA should be available to as many—and as a real safe alternative to all sub-prime lenders. And if that puts some of our partners in a bad situation, that won't hurt us at all. We absolutely believe that FHA is the right product to meet the needs of low- and moderate-income borrowers, minority borrowers, and is a real alternative.

Mr. MILLER OF CALIFORNIA. I want to reclaim my 2 minutes. Ms. Lowrie, in your testimony you noted that 15 years ago, a number of FHA-insured mortgages had dropped from 13 percent to—of total originations to 3.5 percent. Could you discuss the decrease in FHA originations in high-cost areas?

Ms. LOWRIE. Thank you for the question. And you're right. I mean, back almost a decade ago, FHA's market share was over 13 percent, and today, less than 3.5 percent. But I think a lot of that has to do with the fact that it has not been able to keep pace with the private sector market.

And when we talk about risk-based pricing, that's a component in mortgage lending that the investment community, that Wall

Street—not just sub-prime, but even the prime market—has moved toward risk-based pricing.

There are limitations in technology. As the Commissioner mentioned, the inability to be able to transmit loans electronically—I mean, we are moving towards, probably within the next several years, being able to do an electronic e-note mortgage, electronic signatures. And yet, we couldn't even electronically transmit a file to FHA. So, FHA could use improvements in the area of technology, innovation, and new products.

And just one other point, Congressman. It took almost 7 years to put in place a hybrid ARM, a 5/1 and a 3/1 ARM, that the private market had already introduced in years prior, because it has to go through Congress for approval.

Mr. MILLER OF CALIFORNIA. So they lost market shares because of that.

Ms. LOWRIE. Yes.

Mr. MILLER OF CALIFORNIA. Okay. Mr. Fitzpatrick, 5 minutes.

Mr. FITZPATRICK. Thank you, Mr. Chairman. Ms. Lowrie, in your testimony you talked about the need for improvements in the reverse mortgage program. There is a bill pending in Congress, H.R. 2892, that I introduced, that would remove these statutory limit—the cap of 250,000—mortgages. It has passed the House already, and there is a very similar bill pending in the Senate.

The idea being that when there is a cap on the number of mortgages that can be issued in this country, that it actually has a limitation on the number of mortgage bankers that can actually invest and get into the market. Perhaps that lack of competition then increases the ultimate cost of the mortgage program to senior citizens who really need it, might increase the cost of the fees associated with the mortgage.

I was wondering if you believe whether removing what you refer to as the HECM cap, the home equity conversion mortgage program cap, won't in fact lower the cost of getting one of these mortgages for senior citizens in this country.

Ms. LOWRIE. Well, it's hard to answer how the market would react to that, how it would affect liquidity in that product. But I do think that it has a—it offers a great opportunity to reduce the cost for seniors. And I also think that, in addition to eliminating the cap, opening it up to purchases for seniors under the HECM program is also a great opportunity to offer that product to more seniors. So, yes, I do, Congressman.

Mr. FITZPATRICK. And that actually came up during the course of discussion in this committee about what we could do to help homeowners impacted by Hurricanes Rita and Katrina, who actually don't even have a home at that point in time, might have to build a home, which is almost akin to a purchase.

In the event that the cap was not eliminated, what do you think the threat to seniors would be?

Ms. LOWRIE. Well, I think when you look at the issue between high-cost and low-cost areas, it almost seems unfair that a senior in a low-cost area, who has the same amount of equity in their home, could maximize taking that equity out, whether it's to pay bills or to sustain living for the rest of their life, and someone liv-

ing in a high-cost area couldn't do that because they—their property is over the cap.

So, I think there is an inequity there, and I think we see more and more—we just have to look at the demographics in our country, and look at the increasing aging population, that this program not only is becoming more popular, but I think it's a critical component for a lot of seniors in this country, to be able to sustain their lifestyle.

And as Congresswoman Waters said, you know, there are people who can't get a prescription, or you know, purchase groceries. I mean, I think this is—it's an important issue, and I think we have a fiduciary responsibility to address that and keep equity within the program.

Mr. FITZPATRICK. And so, as the program becomes more widely used, is it your experience that seniors are satisfied? Are they happy with the program?

Ms. LOWRIE. Congressman, not only are they more satisfied, I think the industry has done an excellent job in trying to educate. You know, we talk about financial literacy and consumer education being so critical to low-income minority borrowers, but it's also important for the seniors. And I think it took a number of years for seniors to understand the HECM product, and the industry has done a fabulous job in really getting the message out, and educating them, and having them feel more comfortable with the product.

So, I think that's why we're seeing continued growing interest, and a need for these changes and revitalization of the program.

Mr. FITZPATRICK. Thank you for your testimony here today.

Ms. LOWRIE. Thank you.

Mr. MILLER OF CALIFORNIA. Thank you. Mr. Scott, you're recognized for 5 minutes. Mr. Scott? Mr. Cleaver?

Mr. CLEAVER. Thank you, Mr. Chairman. I almost had a chance to be the acting ranking member, but I guess I have forfeited now. This was going to be the highlight of my career, but—

Mr. MILLER OF CALIFORNIA. So much for your career.

Mr. CLEAVER. Mr. Scott has just ruined it.

[Laughter]

Mr. CLEAVER. Thank you, Mr. Chairman. Mr. Pickel, the FHA Modernization Act, which I think is something that this committee ought to approve, and hopefully the House will approve it, but is—how active are your members in the Gulf region, in the aftermath of the three hurricanes: Katrina, Rita, and Wilma?

Mr. PICKEL. Actually, our members are very active in the aftermath of all that. One of the things our association did was set aside $350,000 to help out people who had been actually hurt by the hurricanes.

The other thing that I guess we're doing at this point—and if we had the opportunity, we could do more—would be getting actively involved in helping people do reconstruction, or put their homes back together. A number of mortgage brokers can't do that, simply because they're not allowed to do FHA products, due to the annual audit.

The audit simply says that they have to have $75,000 in net worth. Most audits cost about $10,000 by a CPA. So, for a one-per-

son, or a two-person, or a three-person mortgage broker shop, it's fairly cost prohibitive, and they just choose not to do it.

So, if mortgage brokers were allowed to do FHA products without the audit, it would greatly increase our ability to help more homeowners, especially in those areas. But we are doing quite a bit. Several people have gone down there, actually, from around the country to help out.

Mr. CLEAVER. Thank you. I wanted to ask Mr. Montgomery this question earlier, and maybe any of you can address it.

But wouldn't this, wouldn't the Gulf Coast region be the perfect laboratory for the revitalization, or the expansion, of FHA? I mean, don't you think that this has created perhaps the best opportunity for FHA since the beginning of its—not decline—but its reduction in providing housing for low-income Americans?

I mean, you look at New Orleans, for example. You know, it seems to me that the door is wide open, and if it isn't, then we perhaps ought to make some adjustments in the bill to open the door for FHA. So if any of you would address that, I would appreciate it.

Ms. LOWRIE. Congressman, yes. First of all, the Mortgage Bankers Association totally agrees with you that, you know, FHA can play a vital role. They have already played a vital role in helping to stabilize that market.

I think the issue—and I had the opportunity to visit down in New Orleans, and visit the various parishes and see the devastation. And this would be one piece of it, revitalizing FHA and having FHA be in the forefront of the market, creating opportunities down there. But there are a lot of other issues.

I mean, all of our members, and private capital, need to be supportive, not because—as we mentioned, and the commissioner mentioned, it is private lenders that fund FHA loans that are insured by the Federal Government. So it's a partnership that, you know—we will continue to work very closely with FHA and the other housing authorities, Habitat for Humanity, to try and bring capital and funding into that area, to revitalize the market.

Mr. CLEAVER. Thank you. But if the—I mean, we are—the Federal Government is guaranteeing the loans, and I mean, you are not suggesting at all—and this is an honest question—that lenders are going to be hesitant?

Ms. LOWRIE. No. And when I said it's a complicated issue, without taking up a lot of time or too much time, remapping the flood maps for that area, and having the ability to insure those loans with flood insurance is one of the issues.

Mr. CLEAVER. Okay.

Ms. LOWRIE. So lenders and servicers are grappling with a lot of issues relating to Hurricane Katrina. And I think that FHA and what HUD has done in that market has been phenomenal. And we will continue to work with them over the coming years.

Mr. CLEAVER. Thank you.

Mr. MILLER OF CALIFORNIA. The gentleman's time is up.

Mr. CLEAVER. Thank you, Mr. Chairman.

Mr. MILLER OF CALIFORNIA. Mr. Howard, your testimony alludes to FHA's sliding market share. And should Congress be concerned about FHA's market share, and could the fact that there is a de-

clining market share point to the private sector meeting those needs?

Mr. HOWARD. Yes, sir. I think that Congress should be concerned about FHA's relevance in the marketplace. FHA is designed to help low- and moderate-income people reach home ownership. When FHA's relevance diminishes, it opens the door for more predatory lending, sub-prime lending that is not of the stature of FHA.

So, I think it's a really important component to get the people who are trying to make the first step on the ladder to home ownership. And so FHA's efforts to revitalize, I think, are crucial in that regard.

Mr. MILLER OF CALIFORNIA. And what's your opinion on the 40-year mortgage product, and whether it provides affordability and increases costs and risks to low- and moderate borrowers?

Mr. HOWARD. I think it's a really innovative idea. I mean, our country was the first country to come up with the 30-year conventional mortgage, and increasing it to 40 years just—at the same time as possibly the risk-based cost factor would potentially increase the payments by a moderate-income home buyer, putting the 40-year mortgage in place will bring them back down, and at the same time, ensure that they are building equity.

We think it's a novel idea, a good idea, and given the changing dynamics in our society, one that would fit right in right now.

Mr. MILLER OF CALIFORNIA. Good. Mr. Neugebauer, you are recognized for 5 minutes.

Mr. NEUGEBAUER. Thank you, Mr. Chairman. Mr. Howard, as you know, I have been in the housing business for a number of years. And one of the things that—when Secretary Jackson was here last week, we talked about the fact that when I first got in the housing business, that FHA had a bigger presence in the housing industry.

And now, at this particular time in the history of our country, we have one of the highest homeowner rates in the history of our country. More people own a home today than at any other time. And particularly minority home ownership is increasing.

And yet, we have been able to accomplish that with a diminished role of FHA in that market. And so I guess the question I have—and maybe to the other panel members—is how relevant is the continuation of FHA, and has the private sector moved in and taken over an area where, in the past, when I first got in this business, that was an area they would not tread?

Mr. HOWARD. I think the market conditions in the past several years have been very conducive to private sector involvement, and I think that's great.

But in your State, in Texas, during the credit crunch, the private sector totally disappeared from the market in many cases. Also, out in California at various times, members of the private sector have closed down their housing offices and walked away. And FHA, along with the GSE's, were the only elements of the housing finance system that remained and kept things going.

So, as a back-stop, FHA is vitally important. Moreover, as a conduit to low- and moderate-income home ownership, FHA remains vitally important, particularly if these proposals are enacted, and

the FHA is streamlined, and is able to get its message out to the consumers.

Mr. NEUGEBAUER. Yes, Ms. Lowrie?

Ms. LOWRIE. Congressman, I would like to just add to what Mr. Howard said, and speak to your point about addressing home ownership to minorities. And you're absolutely correct, our home ownership rate is close to 69 percent in this country, the highest it's been in the history of the United States.

However, for minorities, and for immigrants, and for low-income borrowers, there is a gap. And it's a substantial gap. And the statistics have shown that FHA has consistently been able to serve that underserved borrower.

The statistics today show it. If you look, African-American and Hispanic borrowers constitute over 29 percent of the book of FHA business, whereas in the conventional market, it's only a little over 14 percent. So, there is still a definite need for FHA in the marketplace.

Mr. NEUGEBAUER. Mr. Pickel?

Mr. PICKEL. In regards to your question as to its viability, I guess my comment would be that, yes, there are other products that have developed to meet the need. And one of the things that—and by the way, I am a small mortgage guy, I just run a small shop—we consistently hear is the zero down, or you know, no money to get into the house.

And to keep FHA out of that market only disadvantages the very people who really need it. So, quite frankly, even though there are other products out there, if we can get FHA back in there, I mean, we have an opportunity to do something really good. And this would be great, because they could get a fixed rate with—and the MMI premiums, I looked at what they're proposing, I mean, it's really a good thing, and it would really help FHA. And it would help people.

Mr. NEUGEBAUER. Well, I was sorry I was not able to be here when Mr. Montgomery was speaking earlier, but I did talk to Secretary Jackson last week. And one of the things I think we had talked a little bit about, the fact that some of the people that are originating a good number of loans are kind of shut out of that process because of the audit procedure.

And one of the things that certainly we want to pursue is being able to allow the folks that are really originating a good portion of the loans to be actively, you know, originating the FHA loans.

What—as we look at the minority home ownership and the gap, and trying to close that gap, we have had the no downpayments, and HUD has had some different programs, and some of the States have had different programs through housing finance organizations. Where do you see the most critical piece of—if we reshape FHA, what's the critical piece that we need to be thinking about?

I will start with Ms. Adams, and then we will just kind of go down the panel, and I suspect my time will be just about gone.

Ms. ADAMS. Thank you. I think one of the critical pieces of this is the flexibility to offer the no downpayment option. It is critical that we keep FHA as a flexible but affordable product suitable to low-income and minority borrowers.

FHA has really effectively served minority communities by providing conventional products, providing a safe product for borrowers that—many of whom have been trapped in this—or steered, or somehow end up in the sub-prime market because they are not aware of FHA and its options. And we need to keep it in the—make sure it has the flexibility to serve the communities it was intended to serve, and to reach into there.

Mr. HOWARD. Mr. Neugebauer, I think that the flexibility issue is an overarching issue, but I think it also needs to apply to the price limits on FHA borrowing. In some of America's urban and suburban areas, no matter how flexible FHA is, with the current price limits they're not going to be able to reach down to the moderate and low-income people, be they minority or majority in this country.

And so, in addition to the programmatic flexibility, I think they have to also be able to respond to the markets and the increasing prices in housing.

Ms. LOWRIE. Congressman, I would agree with my fellow panelists here that the flexibility and downpayment is critical. And one of the biggest barriers to home ownership is the downpayment. So, the private market—the private sector—has seen the zero down work very well, and when it's underwritten based on certain credit risk parameters.

But I would go even further to say that when we are looking at revitalizing and FHA reform, we need to be looking at not just this one component, but giving FHA the ability to innovate new products without having to go—I mean, the market is so dynamic, you know, my sales people will say to me, you know, "So and So down the street is offering the My-Community 100 percent mortgage." They want it yesterday. It takes years to get something approved for FHA to be able to offer it within the marketplace. So that's one.

And being able to invest in technology, and manage their human resources, giving FHA the flexibility to operate more in line with the private sector, you know. It does put money in the Treasury, it's never cost the taxpayer one cent. And that money going into the Treasury helps reduce the deficit. I think we need to look at what can be done to put some of it back into FHA.

Mr. MILLER OF CALIFORNIA. The gentleman's time has expired. Mr. Pickel, maybe you can answer the question why the financial audit was put in place that keeps you out of the marketplace with FHA.

Mr. PICKEL. Why it was put in place? I think—I wasn't there when it was put in place, but I think—

Mr. MILLER OF CALIFORNIA. You're a great one to answer it, then.

[Laughter]

Mr. PICKEL. I think it was most likely put in place so that they had some type of idea that this broker, or this individual, had some financial soundness to them, or stability. But quite frankly, $75,000 is not much, in terms of financial stability.

Mr. MILLER OF CALIFORNIA. No, not with the cost of the audit.

Mr. PICKEL. No. And then, you know, really, FHA holds the direct endorsement lender accountable for those loans. What we're

looking to prevent with the broker, quite simply, is just the issue of fraud. The broker doesn't underwrite, the broker originates.

I think, you know, in answer to your question with that audit, you know, eliminate the audit so that FHA can have a brand new sales force on fixed rate mortgages, and we will increase home ownership another—

Mr. MILLER OF CALIFORNIA. I agree with you on that. Well, I look forward to this bill moving forward. I would like to thank Mr. Montgomery, Ms. Adams, Mr. Howard, Ms. Lowrie, and Mr. Pickel, for their testimony. It was very well received.

The Chair notes that some members may have additional questions for the panel, which they may wish to submit in writing. Without objection, the hearing record will remain open for 30 days for members to submit written questions to these witnesses and to place the response in the record.

The hearing is adjourned. Thank you.

[Whereupon, at 11:07 a.m. the subcommittee was adjourned.]

A P P E N D I X

April 5, 2006

Opening Statement

Chairman Michael G. Oxley
Committee on Financial Services

Subcommittee on Housing and Community Opportunity
Transforming the Federal Housing Administration for the 21st Century

Wednesday, April 5, 2006

Good Morning Assistant Secretary Montgomery. Today marks the first time in many years that the Department of Housing and Urban Development and its affiliated agency, the Federal Housing Administration, has provided substantial recommendations for an agency overhaul in the way it assists and provides homeownership opportunity for millions of Americans. I applaud HUD and FHA for engaging in that debate and for providing these recommendations.

As many of you know, FHA was created over 70 years ago to address, at that time, inequities in the mortgage finance system during the depression era. Because of FHA, 30-year fixed mortgages are a standard product in the mortgage finance process.

Additionally, FHA spearheaded underwriting standardization and was, in part, responsible for the creation of the nation's first secondary markets that would securitize FHA mortgage-insured products. FHA has been influential in targeting inner-city and rural areas, commonly referred in the 1980s and 1990s as underserved areas.

However, in more recent times, FHA has been a mortgage insurer of last resort. Potential homeowners who can participate in the private mortgage insurance market do so. I believe this is because FHA has become costly and the paperwork unmanageable. Thus, only the riskiest borrowers now use FHA for mortgage insurance. Moreover, while the prime market relatively remained constant, the non-prime market between 2003 and 2005 grew from $118 billion to $650 billion in mortgages while FHA went from insuring 9.2 percent to 4.1 percent of the nation's mortgages. Some will argue that this is evident that the government is involved where the private sector is not. I believe that it raises questions about the proper role of FHA and its intended mission.

Additionally, we know that at the end of the fourth quarter of 2005, the number of American families who owned their own homes continued to

approach the 70 percent rate, with non-Hispanic White homeownership at 76 percent, Black homeownership at 48 percent and Hispanic homeownership at 50 percent. These are impressive statistics, but I believe that private and public-sector initiatives could do better to close the opportunity gaps that exist in the country. I am very interested in how this proposal will close that homeownership gap.

In addition to FHA Commissioner and Assistant Secretary, we have a variety of witnesses on the second panel that I am very interested in hearing their perspectives on the FHA program and its future course.

I want to thank Subcommittee Chairman Ney and Vice-Chairman Gary Miller for their leadership on this issue.

Opening Statement of the Honorable Bob Ney
Chairman, Subcommittee on Housing and Community Opportunity

Hearing on

"FHA Modernization"

Wednesday, April 5, 2006

This morning the Subcommittee meets to discuss the Administration's recent legislative proposal to reform that Federal Housing Administration (FHA).

The Administration's FY 2007 budget proposes comprehensive reform for the Federal Housing Administration's (FHA) single-family mortgage insurance activities. HUD's legislative proposal introduces an array of products to more fairly price FHA's guarantee to individual borrowers. FHA will base each borrower's mortgage insurance premiums upon the risk that the borrower poses to the FHA Mortgage Insurance Fund.

Under this proposal, the mortgage insurance premiums will consider the borrower's credit history, loan-to-value ratio, debt-to-income ratio, and will be based on FHA's historical experience with similar borrowers. The Administration believes that this change will decrease premiums for many of FHA's traditional borrowers, thereby increasing their access to homeownership.

I applaud Secretary Jackson's goal of enabling FHA to respond more flexibly to changing market conditions and to offer new products specifically designed for hard to reach families. Once the proposal is made available, the Committee will carefully consider its merits.

Since its inception in 1934, FHA has played an innovating role in financing homeownership and affordable housing opportunities for all Americans. Over the past eight years alone, FHA has financed nearly eight million homes and over 754,000 units of affordable rental housing. The mortgage market has changed dramatically in recent years, creating what is today the world's most sophisticated real estate finance system. This system has led to the highest rate of homeownership in U.S. history and to the efficient production of thousands of units of affordable rental housing each year.

However, in more recent times, FHA has been a mortgage insurer of last resort. Potential homeowners who can participate in the private mortgage insurance market do so. I believe this is because FHA has become costly and the paperwork unmanageable. Thus, only the riskiest borrowers now use FHA for mortgage insurance. Moreover, while the prime market relatively remained constant, the non-prime market between 2003 and 2005 grew from $118 billion to $650 billion in mortgages while FHA went from insuring 9.2% to 4.1% of the nation's mortgages. Some will argue that this is evident that the government is involved

where the private sector is not. I believe that it raises questions about the proper role of FHA and its intended mission.

I recognize that FHA continues to face challenges in effectively managing its resources and programs in this quickly changing mortgage market. These challenges have already diminished FHA's market share and its ability to serve families not adequately addressed by the conventional mortgage market. Unanswered, these issues will leave the families served by FHA programs with fewer alternatives for homeownership or affordable rental housing. The Committee appreciates the steps the Administration and FHA have taken to rectify this by streamlining its paperwork requirements and removing impediments to its use by lenders and buyers.

Despite the Administration's efforts, I am concerned that over half of FHA's staff is currently eligible for retirement. Coupled with the loss of qualified staff and persistent hiring restrictions, these factors have inhibited FHA's ability to remove itself from GAO's "high risk" designation. The lack of new employees entering FHA has limited its capacity to renew its leadership role in the housing market and to rejuvenate its workforce with qualified personnel.

I look forward to hearing from the Administration and our witnesses about the role FHA should play in the modern mortgage market and how this new legislative proposal will help create new homeowners.

Opening Statement of the Honorable Gary Miller
Vice Chairman, Subcommittee on Housing and Community Opportunity

Hearing on
"Transforming the Federal Housing Administration for the 21st Century"

April 5, 2006

This morning the Subcommittee on Housing and Community Opportunity meets to consider the Administration's proposal to reform the Federal Housing Administration's (FHA) single-family mortgage insurance activities.

Commissioner Montgomery, I welcome you today and would like to commend you for your work to ensure the FHA program once again becomes a viable option for low and moderate income homebuyers.

Your leadership and vision has already resulted in many regulatory improvements to the program, and I look forward to working with you to make the statutory changes necessary to restore the relevance of FHA in today's marketplace.

I wholeheartedly agree with you that we must reform FHA, so its programs can reach the working families it was created to serve.

When I talk to brokers and lenders in my district, it is clear that the FHA program, as currently structured, has not kept pace.

In the past, first-time, low-income, and moderate-income homebuyers who could not qualify for conventional loans because of high loan-to-value ratios or high payment-to-income ratios could still achieve the dream of homeownership through the FHA program.

Today, FHA is no longer a useful product for prospective homebuyers. Instead, working families such as teachers, police officers, fire fighters, nurses and others are faced with a situation where they are unable to own homes in the communities where they serve.

While FHA was created more than 70 years ago to meet the needs of those underserved by the private sector, today it is not living up to this mission and working families are left without an affordable alternative to financing a home.

The problem is that statutory limitations preclude the FHA from adapting to a rapidly changing marketplace. As the private sector mortgage market has become more efficient, the FHA program's inflexible rules and requirements have left it virtually irrelevant as a financing option.

High Cost Areas

This is especially true in high cost areas of the country, where statutory loan limits eliminate the program as an option for the purchase of an entry-level home.

Under the current limits, FHA products are not available for homebuyers in high cost areas of the country because the maximum mortgage limit is lower than housing prices.

Working families who need and qualify for FHA are effectively kept out of the program because of where they live and work.

I have introduced legislation with Ranking Member Frank, H.R. 176, to provide consumers in high cost areas the ability to purchase a home with FHA mortgage insurance.

I am pleased H.R. 176 is incorporated in the Administration's reform proposal, so that the disparity in accessibility of FHA programs caused by the current loan limit is eliminated.

Arguably, working families in high cost areas of the country are just the kind of underserved population the FHA program was intended to serve.

If we want to ensure FHA is relevant for all those who need it, we must reform the program so that it is available to low and moderate income families across the country, even those in high cost areas.

How to Make FHA a Relevant Option for Homebuyers

The bottom line is, to make the FHA program a viable mortgage option, we must ensure that the program allows for the purchase of entry level homes.

This includes not only eliminating the geographic barriers to utilization of the program in high cost areas, but also facilitating the purchase of entry level homes, including condos and manufactured housing.

These forms of housing are an affordable option for entry-level homeownership and they should be included under this program if we truly want to make it help families climb the 'first rung on the ladder of homeownership.'

In addition to reforming *what* can be purchased under the program, we must also consider the competitiveness of FHA products, as currently structured, among the mortgage options available.

In other words, we must explore the reasons that the program is not being utilized when it is an available mortgage product for a potential homebuyer.

The answer is that the program's inflexibility and burdensome processes have left many in the industry hesitant, or actually unable, to offer FHA products to clients.

- Technological deficiencies. While the rest of the mortgage industry is electronically driven, the FHA program remains the dinosaur, still trying to convert from a paper-based process to an efficient electronic one.

- Lack of Flexibility in Downpayment Amounts. FHA used to be the best option for low and moderate income homebuyers because it had the lowest downpayment requirement. This is no longer the case.

  Although the private market has developed flexible downpayment arrangements to meet the needs of borrowers, the FHA program's downpayment requirements are fixed at three percent in statute.

While other mortgage products have recognized that the ability to accumulate enough cash for down payment assistance is universally considered the greatest single barrier to homeownership, the FHA program does not offer flexibility in downpayment levels.

- Mortgage insurance premiums are not based on the credit-worthiness of individual borrower. While the private mortgage insurers have adopted a risk-based premium structure, FHA does not set its insurance premiums according to the risk of the loan. As a result, lower-risk borrowers pay higher premiums to subsidize the higher-risk borrowers.

- Term of mortgage not flexible enough to allow competition with other products. More Americans could qualify for a mortgage if their monthly payments were lower. To make mortgages more affordable, the FHA should have the flexibility to offer mortgages with longer terms than the traditional 30 years. In this way, borrowers would be able to purchase a home with a mortgage product that is less risky than the interest-only products that have become more popular as housing prices increase.

- While mortgage brokers originate the majority of loans, many are not allowed to offer FHA products. Cost-prohibitive and time consuming financial audit and net worth requirements limit mortgage broker participation in the program. This means that FHA is not made available to some borrowers who would get a better deal under this program than under a subprime loan.

Conclusion

America is home to people of many different origins, but we all share a common dream -- to own a home.

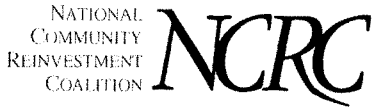
By reforming the FHA program, and making it relevant in today's marketplace, we have the opportunity to ensure that the dream of homeownership can be achieved by more Americans in a way that is most affordable and even less risky.

Commissioner Montgomery, I look forward to hearing from you about how we can remove the impediments to the utilization of FHA so that it can once again help working families across the country have the opportunity to achieve homeownership.

Testimony of Stella Adams,
Board Member, National Community Reinvestment Coalition

Before the House Committee on Financial Services Regarding "Transforming the Federal Housing Administration for the 21st Century"

Wednesday, April 5, 2006



The National Community Reinvestment Coalition (NCRC) is honored to testify before you today. NCRC is the nation's economic justice trade association of 600 community organizations dedicated to increasing access to capital and credit for minority and low- and moderate-income borrowers and communities. The FHA program has been a very important means of extending mortgages to low- and moderate-income and minority families. FHA therefore has been a vital part of the national effort to increase and expand homeownership to these populations.

Mr. Chairman and other distinguished members of the Committee, we applaud your efforts to modernize FHA and update programs that have become antiquated. It is important that these programs remain relevant in today's lending market. Nonetheless we are concerned with some of the proposed reforms that will move FHA more towards private sector pricing patterns. We are also concerned about the proposal that would allow the FHA program to insure homes that are more expensive or consistent with the GSE conforming loan limits. Both of these proposals could have the likely outcome of reducing the numbers of low- and moderate-income and minority borrowers served by FHA. The mission of FHA is to serve low- and moderate-income families with affordable home loans. In general we believe that FHA should be modernized but these proposals would move FHA away from its original purpose.

Risk Based Pricing

NCRC believes that FHA must provide an alternative to subprime lending in order to provide a competitive impetus for pricing to be reduced for borrowers with impaired credit. The proposal to adopt a risk-based pricing mechanism for mortgage insurance would move FHA closer to the risk-based pricing in the subprime market. In other words, FHA pricing would more closely resemble subprime pricing. This move would be the opposite of what is needed. We need to retain and expand upon alternatives to subprime pricing in order to maintain competitive pressure on the subprime market to lower its pricing.

An example illustrates the how the proposed risk based pricing mechanism would move FHA pricing towards subprime pricing. Imagine two borrowers – Josh and Monica. Josh has seriously impaired credit, and is a B minus subprime borrower. Monica has a few nicks on her credit and is an A- minus subprime borrower. Right now, both Josh and Monica get charged roughly the same FHA mortgage insurance premium. Monica cross-subsidizes Josh's premium.

On the other hand if Josh and Monica were to go to the private sector market, Monica could probably get a near-prime loan rate of perhaps around 7 percent. Josh's APR would be much higher, possibly 9 or 10 percent. In contrast, the FHA program reduces the pricing disparity between Monica's and Josh's prices for loans. While this may not be the greatest deal for consumers like Monica, it protects consumers like Josh from onerous and high cost loans in the private market.

FHA's program has lost market share to subprime lenders in recent years. One possible reason for the risk-based premium proposal is to lure A- borrowers like Monica back into the FHA's program. If the risk-based premium approach is adopted, Josh would end up paying substantially more for his FHA loan. The difficulty with this possibility is that borrowers like Josh desperately need affordable alternatives to subprime pricing. While a number of subprime lenders are responsible, predatory lending is a subset of subprime lending. Moreover, abusive lending is particularly prevalent at the lower ends of the credit scoring spectrum since the more credit impaired borrowers are precisely the ones with fewest alternatives.

Currently, FHA loans are an important source of affordable loans for traditionally underserved borrowers. NCRC's data analysis shows that a greater percentage of low-income and minority borrowers receive FHA loans than conventional loans. For instance, African-Americans obtained 16.3 percent of government-insured lending but just 7.9 percent of conventional single family lending during 2004. The percent of government-insured lending to African-Americans was higher than the percent of households that were African-American (11.8 percent) while the percent of conventional lending was considerably below the percentage of households that were African-American. Moreover, the level of subprime lending (or loans with Annual Percentage Rates (APRs) above the triggers for price reporting in HMDA (Home Mortgage Disclosure Act) data) is very low in FHA lending. Lenders issued 746,930 prime government-insured loans and only 10,564 subprime government-insured loans in 2004. As a percent of total loans, subprime loans were 1.4 percent of government insured loans. In contrast, subprime loans were 11.5 percent of conventional home purchase loans in 2004.

As illustrated by the data analysis, a move to risk-based premium pricing could seriously undercut the current affordability of FHA loans for traditionally underserved borrowers. We understand that the proposals involve pricing for mortgage insurance premiums, not APRs reflected in the price reporting in HMDA data. The point about the data analysis, however, is to show the affordable alternative that FHA now provides. We cannot move dramatically away from FHA's vital place in the market as an affordable alternative.

Significant policy questions are whether a move to risk-based premium pricing is necessary to shore up the competitiveness of FHA lending or the safety and soundness of FHA lending. The questions witnesses were invited to answer whether risk-based premium pricing is needed so that the FHA program can offer loans with minimal downpayment requirements and other affordable features. NCRC is not convinced that a move to risk-based pricing is necessary to offer flexible and affordable mortgages. We have had discussions with a number of large lenders offering conventional mortgage loans with very minimal down payments without private mortgage insurance and to borrowers with low credit scores below 600 FICO scores. We ask HUD to more fully explore these types of products and additional credit counseling that may be needed as a complement to some of these products. Enhanced homebuyer counseling and careful underwriting appears to be a more promising path than moving towards a subprime

pricing structure. By making FHA loans more costly for credit impaired borrowers, the chances increase that these borrowers will default, making the FHA program less safe and sound.

FHA Mortgage Limits

NCRC also opposes proposals to increase the maximum dollar amount of mortgages that FHA can insure. Currently the limits are 95 percent of the area's median home price and 87 percent of the Government Sponsored Enterprise (GSE) conforming loan limit. The proposal would change this to 100 percent of area median home price and 100 percent of GSE conforming loan limit. The "floor" would also be increased from 48 percent to 65 percent of the conforming loan limit.

In a number of metropolitan areas, median home prices and GSE conforming loan limits are very high. The proposal, therefore, would allow the FHA program to insure significantly more loans to middle- and upper-middle income families, and decrease their historical focus on low- and moderate-income borrowers. We ask HUD to intensify its efforts to reach minority and low- and moderate-income borrowers rather than Congress adopting a proposal that would further move FHA away from these traditionally underserved populations.

Creative Strategies

NCRC is pleased with aspects of the proposal that will update FHA and make the program more competitive. For instance, we applaud the proposal that would facilitate FHA mortgage lending for condominium units. Condominium units are an important component of affordable housing for low- and moderate-income families in high cost cities on the East and West coasts. In addition, we support proposals to offer FHA loan products with no downpayments, particularly for first time homebuyers. NCRC believes that no downpayment mortgages would be an effective means to compete with the private market, and would probably be more effective than moving to a risk-based pricing structure. Downpayment requirements remain a significant obstacle for first-time homebuyers. These reforms will assist in expanding homeownership to underserved communities.

Conclusion

We thank you, Mr. Chairman, for holding this hearing of great importance for the abilities of minorities and low- and moderate-income borrowers to buy affordable homes. We urge the Committee not to move FHA towards a risk-based pricing system and not to raise maximum loan amounts. As demonstrated above, NCRC believes it is critically important to preserve FHA as an affordable alternative to the subprime market. On the one hand, if FHA remains an affordable alternative, it serves as an important check and balance on the private market, keeping pressure on subprime lenders to lower their prices. On the other hand, if FHA pricing moves towards a subprime pricing structure, private

sector prices for traditionally underserved families would likely increase. Coupled with increasing maximum mortgage amounts, risk-based pricing could slow down, if not stop, the upward trend in homeownership for minorities and low- and moderate-income families.

Testimony of
Jerry Howard

On Behalf of the
National Association of Home Builders

Before the
House Committee on Financial Services
Subcommittee on Housing and Community Opportunity

Hearing on

Transforming the Federal Housing Administration for the 21st Century

April 5, 2006

Introduction

Chairman Ney, Ranking Member Waters, members of the Housing and Community Opportunity Subcommittee, on behalf of the more than 225,000 members of the National Association of Home Builders, thank you for the opportunity to testify today on the important subject of revitalization of the Federal Housing Administration's single family mortgage insurance programs. My name is Jerry Howard and I am the Executive Vice President and Chief Executive Officer of the National Association of Home Builders (NAHB).

The Importance of the Federal Housing Administration

Since its creation in 1934, and for much of its existence, the Federal Housing Administration (FHA) has been viewed as a housing finance innovator by insuring millions of mortgage loans that have made it possible for home buyers to achieve homeownership. Without FHA, many of these buyers either would have had to delay their purchase, been unable to purchase a home, or would have done so at an unnecessarily high cost.

FHA matters for a lot of reasons, not the least of which is that throughout its more than 70- year history, FHA's single family mortgage insurance programs have served home buyers in all parts of the country during all types of economic conditions. Moreover, FHA has done this without any cost to America's taxpayers. NAHB's support for FHA's single- and multifamily mortgage insurance programs has been steadfast through the years.

FHA's Growing Irrelevancy

Over the past two decades, the popularity and relevance of FHA's single family mortgage insurance programs has waned as FHA's programs have failed to keep pace with competing conventional mortgage loan programs. In many respects, this is due to statutory and regulatory constraints that have limited FHA's ability to respond to the needs of borrowers who might have otherwise chosen FHA.

All too often, the differences between FHA's requirements and those for conventional mortgages have been viewed by lenders, appraisers and others as a disincentive to use FHA programs. Likewise, FHA's unique and often burdensome requirements have caused many home builders to avoid using FHA's programs to build homes - including condominiums – that otherwise would have been well-suited to borrowers who planned to use FHA-insured mortgage loans.

Furthermore, FHA's lack of responsiveness to market needs has created opportunities for predatory lenders to charge unreasonably high fees and interest rates to borrowers who, despite limited cash resources and/or tarnished credit, could have qualified for market-rate FHA-insured loans.

The recent decline in FHA mortgage insurance activity, both in real terms and when measured against conventional loans programs, is bothersome in other respects as well. For example, FHA-insured loans serve as collateral for mortgage-backed securities issued by the Government National Mortgage Corporation (Ginnie Mae), which, like the FHA, is part of the U.S. Department of Housing and Urban Development (HUD). Ginnie

Mae serves a vital role in America's housing finance system by providing liquidity for lenders to offer mortgages that are insured or guaranteed by FHA and other government agencies. Because the bulk of Ginnie Mae securities are backed by FHA-insured loans, the declining trend in FHA-insured loan originations, if unabated, could call into question the viability of the Ginnie Mae program.

FHA's Revitalization Bodes Well for Its Future

Important strides have been made to revitalize FHA under the leadership of Assistant Secretary for Housing / FHA Commissioner Brian Montgomery with the support of HUD Secretary Alphonso Jackson. NAHB was gratified to learn that, upon taking office in June 2005, Commissioner Montgomery challenged his staff to identify obstacles that stood in the way of more widespread use of FHA's single family programs. The Commissioner, furthermore, charged his staff with the task of finding ways to overcome those obstacles.

The benefits of Commissioner Montgomery's efforts are already being realized as FHA has aligned its appraisal requirements with market practices by eliminating some bothersome paperwork requirements that needlessly created extra work for lenders, appraisers and home builders simply because a home buyer chose to use an FHA-insured loan to finance the purchase of a home. Other steps that have made the program more user friendly are FHA's new policies that increase the allowable loan-to-value (LTV) ratio for cash-out refinancing transactions and revisions to the 203(k) rehabilitation program.

Congress Should Quickly Act to Empower FHA

Despite these positive moves, FHA's loan limit structure and downpayment requirements, which are established by Congress, seriously constrain FHA's ability to deliver the range of mortgage products that are needed for FHA to fulfill its mission. FHA has proven through the years that it can serve some of the riskiest segments of the borrowing population, and do so in an actuarially sound manner. Accordingly, NAHB believes that Congress should grant FHA the broader authority outlined in the Administration's FY 2007 budget proposal and detailed in draft authorizing legislation. We believe strongly that this proposal will increase FHA's flexibility to mold its mortgage insurance programs in ways that meet the borrowing needs of unserved, underserved and improperly served families and others who desire to purchase a home. These are people who, for a variety of reasons, either cannot get a mortgage loan or who needlessly pay extraordinarily high costs for mortgage credit.

Mortgage Limits

The limit for FHA-insured mortgages is established in statute as 95 percent of the median home price of an area, within the bounds of a national ceiling and floor. FHA's single family loan limit for the 48 contiguous states is currently capped at $362,790, which is 87 percent of the Fannie Mae / Freddie Mac conforming loan limit. This limit is too low to enable deserving potential home buyers to purchase a home in many high-cost

areas. Likewise, the FHA "floor" of $200,160, which is indexed at 48 percent of the conforming loan limit, is too low.

The artificially low FHA loan limits restrict choices for home buyers who use FHA-insured mortgage loans to the lowest echelon of available homes throughout much of the country. In many areas, FHA borrowers are precluded from considering the purchase of a new or recently-constructed home. NAHB does not believe that Congress created the FHA in 1934 with the intent of constraining borrowers to homes priced at the lower end of the market. In fact, NAHB's Board of Directors adopted specific policy in 2005 in support of increasing the FHA loan limit up to the conforming loan limit. NAHB also supports the Administration's proposals to recalibrate local loan limits to 100 percent of the area median from the current 95 percent and to increase the national floor for FHA loan limits.

Downpayments

One of the most common factors preventing potential home buyers from achieving their dream of homeownership is the lack of financial resources to pay the downpayment and closing costs. FHA's current statutory requirement for a cash contribution of 3 percent by a home buyer was innovative when downpayments of 10 percent or more were the norm for conventional loans. Recent strides in credit modeling, such as FHA's TOTAL Mortgage Scorecard, have made it possible to predict with a reasonable certainty the likelihood that a borrower will default on their loan and, therefore, have rendered the downpayment a less critical variable in the underwriting process.

NAHB believes that Congress should grant FHA the flexibility to establish downpayment requirements for its single family programs as long as the programs are operated on an actuarially sound basis. In 2005, NAHB's President David Wilson testified before this subcommittee in support of "The Zero Downpayment Pilot Program Act of 2005" (H.R. 3043), which was subsequently reported out of the subcommittee by a favorable vote. NAHB continues to support H.R. 3043. NAHB also believes it is important for FHA to have the flexibility to establish other reduced-downpayment mortgage options to more fully address market needs.

Mortgage Insurance Premiums

Likewise, NAHB believes FHA should have the authority to set mortgage insurance premiums at whatever levels deemed necessary to maintain actuarial soundness while striving to serve borrowers who have a wide variety of risk profiles. NAHB was pleased that the President's FY 2007 budget request included an initiative for a risk-based mortgage insurance premium. Such a premium pricing structure would temper the current structure where better-performing loans are cross-subsidizing weaker loans in the FHA insurance fund. NAHB looks forward to learning more about this new premium structure.

Loan Maturities

One underlying theme of FHA's revitalization is based upon the need to increase the affordability of the home financing process for prospective home buyers. By extending the maximum loan maturity to 40 years, FHA will enable borrowers' monthly

loan payments to be reduced. Unlike the interest-only loans that are currently popular, an FHA-insured mortgage loan with a 40-year maturity will ensure that some part of the borrower's monthly payment is used to reduce the outstanding loan balance. NAHB believes that 40-year maturities will become commonplace in the not-to-distant future and that FHA should be well-positioned to meet emerging market needs.

Condominium Loans

In many communities, condominiums represent the most affordable path to home ownership. Unfortunately, FHA's requirements for condominium loans are burdensome and differ significantly from the requirements for mortgage loans that are secured by detached single family homes. For a condominium unit to be eligible to be sold to a purchaser who uses an FHA-insured loan, FHA requires the condominium developer to provide documentation related to historical and environmental reviews for the entire project. In contrast, on conventionally-financed condominiums, requirements of this nature are commonly dealt with at the state or local level. Moreover, it is common to have townhomes that are sold as part of a condominium located near townhomes that are part of a planned unit development (PUD). In early 2003, FHA found that its PUD approval process was redundant with local governmental review practices and subsequently dropped its PUD approval requirement. FHA's condominium approval processes are similarly redundant; however, FHA has been forced to retain these because of statutory requirements.

These different requirements exist because condominiums and detached single family homes are authorized under different sections of the National Housing Act and

insurance for these loans is backed by different insurance funds. NAHB has heard from its members who develop condominiums that the burden of the additional and unnecessary requirements, and the delays encountered in attempting to comply with FHA's requirements, have caused these builders to price units that were once intended to serve the FHA market out of the range FHA borrowers could afford. On more than one occasion NAHB has urged HUD to move condominium unit financing under FHA's single family mortgage insurance program. We are very pleased that HUD has agreed to our recommendation and plans to ask Congress to unify all of the single family mortgage insurance programs under one section of the National Housing Act.

Conclusion

In closing, I would like to reiterate NAHB's strong support for FHA and its revitalization under the leadership of Secretary Jackson and Commissioner Montgomery. This leadership team at HUD is working hard at re-establishing FHA's relevance while keeping the program financially sound. With Congress' help, FHA will continue its long record of serving America's home buyers. Thank you once again for this opportunity. Mr. Chairman, I would welcome any questions you may have for me.

STATEMENT

of

Regina M. Lowrie, CMB

on

Transforming the Federal Housing Administration for the 21st Century

before the

Subcommittee on Housing and Community Opportunity

Committee on Financial Services

United States House of Representatives

April 5, 2006

Thank you for holding this hearing and inviting the Mortgage Bankers Association (MBA)[1] to share its views on Transforming the Federal Housing Administration for the 21st Century. My name is Regina Lowrie and I am the President of Gateway Funding Diversified Mortgage Services, LP in Horsham, Pennsylvania and Chairman of the Mortgage Bankers Association. I am here today in support of the single-family proposals offered by FHA to amend the National Housing Act but hope that we can expand the scope of these initiatives to truly allow FHA to meet its mission in the 21st century.

In 1994, I founded Gateway with only seven employees and $1.5 million in startup capital. Over the past 12 years, I have grown the company to over 800 employees working in more than 58 offices, originating $3 billion in loans annually throughout Pennsylvania, Delaware, New Jersey and Maryland. I am proud of the work of Gateway, and of the mortgage industry itself, in providing opportunities for homeownership for families of this great land.

When I started Gateway, the programs of the Federal Housing Administration (FHA) were invaluable in enabling us to serve families who otherwise would have no other affordable alternative for financing their home. Ten years ago, FHA loans comprised 40 percent of Gateway's volume each year. We worked hard to be a good partner with FHA in administering its programs and together FHA and Gateway enabled tens of thousands of families to purchase their first home.

Today, though, the story is very different. While Gateway has grown significantly, our ability to use the FHA program has declined precipitously. Gateway has been able to adapt to changes in the mortgage markets, but FHA has been prevented from doing so. The needs of low- and moderate-income homebuyers, of first-time homebuyers, of minority homebuyers, and of senior homeowners have changed. FHA's programs though, have not followed their historic path of adaptation to meet these borrowers' changing needs.

The numbers are troublesome. In 1990, 13 percent of total originations in the U.S. were FHA-insured mortgages. In 2005, that number has dropped to just 3.5 percent. More importantly, in 1990, 28 percent of new home sales (which are typically a large first-time homebuyer market) were financed with FHA or VA; today that number has dropped to under 12%.

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[1] MBA is the national association representing the real estate finance industry. Headquartered in Washington, DC, the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership 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 3,000 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 website: www.mortgagebankers.org.

The future of FHA is impaired by the perception today of some in the real estate industry. I would like to point out a story that ran in RealtyTimes® on June 21, 2005 in which a Baltimore, MD real estate agent unabashedly advises homebuyers to avoid FHA financing. The agent states: "Approved FHA loan recipients, same notice to you, don't bother bringing it to the table during a sellers market. More times than not, your offer will be rejected. We know that VA and FHA loans allow you the means of purchasing more home for the mortgage, but it only works if you are the only game in town." His advice was based on the often true notion that FHA-insured financing is slower and more laborious than conventional financing.

This is a very unfortunate perspective, especially because FHA is vitally needed today.

MBA is committed to supporting FHA. Nowhere in Washington will you find a stronger supporter of the FHA and the programs it offers. Mortgage lenders are the private delivery system that allows FHA to reach borrowers with affordable financing opportunities, especially low- and moderate-income families, first-time homebuyers, and minorities. MBA members originate about 85% of single-family the FHA-insured mortgages each year. Every day, mortgage lenders sit down with the very families FHA seeks to serve to discuss how we can help them realize their dreams. Maybe we understand better than most that without FHA, many American families simply would not have had and will not have the opportunity to own the home they live in.

The Need for FHA

The FHA program is vital to many homebuyers who desire to own a home but cannot find affordable financing to realize this dream. While the FHA has had a number of roles throughout its history, its most important role today is to give first-time homebuyers the ability to climb onto the first rung of the homeownership ladder and to act as a vehicle for closing the homeownership gap for minorities and low- and moderate-income families.

Despite this country's record high levels of homeownership, not all families share in this dream equally. As of the 4th quarter of 2005, the national homeownership rate stood at a near record 69.0 percent, but only 51.5 percent of minorities owned their own home. Only 48.6 percent of African-Americans and 50.0 percent of Latinos owned their own homes. This compares with 76.0 percent of non-Hispanic white households.

By the end of 2005, 84.3 percent of families earning more than the median income owned their own home, while only 53.1 percent of families below the median income owned their own home.

These discrepancies are tragic because homeownership remains the most important wealth-building tool the average American family has.

FHA's Record

More than any other nationally available program, FHA is increasingly focused on the needs of first-time, minority, and/or low- and moderate-income borrowers.

In 1990, 64 percent of FHA borrowers using FHA to purchase a home were first-time homebuyers. Today that rate has climbed to about 80 percent. In 1992, about one in five FHA-insured purchase loans went to minority homebuyers. That number in recent years has grown to more than one in three. Minorities make up a greater percentage of FHA borrowers than they do in the conventional market.

FHA is particularly important to those minority populations experiencing the largest homeownership gaps. Home Mortgage Disclosure Act (HMDA) data reveal that in 2004, 14.2 percent of FHA borrowers were African-Americans, compared with 5.4 percent of conventional borrowers. Hispanic borrowers made up 15.3 percent of FHA loans, while they only were 8.9 percent of the conventional market. Combined, African-American and Hispanic borrowers constituted 29.5 percent of FHA loans, doubling the conventional market's rate of 14.3 percent. In fact, in 2004, FHA insured nearly as many purchase loans to African-American and Hispanic families than were purchased by Fannie Mae and Freddie Mac combined.

The same data also shows us that over 57.9 percent of FHA borrowers earned less than $50,000, doubling the conventional market where only 27.6 percent of borrowers earned less than $50,000.

Ironically, as the above numbers reveal, FHA's mission to serve underserved populations has been increasingly focused during the same period as the decline in FHA's presence in the market. Thus we are losing FHA's impact at the very time when we need it most. The result is that American families are either turning to more expensive financing or giving up.

It is crucial that FHA keep pace with changes in the U.S. mortgage markets. While FHA programs can be the best and most cost-effective way of expanding lending to underserved communities, we have yet to unleash the full potential of these programs to help this country achieve important societal goals.

To be effective in the 21st century, FHA should be empowered to incorporate private sector efficiencies that allow it to change products and programs to meet the needs of today's homebuyers and anticipate the needs of tomorrow's mortgage markets, while at the same time being fully accountable for the results it achieves and the impact of its programs.

I will tell you that, under the strong leadership of Commissioner Brian Montgomery, FHA has undertaken significant changes to its regulations and its operations in a very short time. In the 10 months since the Commissioner was approved by the Senate, FHA has streamlined the insurance endorsement process, reformed appraisal requirements, and

removed unnecessary regulations. He has instilled a spirit of change and a bias for action within FHA.

MBA compliments the Commissioner on his significant accomplishments to date, though we recognize that more work lies ahead. Lenders still report that FHA is difficult to work with and that oversight activities often focus on minor deficiencies in a loan file rather than focusing on issues of true risk to FHA's insurance funds. We are confident in the Commissioner's ability to address these and other issues.

FHA Background

FHA was created as a separate entity by the National Housing Act on June 27, 1934 to encourage improvement in housing standards and conditions, to provide an adequate home financing system by insurance of housing mortgages and credit, and to exert a stabilizing influence on the mortgage market. FHA was incorporated into the newly formed U.S. Department of Housing and Urban Development (HUD) in 1965. Over the years, FHA has facilitated the availability of capital for the nation's multifamily and single-family housing market by providing government insured financing on a loan-by-loan basis.

FHA offers multifamily and single-family insurance programs that work through private lenders to extend financing for homes. FHA has historically been an innovator. Over the past several decades, its mission has increasingly focused on expanding homeownership for those families who would otherwise either be unable to obtain financing or obtain financing with affordable terms. Additionally, the FHA program has been a stabilizing influence on the nation's housing markets due to the fact that it is consistently available at all times and in all places.

FHA Single-family Programs

Single-family FHA-insured mortgages are made by private lenders, such as mortgage companies, banks and thrifts. FHA insures single-family mortgages with more flexible underwriting requirements than might otherwise be available. Approved FHA mortgage lenders process, underwrite and close FHA-insured mortgages without prior FHA approval. As an incentive to reach into harder to serve populations, FHA insures 100 percent of the single-family mortgage loan balance as long as the loan is properly underwritten.

FHA has a strong history of innovating mortgage products to serve an increasing number of homebuyers. FHA was the first nationwide mortgage program; the first to offer 20-year, 25-year, and finally 30-year amortizing mortgages; and the first to lower downpayment requirements from 20 percent to ten percent to five percent to three percent. FHA was the first to ensure mortgage lending continued after local economic collapses or regional natural disasters.

FHA's primary single-family program is funded through the Mutual Mortgage Insurance Fund (MMIF), which operates similar to a trust fund and is completely self-sufficient. This allows FHA to accomplish its mission at little or no cost to the government. In fact, FHA's operations transfer funds to the U.S. Treasury each year, thereby reducing the Federal deficit. FHA has always accomplished its mission without cost to the taxpayer. At no time in FHA's history has the U.S. Treasury ever had to "bail out" the MMIF or the FHA.

Unleashing FHA's Potential

In order to unleash its potential, MBA believes changes should be made to three areas of FHA. FHA needs flexible authority to introduce new products and program changes, the ability to directly invest a portion of its revenues into technology improvements, and greater control in managing its human resources. These changes will allow FHA to become an organization that can effectively self-adapt to shifting mortgage market conditions and meet the homeownership needs of those families who continue to be unserved or underserved today.

Program Authority and Product Development

FHA programs are sometimes slow to adapt to changing needs within the mortgage markets. In today's market, an organization must be able to move quickly to solve problems and address needs.

A prime example of this problem can be found in the recent experience of FHA in offering hybrid Adjustable Rate Mortgage (ARM) products. A hybrid ARM is a mortgage product which offers borrowers a fixed interest for a specified period of time, after which the rate adjusts periodically at a certain margin over an agreed upon index. Lenders are typically able to offer a lower initial interest rate on a 30-year hybrid ARM than on a 30-year fixed rate mortgage. During the late 1990s, hybrid ARMs grew in popularity in the conventional market due to the fact that they offer borrowers a compromise between the lower rates associated with ARM products and the benefits of a fixed rate period.

In order for FHA to offer this product to the homebuyers it serves, legislative approval was required. After several years of advocacy efforts, such approval was granted with the passage of Public Law 107-73 in November 2001. Unfortunately, this authority was not fully implemented until the Spring of 2005.

The problem began when PL 107-73 included an interest rate cap structure for the 5/1 hybrid ARMs that was not viable in the marketplace. The 5/1 hybrid ARM has been the most popular hybrid ARM in the conventional market. As FHA began the rulemaking process for implementing the new program, they had no choice but to issue a proposed rule for comment with a 5/1 cap structure as dictated in legislation. By the time MBA submitted our comment letter on the proposed rule to FHA, we had already supported efforts within Congress to have legislation introduced that would amend the statute to

change the cap structure. Our comments urged that, if passed prior to final rulemaking, the 5/1 cap fix be included in the final rule.

On December 16, 2003, Public Law 108-186 was signed into law amending the hybrid ARM statutes to make the required technical fix to the interest rate cap structure affecting the 5/1 hybrid ARM product. At this point, FHA was ready to publish a final rule. Regardless of the passage of PL 108-186, FHA was forced to go through additional rulemaking in order to incorporate the fix into regulation. Thus on March 10, 2004, FHA issued a Final Rule authorizing the hybrid ARM program, with a cap structure that made FHA's 5/1 hybrid ARM unworkable in the marketplace. It was not until March 29, 2005 that FHA was able to complete rulemaking on the amendment and implement the new cap structure for the 5/1 hybrid ARM product.

The hybrid ARM story demonstrates well the statutory straitjacket that FHA operates under. A four to six year lag in introducing program changes is simply unacceptable in today's market. Each year that a new program is delayed or a rule is held up, families who would benefit from the program either turn to more expensive alternatives or simply give up.

As such, MBA believes FHA needs greater autonomy so it can make technical changes in its programs and develop new products that will better serve those who are not adequately served by the conventional market. MBA supports FHA's proposed changes to the National Housing Act that would expand the flexibility FHA has to make program changes and to innovate needed product features. However, we believe that FHA should be afforded wider latitude to make program and product changes, to adapt to changing market conditions and to again be a leader in mortgage market innovations.

I would like to spend some time offering MBA's perspective on each of the proposed changes.

Downpayment Requirements

MBA supports the elimination of the complicated formula for determining the downpayment that is currently detailed in statute. The calculation is obviously outdated and unnecessarily complex. The calculation of the downpayment itself is often cited by originators as a reason for not offering the FHA product. They simply do not want to hassle with it. This section of the National Housing Act should be removed and the development of the calculation left to the FHA Commissioner to determine through regulation. MBA would suggest that the downpayment be calculated as a straight percentage of the lesser of the sales price or appraised value.

MBA supports the elimination of the statutory requirement that the borrower provide a minimum cash investment. Improving FHA's products with such downpayment flexibility is one of the most important innovations that FHA can be empowered to make. Independent studies have demonstrated two important facts: first, the downpayment is one of the primary obstacles for first-time homebuyers, minorities, and low- and

moderate-income homebuyers. Second, the downpayment itself is not as important a factor in determining risk as are other factors, such as credit score.

The private market has already demonstrated that the downpayment can be replaced with other risk-mitigating features without significantly hurting performance. Certainly, many borrowers will be in a better financial position if they keep the funds they would have expended for the downpayment as a cash reserve for unexpected homeownership costs or life events.

We believe that FHA should be empowered to establish policies that would allow borrowers to qualify for a certain flexible downpayment and then decide the amount of the cash investment they would like to make in purchasing a home.

Adjusting Mortgage Insurance Premiums for Loan Level Risk

MBA recognizes that FHA may be able to serve more borrowers and do so with lower risk to the MMIF if they are able to adjust premiums based on the risk of each mortgage it insures. A flexible premium structure could also give borrowers greater choice in how they utilize the FHA program.

We caution, though, that creating a risk based premium structure will only be beneficial to consumers if there is a lowering of current premiums. We would not support simply raising current premiums for higher risk borrowers.

In December 2004, FHA eliminated the practice of refunding the unearned portion of the Up-front Mortgage Insurance Premium (UfMIP) to borrowers who prepay their FHA-insured mortgage early and go to another product. MBA was hopeful that the removal of the refund (which admittedly was an administrative cost for FHA and servicers) would have been followed by a correlated lowering of the UfMIP. This did not happen. The net effect was to actually raise the cost of the FHA program. MBA would not want to see the same thing happen under a risk-based premium structure.

Raising Maximum Mortgage Limits

MBA supports the proposal to raise FHA's maximum mortgage limits to 100 percent of an area's median home price (currently pegged at 95 percent) and to raise the ceiling to 100 percent of the conforming loan limit (currently limited to 87 percent) and the floor to 65 percent (currently 48 percent). This proposal is similar to that contained in H.R. 176 introduced by Representaitve Gary Miller (R-CA) and Representative Barney Frank (D-MA), which MBA supports.

There is a strong need for FHA financing to be relevant in areas with high home prices. MBA believes raising the limits to conforming limits in these areas strikes a good balance between allowing FHA to serve a greater number of borrowers without exceeding its mission or taking on excessive risk. In fact, MBA believes that such a move will improve FHA's portfolio performance.

Additionally, in many low cost areas, FHA's loan limits are not sufficient to cover the costs of new construction. New construction targeted to first-time homebuyers has historically been a part of the market in which FHA has had a large presence. MBA believes raising the floor will improve the ability of home builders to build modest homes in low-cost areas because first-time homebuyers will be able to use FHA-insured financing.

Lengthening Mortgage Term

MBA supports authorizing FHA to develop products with mortgage terms up to 40 years. Currently, FHA is generally limited to products with terms of no more than 30 years. Stretching out the term will lower the monthly mortgage payment and allow more borrowers to qualify for a loan while remaining in a product that continues to amortize. We think FHA should have the ability to test products with these features, and then, based on performance and homebuyer needs, to improve or remove such a product.

Consolidation of Single-Family Programs in the MMIF

FHA's proposal to place nearly all single-family mortgage programs within the MMIF certainly is worth considering. Currently, these products are in the General Insurance/Special Risk Insurance (GI/SRI) Fund, which effectively requires them to be scored individually and, if it is determined that the costs exceed the premiums, requires an appropriation from Congress. Such a change would most notably effect the 203(k), HECM, and condominium programs. To the extent that moving the programs to the MMIF allows FHA to obtain some cross-subsidization for products that serve an important social goal but may be more costly on average, MBA would be in support of such a change.

Improvements to FHA Condominium Financing

MBA supports changes to FHA's condominium program that will streamline the process for obtaining project approval and allow for greater use of this program. It is unfortunate to note that FHA insurance on condominium units has dropped at a higher rate than the overall decline in FHA's originations. This decline contradicts the fact that in costly markets, condominium units are typically the only type of housing within FHA's loan limits. Condominium units are also a large source of first-time homebuyer housing. FHA should have a much bigger presence in the condominium market.

Improvements to the Reverse Mortgage Program

Finally, MBA unequivocally supports all of the proposed changes to FHA's Home Equity Conversion Mortgage (HECM) program: the removal of the current 250,000 loan cap, the authorization of HECMs for home purchase and on properties less than one year old, and the creation of a single, national loan limit for the HECM program.

The HECM program has proven itself to be an important financing product for this country's senior homeowners, allowing them to access the equity in their homes without having to worry about making mortgage payments until they move out. The program has allowed tens of thousands of senior homeowners to pay for items that have given them greater freedom, such as improvements to their homes that have allowed them to age in place, or to meet monthly living expenses without having to move out of the family home.

MBA believes it is time to remove the program's cap because the cap threatens to limit the HECM program at a time when more and more seniors are turning to reverse mortgages as a means to provide necessary funds for their daily lives. MBA believes that the HECM program has earned the right to be on par with other FHA programs that are subject only to FHA's overall insurance fund caps. Additionally, removing the program cap will serve to lower costs as more lenders will be encouraged to enter the reverse mortgage market.

Additionally, authorizing the HECM program for home purchase will improve housing options for seniors. In a HECM for purchase transaction, a senior homeowner might sell a property they own to move to be near family. The proceeds of the sale could be combined with a reverse mortgage, originated at closing and paid in a lump sum, to allow a senior to purchase the home without the future responsibility of monthly mortgage payments. Alternatively, a senior homeowner may wish to take out a reverse mortgage on a property that is less than one year old, defined as "new construction" by FHA.

Finally, the HECM program should have a single, national loan limit equal to the conforming loan limit. Currently, the HECM program is subject to the same county-by-county loan limits as FHA's forward programs. HECM borrowers are disadvantaged under this system because they are not able to access the full value of the equity they have built up over the years by making their mortgage payments. A senior homeowner living in a high-cost area will be able to access more equity than a senior living in a lower cost area, despite the fact that their homes may be worth the same and they have the same amount of equity built up. Reverse mortgages are different than forward mortgages and the reasons for loan limits are different, too. FHA needs the flexibility to implement different policies, especially concerning loan limits.

Again, while we applaud these program changes, we believe that FHA should be granted wide latitude to implement program and product changes. Unless FHA is allowed to innovate they will always be following, not leading, the market in addressing the needs of first-time homebuyers, minorities and low and moderate income families that are not adequately served by the private market.

Technology

Technology's impact on U.S. mortgage markets over the past 15 years cannot be overstated. Technology has allowed the mortgage industry to lower the cost of homeownership and has allowed more borrowers to qualify for financing. The creation of automated underwriting systems, sophisticated credit score modeling, and business-to-business ecommerce are but a few examples of technology's impact.

FHA has been detrimentally slow to move from a paper-based process and it cannot electronically interface with its business customers in the same manner as the private sector. During 2004 and 2005, over 1.5 million paper loan files were mailed back and forth between FHA and its approved lenders and manually reviewed during the endorsement process. Despite the fact that FHA published regulations in 1997 authorizing electronic endorsement of loans, FHA was not able to implement this regulation until this past January, eight years after the fact. Complaints by lenders in transacting business with FHA are numerous.

FHA's integration with the industry as a whole is equally deficient. For instance, MBA created the Mortgage Industry Standards Maintenance Organization (MISMO) in 1999, to develop open industry data standards to facilitate the development and acceptance of fully electronic mortgage banking. The industry has released several subsequent versions of the standard. FHA has only adopted the first version, significantly disadvantaging it from garnering the efficiencies that come with an industry standard.

Additionally, as the mortgage industry hurls towards a completely electronic mortgage process, FHA struggles to obtain the simple ability to review and store documents in an electronic format like adobe acrobat ®.

MBA believes FHA cannot create and implement technological improvements because it lacks sufficient authority to use the revenues it generates to invest in technology. Improvements to FHA's technology will allow it to improve management of its portfolio, garner efficiencies and lower costs, which will allow it to reach farther down the risk spectrum to borrowers currently unable to achieve homeownership.

MBA proposes the creation of a separate fund specifically for FHA technology funded by revenues generated by the operation of the MMIF. MBA suggests the establishment of a revenue and a capital ratio benchmark for FHA, wherein, if both are exceeded, FHA can use a portion of the excess revenue generated to invest in its technology. Such a mechanism would allow FHA to invest in technology upgrades, without requiring additional appropriations from Congress or costing taxpayers a dime.

Human Resources

FHA is restricted in its ability to effectively manage its human resources at a time when the sophistication of the U.S. mortgage markets requires market participants to be experienced, knowledgeable, flexible, and innovative. Other Federal agencies, such as

the Federal Deposit Insurance Corporation (FDIC), that interface with and oversee the financial services sector are given greater authority to manage their human resources. MBA believes that FHA should have similar authority if it is to remain relevant in providing homeownership opportunities to those families underserved by the private markets.

FHA should have more flexibility in its personnel structure than that which is provided under the regular Federal civil service rules. With greater control over the personnel structure, FHA could operate more efficiently and effectively at a lower cost. Further, improvements to FHA's ability to manage its human capital will allow FHA to attract and manage the talent necessary to develop and implement the strategies that will effectively provide opportunities for homeownership to underserved segments of the market.

FHA Multifamily Programs

While the focus of this hearing is on FHA's single-family programs, I would be remiss if I did not mention the importance of FHA's multifamily programs in providing decent, affordable housing to many Americans. There are a number of families and elderly citizens who either prefer to rent or who cannot afford to own their own homes. FHA's insurance of multifamily mortgages provides a cost-effective means of generating new construction or rehabilitation of rental housing across the nation.

While Commissioner Montgomery has not yet focused his attention on improving the multifamily programs, we hope that process improvements on the multifamily side of FHA will soon be discussed.

MBA's recommendations above, for (1) providing FHA greater flexibility to make program changes and develop new products, (2) allowing FHA to use revenues generated by the programs to improve technology, and (3) providing more flexibility to FHA in managing its human resources, are equally important for its multifamily programs. Any efforts to transform FHA for the 21st century should include FHA's multifamily programs.

Conclusion

FHA's presence in the single-family marketplace is smaller than it has been in the past and its impact is diminishing. Many MBA members, who have been traditionally strong FHA lenders, have seen their production of FHA loans drop significantly. This belies the fact that FHA's purposes are still relevant and its potential to help borrowers is still necessary.

The time to act is now. MBA calls upon this Subcommittee to advance legislative proposals that will allow FHA to be freed from overly burdensome processes and restrictions and empowered to adopt important product changes, to procure new technologies and to implement better management of its human resources. By doing

so, Congress will empower FHA to be a vital part of today's mortgage market and expand opportunities to underserved homebuyers and renters.

If Congress does not act, MBA believes that consumer choice will be diminished and an increasing number of borrowers, especially first-time, minority, and low- and moderate-income borrowers, will be unable to find affordable homeownership financing.

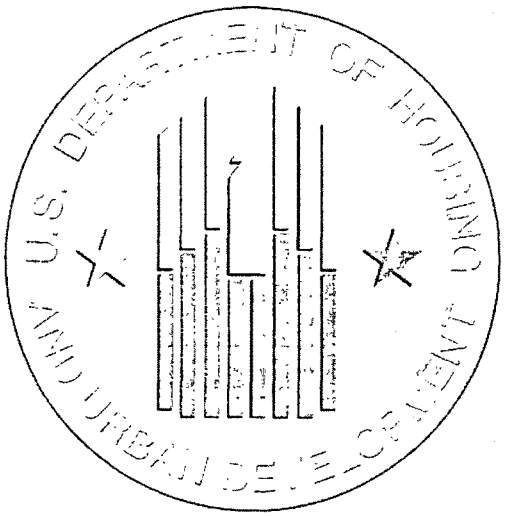
On behalf of MBA, I would like to thank the Subcommittee for the opportunity to testify here today. MBA looks forward to working with Congress and HUD to improve FHA's ability to serve aspiring homeowners.

STATEMENT OF BRIAN D. MONTGOMERY

Assistant Secretary for Housing – Federal Housing Commissioner
U.S. Department of Housing and Urban Development

Hearing before the United States House Committee on Financial Services, Subcommittee on Housing and Community Opportunity

United States House of Representatives



"Transforming the Federal Housing Administration for the 21st Century"

April 5, 2006

Thank you Chairman Ney and Ranking Member Waters for inviting me to be here today to testify on the Administration's proposed FHA Modernization Act.

The bill itself is really very simple, the proposal straightforward. It does just what its name suggests: it modernizes the 72-year-old Federal Housing Administration and restores the agency to its intended place in the mortgage market. Nothing more, nothing less. Yet, the impact of this bill may be tremendous.

Let me explain. FHA was created in 1934 to serve as an innovator in the mortgage market, to meet the needs of citizens otherwise underserved by the private sector, to stabilize local and regional housing markets, and to support the national economy. This mission is still very relevant, perhaps now more so than ever, and most of us would agree that FHA can and should continue to play its important role.

Unfortunately, over the last few years, the housing agency that helped bring the nation out of the Depression, the agency that helped our grandparents and our parents buy their first homes, the agency that stood by the oil patch and rust belt states in the 1980s when the entire real estate market sank in parts of California, Texas, Louisiana, Michigan, Ohio, New York and Pennsylvania – that agency became an almost invisible presence. President Bush committed the federal government and the housing industry to reach an additional five million minority homebuyers by the end of 2010, but the agency most suited to reaching these families was falling behind.

FHA was falling behind for a variety of reasons, from outdated business practices to cumbersome program requirements. Over the last six months, we have made significant changes, streamlining and realigning FHA's operating procedures. While these changes are good and long overdue, they are not enough, a point that FHA's industry partners have clearly conveyed. Therefore, FHA is now requesting that we amend the law to give FHA the flexibility it needs to fulfill its original mission in today's marketplace.

Over the last ten years, the industry changed dramatically. Reliance on automated underwriting systems and risk-based pricing is standard operating procedure today. A multitude of innovative new products were created. The secondary mortgage market was transformed into an investors' paradise, where the array of investment options seemed endless. While this transformation happened, FHA stayed the course; the world changed and FHA remained the same. Simply put, the dynamic mortgage market passed FHA by. For example, in Congressman Tiberi's district, FHA's volume has dropped from 3,096 loans in 2000 to 1,735 loans in 2005. For Congresswoman Harris, during that same time period, FHA's volume dropped from 2,354 to 621 loans. For Ranking Member Waters, FHA's volume has all but shriveled up from 2,207 loans in 2000 to just 34 loans in 2005.

And without a viable FHA, many homebuyers – first-time homebuyers, minority homebuyers and homebuyers with less-than-perfect credit – were left with fewer safe and affordable options. Hundreds of thousands of families heard the message that homeownership helps families build wealth and brings stability to communities. They

wanted to share in the good times. Many of them were able to become homebuyers, but many of them paid a steep price to do so.

Without a viable FHA alternative, many homebuyers turned to high-cost financing and nontraditional loan products to afford their first homes. While low initial monthly payments seemed like a good thing, the reset rates on some interest-only loans are substantial and many families are unable to keep pace when the payments increase. In addition, prepayment penalties make refinancing cost-prohibitive. According to Moody's Economy.com, more than $2 trillion of U.S. mortgage debt, or about a quarter of all mortgage loans outstanding, comes up for interest rate resets in 2006 and 2007. While some borrowers will make the higher payments, many will struggle. Some will be forced to sell or lose their homes to foreclosure. The foreclosure rate for subprime loans is twice that of prime loans. And I think we can all agree that foreclosures are bad for families, bad for neighborhoods, and bad for the economy as a whole.

I know that you're as concerned as I am. I've seen the various pieces of legislation designed to regulate high-cost loans and the lenders who make these loans. We've all heard the warnings from the Federal Reserve, the Office of the Comptroller of the Currency, and the Federal Trade Commission regarding the risk of high-cost loans. And we're all aware of the state and local efforts to regulate this business.

All that said, the FHA Modernization Act is part of the solution. FHA reform is designed to give homebuyers who can't qualify for prime financing a choice again. The legislation will allow FHA to fulfill its original mission, just like it did in 1934, when the same kinds of circumstances existed. In 1934, interest-only loans and balloon loans were prevalent, so FHA was established to give the private sector a way to provide long-term, fixed-rate financing.

I said at the outset that this bill is very simple. It represents a simple solution to a complex problem that affects all of us in this nation. We can talk and talk and issue warnings and guidance. We can create regulations and restrictions and force homebuyers to educate themselves. But really, when it comes right down to it, wouldn't it be a whole lot easier simply to just offer families a better alternative?

I know my introduction was lengthy, but I want you to understand how important FHA reform is to homebuyers and to the industry as a whole. FHA's private sector partners – the brokers, the realtors, the lenders, the home builders – want to tell their clients about the FHA alternative. They want low- to moderate-income homebuyers to have a safer, more affordable financing option. They want FHA to be a viable player again.

Now let me explain a little bit about the simple changes we're proposing. For one, we're proposing to eliminate the complicated downpayment calculation and the traditional cash investment requirement that have been the hallmark of FHA for years. Before the rest of the market began offering low downpayment loans, FHA was often the best option for first-time homebuyers because it required only a minimal downpayment.

But, as I said before, the market passed FHA by. Last year, 43 percent of first-time homebuyers purchased their homes with *no* downpayment. Of those who did put money down, the majority put down two percent or less.

The downpayment is the biggest barrier to homeownership in this country, but FHA has no way to address the barrier without changes to its statute. The FHA Modernization Act proposes to permit borrowers to choose how much to invest, from no money down to one or two or even ten percent. Many first-time homebuyers choose to put less money down simply to save their hard-earned cash to purchase other items to furnish or update their homes. This kind of home-related buying is the reason the housing market contributes so significantly to the overall health of the national economy.

The bill also proposes to provide FHA the flexibility to set the FHA insurance premiums commensurate with the risk of the loans. For example, low downpayment loans would be priced higher, yet appropriately and reasonably to give homebuyers a fairly-priced option and to ensure that FHA's insurance fund is compensated for taking on the additional risk. FHA would also consider the borrower's credit profile when setting the insurance premium. FHA would charge lower-credit risk borrowers a lower insurance premium than it does today, and higher-credit risk borrowers would be charged a slightly higher premium. In so doing, FHA could reach deeper into the pool of prospective borrowers, while protecting the financial soundness of the FHA Fund.

The primary concerns with a risk-based pricing approach are that FHA will target people who shouldn't be homebuyers and charge them more than they should pay. I want to address these concerns directly. Our goal is to reach families who are capable of becoming homeowners and to offer them a safe and fairly-priced loan option.

With a risk-based premium structure, FHA can reach hard-working, credit-worthy borrowers – such as store clerks, bus drivers, librarians, and social workers – who, for a variety of reasons, do not qualify for prime financing. Some have poor credit scores due to circumstances beyond their control, but have put their lives back together and need a second chance. For some, the rapid appreciation in housing prices has simply outpaced their incomes. Many renters find it difficult to save for a downpayment, but have adequate incomes to make monthly mortgage payments and do not pose a significant credit risk. They simply need an affordable financing vehicle to get them in the door. FHA can and should be there for these families.

The higher premiums that FHA will charge some types of borrowers are still substantially lower than they would pay for subprime financing. Let me repeat that point: the higher premiums that FHA will charge some types of borrowers are still substantially lower than they would pay for subprime financing. The cost of a loan with a higher FHA insurance premium is still substantially lower than the cost of a loan with a higher interest rate. For example, if FHA charged a 3 percent upfront insurance premium for a $225,000 loan to a credit-impaired borrower versus that same borrower obtaining a subprime loan with an interest rate 3 percent above par, the borrower would pay over $255 more in

monthly mortgage payments with the subprime loan and over $125,000 more over the life of the loan, if they kept it for a full 30-year term.

Moreover, as I stated earlier, FHA intends to lower the insurance premium for some borrowers. FHA will charge lower-risk borrowers a substantially lower premium than these types of borrowers pay today. For example, homebuyers with higher credit scores who choose to invest at least 3 percent in a downpayment may pay as little as half a percent upfront premium.

So, while FHA may charge riskier borrowers more (and less risky borrowers less) than it does today, the benefit is three-fold. First, FHA will be able to reach additional borrowers the agency can't serve today. There is nothing that upsets us more than to see people taken to the cleaners when they would have fared better with an FHA-insured product. Second, these borrowers will pay less with FHA than with a subprime loan. And finally, the FHA Fund will be managed in a financially sound manner, with adequate premium income to cover any losses.

Another change proposed in the FHA Modernization Act is to increase FHA's loan limits. FHA's loan limit in high-cost areas would rise from 87 to 100 percent of the GSE conforming loan limit and in lower-cost areas from 48 to 65 percent of the conforming loan limit. In between high and lower-cost areas, FHA's loan limit will increase from 95 to 100 percent of the local median home price. This change is extremely important and crucial in today's housing market. In many areas of the country, the existing FHA limits are lower than the cost of new construction. Buyers of new homes can't choose FHA financing in these markets. In other areas, FHA has simply been priced out of the market. For example, in 1999, FHA insured 127,000 loans in the state of California; in 2005, FHA insured only 5,000.

FHA is also proposing some changes to specific FHA products. For example, the bill proposes to permit FHA to insure mortgages on condominiums under its standard single family product. The existing condo program is very specialized and burdensome, as a result of outdated statutory provisions that were written at a time when condominiums were an unfamiliar form of ownership. Condos represent 25 percent of the new and 12 percent of the existing home market today and serve as one of the primary forms of affordable housing for first-time homebuyers. In fact, condos tend to be closer to city centers and offer lower income borrowers an opportunity to buy an affordable home without moving far from their jobs and away from the public transportation that gets them to those jobs. Therefore, FHA should be able to serve condo buyers, just like any other homebuyers, under its standard single family program.

Our reform bill also proposes to modernize the Title I manufactured housing program, eliminating the portfolio insurance feature from the program and increasing the loan limits to reflect the real cost of manufactured housing today. The existing statute restricts FHA claim payments to 10 percent of the value of a lender's loan portfolio. With portfolio insurance, lenders are not guaranteed coverage against loss and subsequently price their loans for additional risk. The higher loan costs, in turn, increase

the likelihood of borrower default. With additional default risk, but insufficient coverage, the losses grew to unsustainable levels in the 1990s and Ginnie Mae pulled out of the program. Ginnie Mae has testified that with the elimination of this outdated insurance model it would reconsider participation in the Title I securities market, which will bring in more lenders and drive down the costs of manufactured home financing.

Finally, the FHA Modernization Act offers some changes to the Home Equity Conversion Mortgage (HECM) program, which enables senior homeowners, aged 62 years or older, to tap into their home equity to live comfortably in their golden years. The bill proposes elimination of the cap on the number of loans FHA can insure; a single, national loan limit set at conforming; and a new HECM for Home Purchase product to permit seniors to move from the family home to more suitable senior housing and convert the purchase loan into a HECM in a single transaction. Today, seniors who want to move, but need additional cash flow to pay their living expenses, must purchase a new home and take out a HECM in two distinct transactions, resulting in two sets of loan fees and charges.

Let me assure you that the changes we are proposing will not increase the overall risk of the MMI Fund or impose a potential cost on taxpayers. We are proposing to manage the Fund in a financially prudent way, beginning with the change in FHA pricing to match premiums with risk. This will avoid FHA being exposed to excessive risk, as it is today, because some borrowers who use FHA are under-charged for their risk to the Fund while others are overcharged. Of course, we will continue to monitor the performance of our borrowers very closely, and make adjustments to underwriting policies and/or premiums as needed.

I know I've talked a lot here today, but I want to convey to you how passionate I am about the proposed changes. I believe we have an opportunity to make a difference in the lives of millions of lower- and modest-income Americans. We have a chance to bring FHA back into business, to restore the FHA product to its traditional market position. To all those families who can buy a home with prime conventional financing, I say, "Go for it!" They're fortunate and they should take full advantage of that benefit. But for those who can't, FHA needs to be a viable option. And when people ask me why are we proposing these changes, I tell them these exact words: "Families need a safe deal, at a fair price. Families need a way to take part in the American Dream without putting themselves at risk. Families need FHA."

I want to thank you again for providing me the opportunity to testify here today on the FHA Modernization Act. I look forward to working with all of you to make these reforms a reality.

Prepared Testimony of

A.W. Pickel, III, CMC, Past President

National Association of Mortgage Brokers

on

Transforming the Federal Housing Administration for the 21st Century

before the

Subcommittee on Housing and Community Opportunity

Committee on Financial Services

U.S. House of Representatives

Wednesday April 5, 2006

Good morning Chairman Ney and members of the subcommittee, I am A.W. Pickel, III, Past President of the National Association of Mortgage Brokers ("NAMB"). Thank you for inviting NAMB to testify today on transforming the Federal Housing Administration ("FHA") for the 21st Century. In particular, we appreciate the opportunity to address the need to: (1) increase FHA loan amounts for high-cost areas, (2) develop risk-based pricing for mortgage insurance on FHA loans, and (3) reform the FHA program to reduce the barriers to mortgage broker participation.

NAMB is the only national trade association exclusively devoted to representing the mortgage brokerage industry. As the voice of the mortgage brokers, NAMB speaks on behalf of more than 25,000 members in all 50 states and the District of Columbia.

America enjoys an all-time record rate of homeownership today. Mortgage brokers have contributed to this achievement as we work with a large array of homebuyers and capital

sources to originate the majority of residential loans in the United States. At the end of last year, the overall homeownership rate neared 70%. This is an astounding number until one realizes that the homeownership rate for Hispanics is just over 50% and for African-Americans, is only 48%. Many families still need assistance in obtaining homeownership and NAMB believes that the proposed reforms to the FHA program are critical to expanding homeownership opportunities for prospective first-time, minority, and low to moderate-income homebuyers.

FHA Utilization of Mortgage Brokers

NAMB supports the U.S. Department of Housing and Urban Development's ("HUD") proposed reforms to the FHA program ("Proposal"), but believes that the FHA program must first be a viable option for prospective borrowers. Regardless of how beneficial a loan product may be, it requires an effective distribution channel to deliver it to the marketplace. Unfortunately, many prospective borrowers are denied the benefits offered by the FHA program because mortgage brokers—the most widely used distribution channel in the mortgage industry—are limited in offering FHA loan products.

According to Wholesale Access, mortgage brokers originated 38.6 percent of all FHA loans for a total of $110 billion in 2003. Mortgage brokers want to further increase origination of FHA loan products for first-time, minority and low to moderate-income homebuyers. However, current financial audit and net worth requirements create a formidable barrier to mortgage broker participation in the FHA program. This barrier makes it difficult for mortgage brokers to offer FHA loan products to those borrowers that could clearly benefit by participating in the FHA program.

NAMB supports increased access to FHA loans so that prospective borrowers who may have blemished or almost non-existent credit histories, or who can afford only minimal down payments, have increased choice of affordable loan products and are not forced by default to the sub-prime loan market. In this spirit, NAMB believes the audit and net worth requirements should be eliminated for mortgage brokers that want to offer FHA loan products to consumers.

First, current FHA requirements impose cost prohibitive and time consuming annual audit and net worth requirements on mortgage brokers that want to originate FHA loans. These requirements place serious impediments in the origination process that functionally bar mortgage brokers from distributing FHA loans to the marketplace, leaving sub-prime loan products as the only other option for many borrowers.

Most small businesses find the cost to produce audited financial statements a significant burden. An audit must meet government accounting standards and only a small percentage of certified public accountants ("CPAs") are qualified to do these audits. Moreover, because many auditors do not find it feasible to audit such small entities to government standards, even qualified CPA firms are reluctant to audit mortgage brokers. Cost is not the only factor. A mortgage broker can also lose valuable time—up to several weeks—preparing for and assisting in the audit. Between the cost of hiring an accountant

who meets government auditing standards and is willing to conduct the audit and the hours needed to compile and report the needed data, it is simply impractical for a small business to conduct this type of financial audit.

The net worth requirement for mortgage brokers is also limited to liquid assets because equipment and fixtures depreciate rapidly and loans to officers and goodwill are not allowable. Adding insult to injury, a broker who greatly exceeds the net worth requirement is forced to keep cash or equivalents of 20% of net worth up to $100,000. There has been no evidence presented by FHA that loans originated by high net worth originators perform better than those with a lower net worth.

Moreover, annual audit and net worth requirements are unnecessary. Originators are already governed by contract agreements with their respective FHA-approved lenders, affording HUD adequate protection against loss. FHA-approved lenders already submit to audits, thereby ensuring that customers are protected and can seek relief from dishonest originators.

In sum, the audit and net worth requirements are prohibitively expensive for a large majority of mortgage brokers and as a direct result, many brokers have been left with little choice but to originate loans other than FHA. As a result, the audit and net worth requirements actually limit the utility and effectiveness of the FHA program and seriously restrict the range of choice available for prospective borrowers who can afford only a minimal down payment. At a minimum, NAMB believes annual bonding requirements offer a better way to ensure the safety and soundness of the FHA program than requiring originators to submit audited financial statements.

Second, FHA's formal position is that it only approves lenders to originate FHA loans. FHA does not even acknowledge the term "mortgage broker" in its guidelines and therefore, no provision currently exists that would explicitly permit mortgage brokers to originate FHA loans. In fact, until several years ago, FHA required all loans to be closed in the name of the originating party. Fortunately, this prohibition was somewhat alleviated when FHA allowed the loan to close in the name of the actual source of the funds. Today, anyone who originates, but is not the ultimate source of funds, is referred to as a "Correspondent Lender"—a term normally only used for mortgage bankers.

A stated objective of HUD, and the FHA program, is to increase origination of FHA loan products and expand homeownership opportunities for first-time, minority, and low to moderate-income families. NAMB believes the solution to increase FHA loan production is simple—allow more stores, such as mortgage brokers, to offer FHA loan products directly to consumers. As stated previously, mortgage brokers originate the majority of all residential loans and therefore, would provide HUD with the most viable and efficient distribution channel to bring FHA loan products to the marketplace.

FHA Risk-Based Premiums are Relevant to the Market

The ability to match borrower characteristics with an appropriate mortgage insurance premium has been recognized as essential by every private mortgage insurer ("PMI"). PMI companies have established levels of credit quality, loan-to-value and protection coverage to aid in this matching process. They also offer various programs that allow for upfront mortgage insurance premiums, monthly premiums or combinations of both. This program flexibility has enabled lenders to make conventional loans in the private marketplace that either are not allowable under FHA or that present a risk level that is currently unacceptable to FHA.

Unfortunately, where FHA is not available as a viable competitor, PMI premiums are quite expensive. Should FHA decide to enter this market, it will increase competition for these programs and ultimately, drive down costs for borrowers.

For example, many mortgage products that require minimal or no down payment or equity do not use PMI insurance. Rather, these loans are split into two—a first mortgage, which is offered at a lower interest rate, and then a second mortgage offered at a considerably higher interest rate. This "combo" or "80/20" type of mortgage product is commonly offered to borrowers with less than perfect credit. Borrowers who are unable to adequately prove their income also commonly utilize "combo" mortgages. In this market, PMI may not be offered or is offered at a prohibitively high premium. Again, FHA could act as a competitor to drive down costs for these types of products.

Risks Posed to FHA by Risk-Based Premiums

PMIs have demonstrated the ability to balance risk with the premiums charged and the FHA program should be afforded the same opportunity. If the risks are assessed appropriately, the premiums charged should ensure that the Mutual Mortgage Insurance Fund ("MMIF") will not be adversely affected. FHA is not required to make a suitable profit or demonstrate market growth to shareholders; therefore, it is likely that FHA can afford to assume even greater risk levels than PMIs can currently absorb. This increased capacity to assume and manage risk will allow FHA to serve even those borrowers who presently do not have PMI available as a choice.

This Proposal also allows FHA to offer lower premiums to lower credit risk homebuyers, which will have the net effect of reducing the overall default rates at FHA. Recent changes made by HUD such as permitting formerly non-allowable fees to be charged and utilizing Fannie Mae appraisal guidelines have had the effect of modernizing the FHA program. These advances make the FHA program easier to use, which in turn attracts more borrowers who would not otherwise tolerate the red-tape long-associated with origination of FHA loans. Real estate agents, sellers and mortgage companies who have not viewed FHA financing as a viable alternative to the private marketplace would also return to the program, bringing with them suitable borrowers that would make FHA's default rate comparable to that of conventional loans.

Because a substantial body of data for risk-based lending is available, this Proposal is not a leap into the unknown. Rather, it creates a venue to bring FHA into parity with what has already proven to be reasonable assumption of risk for the marketplace.

This Proposal is not intended to be a change to the FHA program that will create losses. Rather, it is designed to avoid losses to the MMIF. The Proposal contains needed reforms that will help FHA meet its chartered mandate of increasing homeownership opportunities for first-time, minority and low to moderate-income homebuyers, and which may actually have the side effect of improving the solvency of the MMIF.

All insurance constructs involve assumption of risk. When an insurer can use sound actuarial data and price in a manner that is responsive to trends revealed by such data, the risk is spread over a sufficiently large base to minimize the chance of loss. Because FHA's share of the market is approaching marginal levels, the risks to the program are likely to be greater under the status quo than with the Proposal.

Benefits to Consumers, Particularly First-Time HomeBuyers, Minority and Low to Moderate-Income Families

Lenders and insurers tend to demand a higher proportional return when they enter a riskier market. It has been demonstrated that the return demanded is considerably higher for sub-prime loan products than for prime loans because of the inherent risks presented by the sub-prime market. At the same time, consumer advocates have claimed that fees and rates for many sub-prime borrowers are too high. FHA has the ability to enter into the sub-prime market safely and still offer significant savings to prospective borrowers. The benefits received by expanded FHA entry into the sub-prime market would be particularly useful for first-time, minority and low to moderate-income homebuyers who could receive prime interest rates on their loans by using FHA insurance.

The FHA program also possesses many attributes that are particularly friendly to prospective borrowers who may have less money available for closing costs, temporary income, or a limited credit history. For example, FHA Direct Endorsement Underwriters are given considerable latitude to make loans that they believe should be made, but may not have all of the requisite attributes conventional guidelines require. FHA servicing is far less likely to quickly send a loan to foreclosure and must follow borrower-friendly practices whereas some conventional lenders have been cited for questionable loan servicing practices. FHA loans usually offer fixed interest rates compared to the adjustable rates offered on most sub-prime mortgages.

Whether This Proposal Supplants or Complements the Private Sector

We should look first where this Proposal complements the conventional sector, and then address whether the Proposal supplants. As discussed earlier, America is built on the concept that competition is healthy for the market. It improves efficiency and quality while offering more competitively-priced products to consumers. Making FHA more competitive will improve the services and products provided by other lenders and

insurers in the industry. Consumers will be offered FHA programs that serve a similar purpose but are certainly not identical to conventional programs now available. This healthy level of competition should drive down the cost of programs that serve those with minimal down payments or who need flexible underwriting to obtain home financing.

Borrowers who can afford larger down payments or who have reasonable equity levels do not find the FHA program to be a reasonable alternative to conventional financing. Nearly all FHA borrowers have a loan-to-value ratio in excess of ninety percent. Since 1980, FHA has never served more than fifteen percent of the total housing market but, at times, it insured nearly fifty percent of urban mortgages. Clearly, the Proposal will not make the FHA program a threat to the overall mortgage market. At most, this Proposal will help to restore FHA loan product origination to levels of previous years.

Nevertheless, the possibility that FHA could supplant certain conventional loans does exist.. Such a result is inevitable if FHA regains market share. However, the conventional loans most likely to be supplanted are those made to borrowers who fall just short of receiving A-grade conventional loans, but do not deserve a sub-prime loan. Many first-time, minority and low to moderate-income homebuyers find themselves in this situation but are forced to turn to the sub-prime market to achieve homeownership. This Proposal makes FHA loan products a viable alternative for these prospective borrowers.

The Elimination of the Down Payment Requirement

NAMB supports eliminating the down payment requirement and granting FHA the flexibility to offer 100% financing to aid in the effort to increase homeownership for first-time, minority, and low to moderate-income families.

Homeownership is a dream that many wish to experience, but for years barriers have existed that prevent many low-income and minority families from purchasing a home. In fact, a recent study published in March 2006 by the Center for Housing Policy[1] reveals that many working minority families with children are less likely to achieve the dream of homeownership today than in the 1970s. A principal barrier to achieving homeownership for these families is financial – the lack of money for a down payment and closing costs. The Proposal to eliminate the down payment requirement will help break down this financial barrier for many low to moderate-income and minority families. This Proposal will help significantly to achieve the Administration's stated goal of increasing minority homeownership by 5.5 million by 2010.

[1] The Center for Housing Policy recently released a study entitled "Locked Out: Keys to Homeownership Elude Many Working Families with Children," in March 2006 which showed that the cost of homeownership outpaced income growth for many low to moderate-income working families with children.

Future of the FHA Program If Proposal is Enacted or Not Enacted

Proposed changes are needed to the FHA program to meet its chartered mandate, which is to aid the underserved and underprivileged obtain the dream of homeownership. PMI will dominate the low and zero down payment market with little competition among the few players in that industry. The sub-prime mortgage market will fulfill the needs of those unable to obtain PMI insurance. Foreclosure rates could escalate. Minority families and first-time homebuyers may be underserved or even shut out of the housing market entirely. It is possible that FHA will have a pool of loans too small to effectively manage risk. Ultimately, FHA could be removed as a helping hand to those who need it the most. The ripple effect of negative consequences could easily extend to the homebuilding industry and to the general economy as well.

On the other hand, Congress has the opportunity to revitalize the FHA program with this Proposal. Borrowers will receive better loan programs at lower interest rates. We strongly urge this subcommittee to support the Proposal.

Increase FHA Mortgage Amounts for High-Cost Areas

Congress and this Administration have made homeownership a priority in this country and indeed, the growth of homeownership in this country has been steadfast for the past few years. Unfortunately, the demand for homes continues to outstrip new housing development and sales of existing homes, causing escalation of home prices. In an environment of rising interest rates, many first-time, minority, and low to moderate-income homebuyers will need the safer and less-expensive financing options that the FHA program can provide. For this reason, NAMB **uniformly** and **unequivocally** supports increasing FHA loan limits in high-cost areas.

To accommodate the escalating demand for homes, NAMB believes the formula used to calculate FHA maximum loan amounts should be revised to make the FHA program accessible to those homebuyers living in high-cost areas. The benefits of the FHA program should belong equally to all taxpayers; especially those residing in high-cost areas that often are most in need of affordable mortgage financing options.

For example, in California, twenty-nine of the fifty-eight counties are currently at the FHA ceiling of $362,790, with another six counties approaching the ceiling when one factors in the latest escalation in home prices. These twenty-nine counties represent approximately eighty-five percent of California's population, many of whom are struggling to become or remain homeowners in an area where the median house price is currently $535,470. California is not alone. High-cost areas exist in many states across the country. Maryland, for example, has five of twenty-four counties currently at the $362,790 FHA maximum with another seven counties within $1,885 of the limit. Again, these counties represent a great majority of the population for Maryland. Additional states that currently feature counties at or approaching the maximum FHA loan limit include Pennsylvania, Connecticut, New York, and New Jersey among others.

Recognizing high-cost areas with regard to FHA loan limits is not new to this legislative body. Congress already recognizes high-cost areas for FHA loan limits in Hawaii, Alaska and various United States Territories. These areas feature an exception that takes their available loan limit to one hundred and fifty percent of the current FHA loan limit.

We must not forget that the FHA program was created by the National Housing Act of 1934 with the intent of increasing homeownership and assisting the home building industry. Since its inception, FHA has insured over 33 million loans and is the largest insurer of mortgages in the world. FHA insured loans are the staple for first-time homebuyers. FHA insured loans are more accommodating to first-time homebuyers than other types of loan programs. The program is designed to incorporate flexibility for debt-ratios, income and credit history items not included in the government sponsored enterprise (*i.e.,* Fannie Mae and Freddie Mac) guidelines.

Congress must ensure that FHA insured loan programs continue to serve as a permanent backstop for all first-time homebuyer programs. For this reason, we believe that Congress should create the ability for FHA loan limits to be adjusted up to 100% of the median home price, thereby providing a logical loan limit that will benefit both the housing industry and the consumer. Tying the FHA loan limit to the median home price for an individual county, and letting it float with the housing market, allows the FHA loan limits to respond to changes in home prices instead of some esoteric number computed through a complicated formula. In this fashion, the FHA loan limit will reflect a true home market economy. Rather than restrict purchases of new homes through a legislatively mandated ceiling, the FHA loan limit can automatically adjust under current guidelines established for increasing the FHA loan limit on a county-by-county basis.

Conclusion

NAMB appreciates the opportunity to offer our views on transforming the FHA program for the 21st century. I am happy to answer any questions.

Written Statement

of the

NATIONAL ASSOCIATION OF REALTORS®

submitted to the

House Financial Services Committee
Subcommittee on Housing and Community Opportunity

On

"Transforming the Federal Housing Administration for the 21st Century"
April 5, 2006

Written Statement
of the
NATIONAL ASSOCIATION OF REALTORS®
submitted to the
House Financial Services Committee
Subcommittee on Housing and Community Opportunity
On
"Transforming the Federal Housing Administration for the 21st Century."
April 5, 2006

The NATIONAL ASSOCIATION OF REALTORS® represents a wide variety of housing industry professionals committed to the development and preservation of the nation's housing stock and making it available to the widest range of potential homebuyers. The Association has a long tradition of support for innovative and effective Federal housing programs and we work diligently with the Subcommittee and the Congress to fashion housing policies that ensure Federal housing programs meet their mission responsibly and efficiently.

While the homeownership rate continues to rise, there are still many hard-working families that simply cannot qualify for a conventional mortgage. Minority homeownership rates are significantly lower than the national average—around 50%, compared with nearly 70% for the nation as a whole. The homeownership rate for African American households the first quarter of 2005 was 48.8 percent, while Hispanic households were at 49.7 percent. The homeownership rate for Asian, Native Americans, and Pacific Islanders was 59.4 percent. By comparison, 76.0 percent of non-Hispanic whites were homeowners.

FHA's single-family mortgage insurance program is a valuable government program that has proved highly beneficial in helping low-, moderate-, and middle-income people achieve the dream of homeownership. FHA insurance is available to individuals regardless of their racial, ethnic or social characteristics and its universal availability helps stabilize housing markets when private mortgage insurance is nonexistent or regional economies encounter disruptions. We believe that the FHA program can be empowered with tools to close the minority homeownership gap and keep homebuyers from risky loan products currently being provided by the conventional and sub-prime markets.

It is important to note that FHA is NOT a lender. The argument that FHA will take the market away from lenders is simply false. FHA simply insures safe and fairly-priced mortgages that are made by private lenders. It has also been argued that FHA is a subsidy that the federal government need not provide. FHA is fully self-supporting. The FHA fund is fully paid with insurance premiums paid by borrowers. There is no cost to the taxpayer; in fact FHA generates revenue for the U.S. Treasury.

A growing number of homebuyers are deciding to use one of several new types of specialty mortgages that let them "stretch" their income so they can qualify for a larger loan. Specialty mortgages often begin with a low introductory interest rate or payment plan—a "teaser"—but the monthly mortgage payments are likely to increase significantly in the future. Some are "low documentation" mortgages that provide easier standards for qualifying, but also feature higher interest rates or higher fees. Some lenders will finance 100% or more of the home's value, but these mortgages also present a big financial risk if the value of the house decreases. Mortgages such as interest-only, negative amortization, and options ARMs

can often be risky propositions to borrowers. These pose severe risk burdens to consumers who may be unable to afford the mortgage payment in the future because monthly payments may increase by as much as 50% or more when the introductory period ends, or cause their loan balance (the amount you still owe) to get larger each month instead of smaller.

For many of these potential homebuyers, FHA can play a major role in meeting their homeownership aspirations without adverse consequences. FHA typically serves borrowers who have lower annual incomes, make smaller down payments, and purchase less expensive homes. However, FHA's market share has been dropping in recent years. In the 1990s FHA loans were about 12% of the market. Today, that rate is closer to 3%. As the market has changed, FHA must also change to reflect consumer needs and demands. Conventional and sub-prime lenders have been expanding their products and offering more types of loans to more types of borrowers. However, not all of these loans are in the best interest of the borrower. If FHA is enhanced to conform with today's mortgage environment, many borrowers would have available to them a viable alternative to the riskier products that are marketed to them.

In today's market, interest rates are low, home prices are rising, and lenders have expanded their pool of tools to offer borrowers. But will these options still be available during periods of economic uncertainty? FHA has been there for borrowers. When the housing market was in turmoil during the 1980s, FHA continued to insure loans. Following Hurricanes Katrina and Rita, FHA has continued to provide a foreclosure moratorium for borrowers who are unable to pay their mortgages while they recover from the disaster. The universal and consistent availability of FHA is the principal hallmark of the program that has made mortgage insurance available to individuals regardless of their racial, ethnic, or social characteristics during periods of economic prosperity and economic depression. FHA is the only national mortgage insurance program that provides financing to all markets at all times.

To enhance its viability in mortgage markets, the Administration is proposing a number of important reforms to the FHA single-family insurance program that will greatly benefit homebuyers nationwide. FHA is proposing to eliminate the statutory 3 percent minimum cash investment and downpayment calculation, allow for extended loan terms from 30 to 40 years, and increase the loan limits from 87 percent to 100 percent of the conforming loan limit in high cost areas and increase the floor from the current 48 percent to 65 percent of the conforming loan limit across the country.

The ability to afford the downpayment and settlement costs associated with buying a home remains the most challenging hurdle for many homebuyers. Eliminating the statutory 3-percent minimum downpayment will provide FHA flexibility to offer varying downpayment terms to different borrowers. Although housing remains strong in our nation's economy and has helped to increase our nation's homeownership rate to a record 69 percent, many deserving American families continue to face obstacles in their quest for the American dream of owning a home. Providing flexible downpayment products for FHA will go a long way to addressing this problem.

The term of a mortgage insured under the FHA single-family mortgage insurance program has traditionally been 30 years. Increasing the term would reduce the monthly mortgage payment, enable more households to qualify for a mortgage, and increase homeownership. Research conducted by the NATIONAL ASSOCIATION OF REALTORS® (NAR) shows that approximately 41 percent of American households could qualify to purchase the U.S. median priced home of $208,300 with a 30-year mortgage. This amounts to approximately 45.1 million households. Extending the term to 35 years would permit 2.1

million more families to buy a home with an FHA mortgage. Extending the term to 40 years would permit 3.6 million more families to buy a home with an FHA mortgage than they can today.

FHA mortgages are used most often by first-time homebuyers, minority buyers, low- and moderate-income buyers, and other buyers who cannot qualify for conventional mortgages because they are unable to meet the lender's stringent underwriting standards. Despite its successes as a homeownership tool, FHA is not a useful product in high cost areas of the country because its maximum mortgage limits have lagged far behind the median home price in many communities. As a result, working families such as teachers, police officers and firefighters are unable to buy a home in the communities where they work. Prospective homebuyers in high cost states should not be left behind just because of their geographic location. Increasing FHA loan limits in high cost areas will address these problems.

Under the Administration's proposal, FHA's limits for single unit homes in high cost areas would increase from $362,790 to the 2006 conforming loan limit of $417,000. Research conducted by the National Association of REALTORS® indicates that this will result in 28% more FHA originations in California and 19% more originations in Massachusetts. In non-high cost areas, the FHA limit (floor) would increase from $200,160 to $271,050 for single unit homes. The high cost increase would bring FHA loans on par with loan guarantees provided by the Department of Veterans Affairs. In 2004 President Bush signed legislation authorized by Congress to increase the Veteran's loan guarantee to 25% of the conforming loan limit. This means veterans can purchase homes using the VA loan product for up to $417,000, the current conforming loan limit.

Increasing the FHA loan limits will stimulate homebuying opportunities in all segments of the country and provide an important benefit to thousands of average income families seeking to purchase modest homes throughout all regions of the country. Increasing the high-cost maximum mortgage limit constitutes basic regional equity allowing qualified moderate-income homebuyers in high cost areas to share the benefits of FHA homeownership that FHA users in other regions of the country now enjoy. Increasing the base loan limit will enhance FHA's ability to assist homebuyers in areas not defined as high-cost, but where home prices still exceed the current maximum of $200,160. This includes states like Arizona, Colorado, Florida, Georgia, Illinois, Maine, Minnesota, Nevada, North Carolina, Ohio, Oregon, Pennsylvania, Utah, Vermont, and Washington. None of these states is generally considered "high cost" but all have median home prices higher than the current FHA loan limit.

The Administration also proposes to combine all single-family programs into the Mutual Mortgage Insurance Fund. The FHA program has four funds with which it insures its mortgages. The Mutual Mortgage Insurance (MMI) Fund is the principal funding account that insures traditional 203b single-family mortgages. The fund receives upfront and annual premiums collected from borrowers, as well as net proceeds from the sale of foreclosed homes. It is self-sufficient and has not required taxpayer bailouts.

For accounting purposes, the MMI fund is linked with the Cooperative Management Housing Insurance Fund (CMHI). The CMHI finances the Cooperative Housing Insurance program (Section 213), which provides mortgage insurance for cooperative housing projects of more than five units that are occupied by members of a cooperative housing corporation. FHA also operates Special Risk Insurance (SRI) and General Insurance (GI) Funds, insuring loans used for the development, construction, rehabilitation, purchase, and refinancing of multifamily housing and healthcare facilities, as well as loans for disaster victims, cooperatives and seniors housing.

Currently, the FHA condominium loan guarantee program and 203k purchase/rehabilitation loan guarantee program are operated under the GI/SRI Fund. NAR strongly supports inclusion of these programs in the MMIF. In recent years programs operating under the GI/SRI funds have experienced disruptions and suspensions due to funding commitment limitations. Because the multifamily housing programs are under the GI/SRI funds and thus susceptible to future funding expirations, maintaining the single family programs under the GI/SRI funds would expose these programs to possible future disruptions. Thus, from an accounting standpoint, it makes sound business sense to place all the single-family programs under the MMIF.

Besides combing the 203(k) and condominium programs under the MMIF, NAR also recommends key enhancements to increase the programs' appeal and viability. Specifically, NAR recommends restoring investor participation in the 203(k) program. We also recommend that HUD lift the current owner-occupied requirement of 51 percent before individual condominium units can qualify for FHA-insured mortgages. The policy is too restrictive because it limits sales and homeownership opportunities, particularly in market areas comprised of significant condominium developments and first-time homebuyers. In addition, the inspection requirements on condominiums are burdensome. HUD has indicated that it would provide more flexibility to the condo program under the MMIF. We strongly support loosening restrictions on FHA condo sales and 203k loans to provide more housing opportunities to homebuyers nationwide.

The NATIONAL ASSOCIATION OF REALTORS® recognizes that homeownership is a primary goal of American families. Housing has always been and continues to be one of the highest personal and social priorities in America with study after study affirming that a large proportion of Americans would rather own than rent a home. Homeownership directly benefits society by fostering pride and participation in one's community, encouraging savings and promoting social and political stability. Homeownership has been emulated on television, romanticized in literature, and coveted in the popular social consciousness. It is advocated by private enterprise and encouraged by government policy. Clearly, it is the proud achievement of most American families, the ultimate assimilation for generations of immigrants to this country, and the pinnacle for Americans generally as they climb the ladder of economic success.

The NATIONAL ASSOCIATION OF REALTORS® applauds the private sector for the recent development of innovative and affordable housing products that are providing housing opportunities for many deserving families. However, not all needs are being met, and some homeowners may not be in a loan that is appropriate for them. Consequently, the NATIONAL ASSOCIATION OF REALTORS® steadfastly maintains that government mortgage programs in general and the Federal Housing Administration in particular represent the most important source of homeownership for many American families. FHA provides a homeownership tool that provides security and stability to homeowners. We urge you to seriously consider these reforms to the FHA single-family home loan guarantee program to ensure all homeowners are afforded the true dream of homeownership.

Testimony of

Peter H. Bell, President
National Reverse Mortgage Lenders Association

Submitted to
The Subcommittee on Housing and Community Opportunity of the
Committee on Financial Services
U.S. House of Representatives

April 5, 2006

National Reverse Mortgage Lenders Association (NRMLA) is pleased to submit testimony in support of the U.S. Department of Housing and Urban Development's (HUD) proposed legislation to streamline and improve FHA single-family loan programs, including the Home Equity Conversion Mortgage (HECM) program. NRMLA commends HUD for its leadership and recognition of the importance of the reverse mortgage program. We salute the Department's willingness to make innovative improvements to make the HECM program more beneficial to seniors nationwide.

NRMLA is the principal nationwide non-profit trade association for banks and financial services companies that originate, service and invest in reverse mortgages. The association fulfills several roles: educating consumers about the opportunity to utilize reverse mortgages, training lenders to be sensitive to the needs of older Americans, and developing Best Practices and a Code of Conduct to make sure lenders offering reverse mortgages treat seniors respectfully.

As you know, reverse mortgages enable senior homeowners 62 or older to convert part of the equity in their homes into tax-free cash without having to sell, move, give up title, or take on new monthly mortgage payments. Borrowers are never, under any circumstances, forced to leave their homes providing they make their real estate property tax and insurance payments. Borrowers can choose to receive reverse mortgage funds as a lump sum, fixed monthly payments (for up to life), line of credit, or as a combination of monthly income and line of credit. No mortgage payments are due during the life of the loan. Borrowers can use the funds anyway they wish. The loan is repaid when the last surviving borrower (in the case of a couple) sells the home or permanently moves out.

The most widely used reverse mortgage, accounting for an estimated 90 percent of the marketplace, is the FHA-insured Home Equity Conversion Mortgage, or "HECM." Since its adoption in 1990, FHA has insured just under 200,000 HECMs. Nationwide, in 2005, some 43,000 seniors obtained a HECM to pay off existing debts, fund health care expenses, pay for modifications to make their homes safer and more comfortable, or simply to create an income stream that provides additional cash and peace of mind.

HUD's proposed reform package would make the following improvements: eliminate the cap on the number of HECM loans that HUD can insure; create a single national loan limit for the HECM program; and implement a HECM for Home Purchase option.

Eliminating HECM Cap
In response to rapid growth in the reverse mortgage program, a key legislative priority for NRMLA in 2006 is focused on removing the cap on the number of reverse mortgages that HUD can insure. Without legislation, the Department can only insure 250,000 HECM loans—a cap that our industry could approach within a year as volume continues to steadily increase.

When Congress first authorized the HECM program in 1987, it was created as a demonstration program and the number of loans that could be made was limited. The idea back then was to gain some experience with the program and observe how it performed. In 1998, Congress adopted legislation making the program permanent, but set a cap of 150,000 HECM loans that could be outstanding. Early last year, production of HECM loans began to bump up against that cap and HUD took steps to shut down new loan origination activity. To avoid this, just in the nick of time, Congress increased the HECM authorization cap to 250,000 loans in a supplemental appropriations bill that was about to be enacted.

That emergency supplemental appropriation enabled the HECM program to continue without interruption, but demonstrated the need to eliminate the cap. Had there not been an appropriate legislative vehicle moving forward at precisely that time, seniors would have been shut off from the opportunity to utilize FHA-insured reverse mortgages to tap the equity in their homes.

HUD's proposed FHA reform bill would permanently eliminate this uncertainty and create a market environment in which existing and new participants could bring down costs to consumers through product innovation and competition. A performance track record of the HECM program has now been clearly established. The program was initially designed with the intent of producing a "break even" cash flow. It has far surpassed that and yielded a significant surplus. It is time to remove the HECM loan volume cap so this important program can help more seniors live comfortable lives in their own homes.

Single National Loan Limit
NRMLA supports a single, nationwide loan limit for the HECM program.

FHA's other mortgage insurance programs were established by Congress for families that might not otherwise be able to obtain mortgages to purchase modest homes. Because housing costs vary considerably from market to market, Congress established loan limits for FHA programs that vary according to the median home price in each market.

However, the FHA HECM program was established by Congress to enable elderly homeowners to convert the wealth that they have amassed in their home equity into cash

to help pay for living expenses. These expenses, which can include health care and home maintenance, do not vary considerably from market to market, and have little if any relationship to the median home price of the area. The disparities in the current FHA loan limits mean that senior homeowners living in areas with low FHA loan limits cannot access as much of their equity as seniors with comparably valued homes living in areas with higher FHA limits, regardless of their relative need for the funds. This unfairly penalizes senior homeowners in low-cost areas.

HECM for Home Purchase Option

Although the reverse mortgage was originally conceived as a financial tool to help seniors stay in their current homes, it is evident that some homeowners may want to use reverse mortgages to purchase new homes that are better suited to their current needs or closer to their families. Newer homes might be preferred because they require less maintenance or have a single-story design, making it easier to "navigate" the home. The reverse mortgage should be recognized as a tool to help individuals buy homes that better serve their needs without having to exhaust cash reserves or take on new monthly mortgage payments.

NRMLA strongly believes that the use of HECM loans for the purchase of new homes is consistent with the intent of the program to help seniors live comfortably in homes of their own. We urge Congress to provide HUD with the authorization to insure loans used for this purpose.

Conclusion

A healthy, active HECM program could be a key component for helping seniors take control over their financial situation. Reverse mortgages are a promising way to unlock billions of dollars in home equity, providing financial security, independence, and great improvement in the quality of life for thousands of senior homeowners and their families. Wider acceptance of reverse mortgages can mean reducing the need for costly increases in federal spending on health care and other benefits for seniors in the future.

The FHA Home Equity Conversion Mortgage is the primary source of reverse mortgages. Congress should enact HUD's proposals to make needed changes that will result in more senior homeowners enjoying the benefits of this outstanding program.

NRMLA and all of our member lenders stand ready to assist Congress and HUD in this vitally important effort.

Respectfully Submitted,
Peter H. Bell, President
National Reverse Mortgage Lenders Association
Washington, DC

April 4, 2006

The Honorable Bob Ney
Chair
Subcommittee on Housing and Community Opportunity
House Financial Services Committee
U.S. House of Representatives
Washington, DC 20515

Dear Chairman Ney:

As the Subcommittee considers legislation to modernize and update the National Housing Act and enable the Federal Housing Administration (FHA) to use risk-based pricing to more effectively reach underserved borrowers, we respectfully urge you to consider the impact of these types of programs in light of the high foreclosure rate. The government's desire to reach underserved borrowers is a potentially laudable goal, but the high-risk program that the U.S. Department of Housing and Urban Development (HUD) proposes will potentially adversely affect the Mutual Mortgage Insurance Fund (MMIF) and, because it allows credit subsidy, may raise costs for all FHA borrowers.

The way HUD has structured this latest proposal clearly suggests that the Department has its own concerns with high-risk, no-downpayment loans. HUD says the program will not require government credit subsidy because the mortgages will be priced based on the risk factors associated with the loan and the borrower's characteristics. However, HUD also asks for the authority to allow the FHA insurance program to permit the use of cross-product credit subsidy, indicating that some credit subsidy will likely be required. This proposed legislation not only puts the risk squarely on FHA by allowing credit subsidy, it is also likely to cost all FHA borrowers more in the form of higher insurance premiums and costs.

HUD also proposes to expand the amortization period from 35 to 40 years. On the face of it, it appears that this change may help more families get into homeownership, but in actuality, it will further erode the borrower's equity investment. This will negatively impact the partnership that homeownership requires between the lender and the borrower.

Even more disturbing is the impact the bill would have on foreclosure rates. Foreclosures of all loans jumped 68 percent from February 2005 to February 2006[1]. FHA foreclosure trends are even worse. At the end of 2004, FHA foreclosures were at their highest level ever, more than double the average for the past 21 years. After two quarters of improvement, the FHA foreclosure rate is rising again and is now at a level higher than at any time prior to 2003.[2] In the fourth quarter of 2005, FHA mortgages that were seriously delinquent (three or more months overdue) were at record levels, suggesting that foreclosures may continue to rise in the near-term.[3] If foreclosures are this high under a program that requires a three percent downpayment, it is not hard to imagine the situation becoming even worse if Congress allows the FHA to reduce the downpayment even lower.

Zero-downpayment mortgages failed miserably in the 1980s when tens of thousands of home buyers had no recourse but to abandon their house and mail the keys back to their lender. Despite

[1] RealtyTrac press release at: www.realtytrac.com/news/press/pressRelease.asp?PressReleaseID=93.
[2] Analysis by the National Multi Housing Council of quarterly National Delinquency Surveys conducted by the Mortgage Bankers Association.
[3] Ibid.

this experience and the great strain it put on the nation's banking industry here we are once again considering the merits of zero-downpayment loans.

We are not here to argue against homeownership. The pursuit of homeownership is a worthy goal, but the time has come to ask whether a "homeownership above all else and at any cost" policy is wise. There is a dangerous disconnect between our nation's housing policy and our nation's housing needs. Local mayors and congressional commissions agree that our top housing priority should be creating more rental housing, yet every year more of our limited resources are diverted to subsidizing homeownership. We simply cannot solve all of our nation's housing problems on the back of homeownership alone. What the nation truly needs is a more balanced housing policy.

The government must also be careful not to oversell homeownership. Creating more homeownership opportunities for minorities is a worthy goal, but unsustainable homeownership is not in anyone's interest. Many families never question whether buying a house is a path to financial security. They just assume it is, especially when the federal government tells them they should buy a house. But for too many households, the joys of homeownership have turned into an agony of onerous and unsustainable debt that harms their financial future.

We do hard-working families a grave disservice when we encourage them to buy homes that they are not likely to be able to maintain or keep. The low- and moderate-income families targeted by this initiative are more likely to buy older houses that are more expensive to maintain and are located in struggling neighborhoods where price appreciation can be elusive. With no equity and little cash reserves, these households are one paycheck away from financial disaster. Even worse, homeownership can trap highly leveraged families in distressed neighborhoods.

Putting families into houses they cannot sustain has a ripple effect. If the new homeowner cannot maintain the house, nearby property values will decline. If families default and abandon their houses, cities, counties, towns and school districts also lose tax revenue. One researcher estimated that cities spend, on average, $27,000 per FHA foreclosure.

We need a more balanced housing policy. Local governments have made the connection between job growth, economic growth and rental housing. They know that towns without sufficient rental housing forego valuable consumer spending and discourage businesses from expanding or relocating there because they cannot house prospective workers.

The tagline for America may be that we are a nation of homeowners, but actually 33 percent of our citizens are renters, and 40 percent of them rent by choice[4]. As American lifestyles have gotten busier, young professionals and empty nesters who could afford to buy are choosing to rent instead. In fact, households making $50,000 or more make up 23 percent of all apartment renters[5]

Rental housing may not be as strong a political message as homeownership, but the simple fact is that this nation needs apartments. We need them for the 73 million Echo Boomers and the 13 million immigrants expected to flood into the housing market in the next decade. We need them for the millions of hard-working families who cannot find affordable housing near their jobs.

We need them for every town that wants to accommodate population growth without giving up all its

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[4] Fannie Mae Foundation. 2002 Annual Housing Survey.
[5] NMHC tabulation of 2005 Current Population Survey Annual Social and Economics Supplement, US Census Bureau.

green space and adding to pollution and traffic. And we need them for every city that wants to reclaim a decaying downtown neighborhood. The biggest housing success story of the last 10 years is the downtown revivals taking place from Philadelphia to San Jose. These stories owe their success not to new homeownership initiatives, but to apartment developers who took a chance and created new housing downtown.

The nation's experience with the 2005 Gulf Coast hurricanes serves as the latest and most dramatic evidence to date of why the nation needs to more explicitly value its rental housing industry. When the nation needed to find housing for hundreds of thousands of evacuees, it turned to the apartment sector. The industry's response was immediate, creative and generous. As a result, victims across the country are now starting to rebuild their lives in apartments. Without a vibrant rental housing stock, such a massive relocation effort would never have been possible.

Promoting homeownership is a worthy goal, but our homeownership programs should be structured to "first, do no harm." HUD's newest proposal does not meet that standard. We have real housing problems we need to solve, and we can only do that through a more balanced housing policy that does not view homeownership as a panacea to all that ails struggling Americans.

Sincerely,

Doug Bibby
President
National Multi Housing Council

Douglas S. Culkin, CAE
President
National Apartment Association

Ray Carlisle,
President

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April 4, 2006

Honorable Robert Ney
Chair, Sub-Committee
Housing and Community Opportunity
of the House Committee on Financial Services
2129 Rayburn HOB
Washington, D. C. 20515

Honorable Maxine Waters
Ranking Member, Sub-Committee
Housing and Community Opportunity
of the House Committee on Financial
Services
2129 Rayburn HOB
Washington, D. C. 20515

Re: NID Support of FHA Modernization Proposal

Dear Mr. Chair and Madam Ranking Member:

The National Association of Real Estate Brokers, Investment Division (NID) is the largest and oldest urban based network of African American real estate professionals focused on urban community development in America. NID is a public benefit corporation and an independent affiliate of the National Association of Real Estate Brokers (NAREB), the largest and oldest African American real estate trade association in America.

Over the past 25 years NID has spearheaded numerous efforts to improve home mortgage delivery services to urban areas, minority populations and other protected classes under the laws, regulations, executive orders and special programs of both the government and private sectors. Fair treatment, quality services and equal opportunity in the marketplace remains a severe challenge in both sectors. The government sector (FHA) has been too restrictive and cumbersome. The private sector has been more geared toward corporate profit than service to underserved communities and households, for a number of justifiable (unfair competition by government with the private sector) and unjustifiable (predatory and/or discriminatory practices) reasons that have been reported on over the years.

The time has come for the proposed FHA Modernization Act of 2006 (the Act) to assist both the government and private mortgage lending sectors to provide products and services, in a fair, cost effective and financially sound manner to all home mortgage product consumers, particularly urban and minority populations. The Act will improve competition, lower overall cost to borrowers, expand fair mortgage lending opportunities and increase the homeownership rates of African American and Hispanic Origin homebuyers in traditionally underserved urban and rural areas.

The proposed FHA mortgage insurance premium structure will foster fair and transparent "risk-based pricing" policies for high, low and even loan to value ratio mortgage loan products and reduce the bait and switch tactics that permeate the home mortgage market today in urban and rural areas and for minority and immigrant households in all areas of the country, including "high cost areas".

The Act will implement improved, transparent, time sensitive and accountable home mortgage insurance program management policies. Policies which are primed to assist FHA in spearheading the expansion of homeownership and mortgage borrowing opportunities to households and areas that remain traditionally underserved by the conventional home mortgage market through increased market competition. The Act requires improved oversight by Congress which will also provide the Congress with valuable market information as it considers policy improvement and accountability of the both the government and conventional home mortgage marketplace.

The innovative HECM and Manufactured Housing mortgage insurance proposals further expands affordable homeownership opportunities to lower-income households in all areas of the country.

There has already been several product and policy improvements implemented pertaining to FHA during the past four years. The proposed Act will properly and effectively enhance the progress already made to bring FHA, and its traditional client base into the mainstream. This will support building better communities and creating family stability and wealth in America, through fair and decent homeownership opportunities.

NID will continue to follow the development of this extremely important and timely legislation and urge the vigorous support to immediately update the National Housing Act with the FHA Modernization Act of 2006 of the full Subcommittee on Housing and Community Opportunity.

Thank you,

Ray Carlisle
President, NID

Written Statement of the

Manufactured Housing Institute

and the

Manufactured Housing Association
for Regulatory Reform

Hearing on
Transforming the Federal Housing Administration for
the 21st Century

Before the

Housing and Community Opportunity Subcommittee
of the Financial Services Committee
U.S. House of Representatives

April 5, 2006

Introduction

The Manufactured Housing Institute (MHI) and the Manufactured Housing Association for Regulatory Reform (MHARR) jointly submit this written statement relating to the April 5, 2006 subcommittee hearing on "Transforming the Federal Housing Administration for the 21st Century". We respectfully request that this written statement be made part of the official hearing record.

MHI and MHARR strongly support H.R. 4804, the "FHA Manufactured Housing Loan Modernization Act of 2006." This bill was introduced by Subcommittee Member Pat Tiberi and Full Committee Ranking Member Barney Frank. H.R. 4804 represents a bi-partisan effort to reform an important affordable housing program. The FHA Title I mortgage insurance program insures loans made by private lenders to finance the purchase of manufactured homes that will be placed primarily in land-lease communities or private land. This program is targeted to benefit lower income homebuyers to find adequate affordable housing who are particularly challenged with escalating construction material prices.

Background

The manufactured housing industry has gone from 376,000 building starts in 1998 to approximately 145,000 in 2005. This represents a sixty percent (60%) decline in housing shipments and sales. The primary cause for this market contraction has been the loss of available financing for potential homeowners who apply for a manufactured housing loan. As a result, the industry has not been able to serve the housing needs of individuals and families of low-to moderate-income who want to purchase a home without the encumbrance of land or real estate.

In the past, when credit availability became curtailed, the FHA Title I program provided much needed liquidity. In recent years, however, FHA Title I has not functioned as an "automatic stabilizer" in the marketplace. During the early 90's, Title I insured over 30,000 loans per year. In each of the past three years, FHA Title I insured less than 10% of that amount, or less than 2,000 manufactured home loans per year. While Fannie and Freddie are permitted under their charters to purchase and to create a secondary market for "home-only" loans, both GSEs have not done so to date. The sole secondary market participant for Title I loans is the Government National Mortgage Association (Ginnie Mae). As described below, Ginnie Mae's participation in this market has been extremely limited in recent years.

Ginnie Mae, which facilitates the securitization of FHA loans, attributes the decline of Title I activity to certain "structural problems" which make it very difficult for it to recoup its losses when lenders go out of business. This does not happen with FHA Title II (real property) loans because under that program, insurance is set on a loan-by loan basis. Ginnie Mae officials have stated that if these structural problems (especially the insurance issue) can be addressed as submitted within, they would end the moratorium on certifying new lenders and

would help facilitate the securitization of more Title I loans. This would add much needed liquidity to the program.

Current System

The existing loan limits are set by statute and have not been increased since 1992. Ninety-five percent of the loans insured under Title I are "home only" transactions. Such loans are also commonly referred to as personal property or chattel loans.

The current loan limit set by Congress in 1992 for "home only" loans is $48,600. This amount is woefully inadequate to meet the average loan needed to purchase a manufactured home and it remains one of the primary reasons for the recent inactivity in the Title I program. The current loan threshold would limit home buyers to a single-section manufactured home which, on average, would be less than 1,000 square feet in living space and lack many of today's aesthetic improvements to manufactured housing. Such cramped living quarters are hardly conducive to family living.

One of the bill's purposes is to move the current weak and inefficient Title I insurance system for manufactured housing toward the stronger and more mainstream Title II insurance system. One of the weaknesses of the current system is that the underwriting standards are very vague and leave too much discretion to individual lenders. FHA does not review lender underwriting today--the insurance is automatic with few financial safeguards. The insurance premiums are also too low which further exacerbates the fiscal soundness of this program.

Another weakness is that, unlike Title II where every loan is fully insured, under Title I FHA maintains a separate account for each lender for future claims equal to 10% of the principle balance of all Title I loans that lender originates. For example, if a lender originates $1 million in Title I manufactured home loans, only $100,000 is insured by FHA — the remaining $900,000 in not covered. Once that account becomes depleted due to foreclosures and insurance payouts, there is no insurance coverage remaining to pay future claims for loans that particular lender had originated. If additional loans end up in foreclosure and if the lender has inadequate loan reserves, Ginnie Mae (which guarantees the timely payment of principal and interest to investors) must compensate investors for principle and interest payments owed to them. During the 1990s, this insurance system created large losses for Ginnie Mae and resulted in it refusing to issue certificates ("eagles") to all but three manufactured housing lenders.

Proposed System

The new system proposed under H.R. 4804 would require that each loan be insured separately, as with Title II today. The bill would also institute a new system of financial "belts and suspenders" whose purpose is to provide a negative credit subsidy for taxpayers, which the legislation mandates. Specifically, the bill would: require HUD to increase the upfront insurance premium and address underwriting standards; strengthen down payment requirements; increase lender capital requirements; and maintain the current requirement that lenders co-insure 10% of each insurance loss. The current lender "account system" would disappear and each loan would be insured by FHA, similar to the Title II program today.

Under H.R. 4804, each party to the transaction would be responsible and held accountable for loan performance: the borrower would be required, of course, to keep monthly payments current; HUD would be responsible for increasing insurance premiums and addressing underwriting standards as market conditions dictate; and the lender would be accountable for 10% of the losses on loan defaults.

The loan limits have not been increased since 1992. H.R. 4804 would remedy this by instituting a one-time loan limit increase of 40% pegged to the current limits. While this might sound like a large increase, in reality it is not when you take into account the fact that production costs for the construction of manufactured homes have increased by over 50% since 1992. The new loan limits would be indexed for inflation going forward under the same consumer price index (CPI) used for other FHA programs.

The sum total of these reforms would result in lower-income families across the country being able to utilize the Title I program to purchase larger homes. In addition, the new financial safeguards will allow FHA to insure every loan. This should increase Ginnie Mae participation with more lenders being certified to issue Ginnie Mae securities. More securitizations would open up the secondary market for these loans – hopefully adding much needed liquidity and resulting in lower interest rates and fees. The ultimate beneficiaries, of course, would be low- and moderate-income homebuyers who will be able to enjoy more living space at a lower cost of financing.

Independent Studies In Support of Reform

Over the course of the past four years, four independent housing studies have been performed which address manufactured housing – all of which support reform of the Title I program. Three of the reports focus exclusively on manufactured housing, and two reports focus entirely on FHA Title I. The relevant pages from these reports have been provided to the subcommittee

electronically as appendices to this written statement. The reports and relevant findings are summarized below.

The Millennial Housing Commission was a statutory bi-partisan commission established by Congress in 2000. The commission was charged with examining, analyzing and exploring affordable housing programs in the US and how they might be improved going forward. It submitted its report to this committee in May 2002, as well as to the Senate Banking, Housing and Urban Affairs Committee and to the House and Senate Appropriations Committees. The recommendations contained in this report have served as a blueprint for housing legislation considered by Congress in subsequent years.

The report specifically covers the credit crunch currently prevalent in the financing of manufactured homes on leased land. On page 81 of the report, the Commission highlights the problem and recommends that "FHA's Title I and II programs be promoted and loan limits be increased; and Ginnie Mae approve more lenders as issuers/servicers, or instruct current issuers to make and service loans for manufactured homes". H.R. 4804 embodies the recommendations made in the Millennial Housing Commission report.

Later in 2002, the Neighborhood Reinvestment Corporation in collaboration with the Joint Center for Housing Studies at Harvard University issued a report to the Ford Foundation. The report, dated September 2002, was entitled "Manufactured Housing as a Community-and Asset Building Strategy". One of the authors of this report is former FHA Commissioner William Apgar, Senior Scholar of the Joint Center for Housing. Mr. Apgar served as HUD's FHA Commissioner from 1997-2001 and has a unique perspective of the FHA Title I program as its former regulator.

The Ford Foundation report points out that unlike the beneficiaries of multifamily programs, owners of manufactured homes who do not own the land upon which the home sits do in fact build home equity and accumulate wealth. This is due to basic principle pay down in their monthly payments. These homeowners also benefit from homeownership tax breaks---mortgage interest deductions and property tax deductions—which are not available to renters. These factors are pointed out on page 9 of the report under the heading "Affordable Rental Housing".

Not surprisingly, the report mentions that land ownership is a key driver of home price appreciation. However, it goes on to say (top of page 9) that "the absence of land acquisition costs makes manufactured housing on leased land an affordable home ownership option to lower-income people." The report notes that increased privacy, greater access to land, and reduced financing costs make owning a manufactured home on leased land a reasonable alternative to multifamily housing for lower income families. Under the heading "Limited Sources of Mortgage Capital" found on page 14, the report states that "FHA and

HUD need to allocate more staff and resources to explore options for supporting this segment (i.e. FHA Title I) of home ownership". H.R. 4804 embodies the recommendations made in the Ford Foundation report.

In 2003, HUD began to explore reform of the Title I program. In an effort to research both the need and the methods to reform the program, it retained the services of an outside contractor, Frontline Systems Inc., to prepare a comprehensive program analysis. Frontline Systems submitted its report to HUD entitled "FHA Final Title I Business Process Improvement Report" in June 2003. This report found that the Title I program was in dire need of modernization and made several policy and operational recommendations to HUD including: raising the Title I loan limits; modifying current underwriting guidelines; changing the insurance structure to the Title II insurance model; and increasing lender participation. H.R. 4804 embodies these specific recommendations made in the Frontline Systems report.

As a follow-up to the Frontline Systems report, in 2004 HUD contracted for a second Title I study with another outside contractor, Information Engineering Services Inc ("IES"). This study was intended to drill down and build upon the Frontline Systems report by suggesting additional statutory, regulatory, and administrative (handbook) recommendations. IES submitted its report to HUD entitled "Title I Program Findings and Recommendations" in July 2005. Consistent with the findings of the earlier Frontline Systems report, the IES report made several recommendations for reform and modernization of the Title I program. These recommendations include: changing the existing insurance structure to mimic the Title II structure; raising the loan limits and tying future increases to CPI; modifying underwriting standards; and updating the perception of manufactured housing and understanding the role it plays in affordable housing. H.R. 4804 embodies specific recommendations suggested in the IES report.

All four reports outlined above not only make the case for Title I reform, but each report contained specific suggestions for improving this program. As pointed out, H.R. 4804 is not an original body of thought. Rather, it contains the suggestions of independent public policy experts, academics, former Members of Congress and federal housing regulators who have studied this program and have concluded it is in dire need of reform.

Conclusion

As members of this subcommittee are well aware, the homeownership affordability crisis in the United States has reached epic proportions in recent years. Land appreciation has driven homeownership beyond the reach of countless low- and moderate-income homebuyers across the country. While the FHA Title I program is largely immune from these problems due to the absence of land from typical transactions, it is subject to problems of a different sort. The

outdated insurance structure, inadequate financial controls, and artificially low loan limits have all conspired to atrophy this program.

Congress, working together with HUD and the manufactured housing industry must reform this much needed program now. Material prices for home building have increased more than 20% in the past five years while the loan limits have remained unchanged since 1992. Implementing the necessary reforms outlined above will give lower income homebuyers the opportunity to enjoy one of the most efficient forms of housing available today.

NeighborWorks®
PROGRAM

Manufactured Housing

Ford Foundation

An Examination of Manufactured Housing as a Community- and Asset-Building Strategy

Report to the **Ford Foundation**
by Neighborhood Reinvestment Corporation
In collaboration with the
Joint Center for Housing Studies of Harvard University

William Apgar, Joint Center for Housing Studies
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September 2002

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ABSTRACT OF FINDINGS

An increasing share of lower-income families, the same population targeted by community-development organizations, are opting to live in housing that was built off-site in a factory to meet the performance standards of the national HUD manufactured-housing code. However, most community-development practitioners are just beginning to come to terms with the implications of manufactured housing for their work.

This paper explores advantages and disadvantages of manufactured housing for those entities whose mission is community development and asset building. Several challenges are presented for practitioners: First, working to educate consumers while also creating financing processes that ensure manufactured-home buyers obtain credit on the best terms for which they can qualify. Second, using the increased scrutiny under the Manufactured Housing Improvement Act of 2000 to advocate for states to enforce more rigorous installation standards and increased accountability. Third, working to overcome land-use controls which prevent manufactured homes from being placed in communities in need of affordable housing, as well as areas with more potential for appreciation. Fourth, working with designers and planners to develop innovative designs and housing developments, while maintaining manufactured housing's affordability advantages. Finally, equal effort must be devoted to address the difficult conditions of many lower-income people—owners and renters alike—living in older, and often deteriorating, mobile homes. While a few of these families and individuals could be relocated to new and better quality homes with the help of subsidies, resource limitations suggest the need to create cost-effective methods to eliminate health and safety problems by upgrading or rehabilitating this extremely affordable element of the nation's housing inventory.

As a companion to this paper, an exhaustive literature review has been compiled.

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INTRODUCTION

There are over eight million manufactured, HUD-code homes in the United States today, representing two-thirds of affordable units added to the stock in recent years and a growing portion of all new housing. In fact, buyers of manufactured homes contributed to a substantial share of the growth in low-income home ownership evidenced in the 1990s. These statistics send a message to all who seek to promote home ownership for low-income families, as well as promote safe, affordable housing opportunities in disenfranchised communities. An increasing share of the people whom community-development organizations serve are opting to live in housing that was built off-site in a factory to meet the performance standards of the national HUD manufactured-housing code. Many community-development practitioners are just beginning to come to terms with the implications of this for their work.

This report and the "Developing Community Assets with Manufactured Housing: Barriers and Opportunities" symposium held in Atlanta in February 2002 by the Neighborhood Reinvestment Corporation are part of an effort to better understand the implications and opportunities of manufactured housing for the community-development field. The goal of this project is to increase education and awareness about manufactured housing among practitioners. Similar to other markets, community-based organizations have the potential to help ensure that consumers make informed choices regarding manufactured housing, and to use programmatic and policy tools to make a positive impact on communities.

To supplement the quantitative findings of research conducted by staff of the Joint Center for Housing Studies of Harvard University, anecdotal information was collected from the national NeighborWorks® network of nonprofit community-development organizations, and model program profiles were developed to provide a more complete picture of the opportunities and challenges of manufactured housing. In addition, focus groups with community-development practitioners, lenders, manufactured-housing retailers, homebuyer-education specialists and actual clients and consumers were convened to assess perceptions, knowledge and experience with manufactured housing. Guiding this research were questions related to the community-development field, namely, what—if anything—should community-development entities be doing about manufactured housing? How can this field begin to discern what improvements in public policy are needed and what programs might be successful?

This report provides a unique overview of manufactured housing, including a thorough analysis of historic trends, household demographics and the characteristics of manufactured stock, as well case studies that highlight innovative programs and developments. As a companion to this report, an exhaustive review of existing literature has also been summarized (beginning on page 49).

I. MANUFACTURED HOUSING CONTINUES TO EVOLVE

What is Manufactured Housing?

Manufactured housing began as an offshoot of the recreational-vehicle industry in the 1930s, providing shelter for households with mobile lifestyles as well as temporary housing needs. Following World War II, housing shortages induced many households to turn to mobile homes for permanent shelter. Recognizing an opportunity, during the 1950s the industry began designing and constructing units intended to be permanent shelters. This development engendered some quality improvements, but industrywide standards remained uneven.

Within a few decades, concerns over the quality, durability, health and safety of manufactured homes led to federal action. In 1974 Congress passed the Federal Manufactured Housing Construction and Safety Standards Act, which led to the creation of a national manufactured-housing code (the "HUD code"). Unlike site-built homes, modular housing and other types of factory-produced homes, which are built to a variety of state and local building codes, HUD-code manufactured homes are built to a single, national quality and safety standard. This standard is generally based on the performance of the design and materials, rather than prescribing a specific material type or dimension must be used. Therefore, HUD-code units may use engineered lumber or alternative materials not commonly permitted under local building codes.

Homes built to the HUD code are still built on a permanent chassis like mobile homes built prior to 1976, but HUD-code units are of a higher quality, safer, and more durable than earlier models. Importantly, the HUD code pre-empts state and local building regulations, allowing manufacturers to use standardized building materials and components and avoiding the delays associated with local building inspection procedures.

Because of these streamlined codes, reduced delays and other efficiencies, one of manufactured housing's most distinctive features is its affordability. These cost advantages do not stem from inherently inferior quality standards in the HUD code as compared to site-built homes. Detailed studies by the University of Michigan and others suggest that quality differences of the local site-built codes compared to the HUD code is minimal (Warner and Johnson 1993, Gordon and Rose 1998). In fact, manufactured housing's affordability stems largely from cost savings from production processes.

Five factors primarily drive these efficiencies:

1. economies of scale in high-volume materials purchase,
2. ability to better coordinate production using assembly-line techniques,
3. a controlled environment devoid of weather or other delays,
4. standardized design and materials, and
5. reduced costs (primarily time) of securing approval from local code officials.

Overall these advantages can generate significant cost savings, as indicated by a recent HUD study showing that building a 2,000-square-foot manufactured unit costs just 61 percent as much as a comparable site-built home (HUD 1998). Of course transportation and installation costs reduce HUD-code homes' construction cost advantages, but anecdotal reports from

Manufactured Home: Factory built to meet the performance standards or the HUD code, MUST have a chassis, rarely moves once placed.

Mobile Home: Typically refers to units built before 1976 and most similar to a trailer; occasionally used to refer to units built after 1976, despite the fact these units are technically (and legislatively) defines as manufactured homes.

Modular Home: Factory-built with some on-site assembly and some on-site construction, built to meet prescriptive standards of state and local codes. Chassis is optional.

Panelized Home: Factory-built panels are assembled on site and supplemented with on-site construction to meet prescriptive standards of state and local codes.

Trailer Home: Can be hitched to an automobile and moved, NOT built to a federal code. Also referred to as campers.

Source: Bradley, Donald S. 1997. "Will Manufactured Housing Become Home of First Choice?," *Freddie Mac 1997 Mortgage Market Trends*, pp. 29-33.

developers suggest manufactured units can deliver affordable housing for 20 to 30 percent less than comparable site-built units.

There are other forms of factory-built housing, such as modular and panelized construction, but these designs are not built to the national HUD code but rather to local codes, such as Uniform Statewide Building Code (USBC) or Building Officials Code Administrators (BOCA). These forms of factory-built housing also provide costs savings, but not at the scale of HUD-code units, because each must be tailored its site. Annually, fewer than 40,000 modular units are placed, compared to 250,000 or more manufactured units. Panelized, or precut construction is of a similar scale, but its use may be growing among larger builders (Ahluwalia 2001).

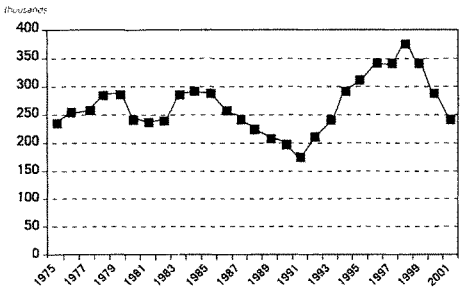
Manufactured Housing's Role in Housing Markets

Manufactured housing has had a role in boosting affordable home ownership opportunities. Between 1993 and 1999, manufactured housing accounted for more than one-sixth of the growth in owner-occupied housing stock. For particular submarkets the share is considerably higher. For example, among households with very-low incomes (that is, less than 50 percent of area median), 23 percent of home-ownership growth between 1993 and 1999 came through manufactured housing. For southern households the figure was 30 percent, and for rural households 35 percent. Indeed, in the rural South manufactured-home purchases accounted for a stunning 63 percent of the increase in very-low-income home ownership. Nationwide, manufactured homes are a major source of unsubsidized, low-cost housing for many owners and renters with few housing alternatives.

Over the past decade and a half, manufactured housing has emerged as an important affordable-housing option. Even amid rapid expansion of site-built housing, the number of owner-occupied manufactured units rose from 3.9 million in 1985 to 6.7 million in 1999, increasing its share more than a percentage point to 8 percent of the total owner-occupied inventory. Production has been highly cyclical, peaking in the late 1970s, mid-1980s, and again in the 1990s, with placements reaching an all-time high of 373,000 units in 1998. According to the Census Bureau's Construction Reports, during the 1990s manufactured housing accounted for between one-quarter and one-third of all production of single-family, detached homes.

By 2001, however, placements plummeted to 185,000 as demand for new units crashed (Figure 1). This falloff is related to the sharp industry correction that followed soaring placement levels in 1996 to 1998, which had been made possible by what now appears to be overly aggressive credit terms offered to marginally qualified buyers.

Figure 1: Annual Placements of Manufactured Homes



Source: U.S. Housing Markets, HUD 2002

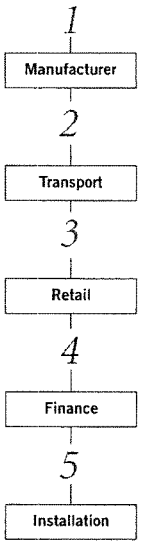
The Organization of the Manufactured-Housing Industry

The unique production and distribution channels for manufactured housing are responsible both for much of the cost savings that make the product a desirable option for lower-income borrowers, and for many of the quality problems that continue to plague the industry. Getting a manufactured unit from the factory floor to its final site involves firms that produce, sell, finance, deliver and install manufactured homes. During the 1990s, the manufactured-housing industry underwent significant change, as many smaller manufacturers were acquired or put out of business, and larger firms gained market share. Similarly, larger financial-services firms gained increasing shares of the market to provide mortgage capital to purchasers of manufactured

housing. The industry is integrating vertically as well, with many manufacturers acquiring retailers and, more recently, finance companies. Retailing remains a highly fragmented side of the industry, however, and as local financial institutions enter the manufactured-housing market, lending may counter overall concentration trends.

Manufacturing and Transport

Historically, producers of manufactured homes were small firms that specialized in producing recreation vehicles. They were followed by large recreation-vehicle and trailer manufacturers, again with limited homebuilding experience. Many firms eventually expanded their capacity to produce better quality manufactured homes, while other firms were acquired or driven out of business by competitors. Even so, the industry remained fragmented, with many relatively small producers, owing at least in part to the location of many smaller plants close to specific regional markets due to the difficulty and expense of transporting the final product. In the last decade, however, the industry consolidated. Of the 100 manufactured-home producers in 1990, only 70 remained by 2001. In 1998 the 25 largest producers shipped 92 percent of all units, while the 10 largest accounted for 78 percent (Nkonge 2000). This compares to the site-built industry, where the 50 largest builders controlled just 16 percent of the market in 1997 (Ahluwalia 1998).



Before leaving the factory, each unit is inspected by a HUD-certified independent inspector. If the unit passes inspection it receives a red and silver shield which is riveted to the exterior and certifies that the unit meets the standards of the HUD code. Of course, the distinguishing feature of manufactured housing is that it is required to have a chassis. A holdover from its mobile beginnings, the chassis—a supporting frame with removable axle and wheels—is mandated by the HUD code and used to transport the home from the factory to the site, and remains integral to the home throughout its useful life.

Many of the largest producers have manufacturing facilities in or near every state, in order to minimize distribution costs. Transportation is typically contracted to outside firms and is tightly restricted by state highway regulations for the maximum size, weight and even times and days units are allowed to be transported. State highway regulations and the need to transport a finished home under bridges, underpasses and power lines have, to a certain extent, determined the maximum allowable dimensions and design potential of manufactured homes.

Retail Sales and Finance

Once built, most units are shipped to dealers at retail sales centers, where they are displayed and sold to consumers. Consumers who plan to place their unit on owned land can buy them through retail centers, but often have their homes "built to order" based on a variety of customization options offered by the manufacturer. The ability to choose from a wide array of wall finishes, cabinet designs, appliances, and carpet and drapery colors is a significant selling point for many consumers. In some cases, developers and owners of manufactured-housing communities act as dealer representatives and handle sales in the communities directly.

Manufactured-home loans sometimes are more similar to auto financing than real estate financing. So-called chattel loans are secured only by the manufactured home, not by the land on which it is placed. Compared with conventional home-purchase mortgages, manufactured-home loans tend to carry higher interest rates and less favorable terms. Further, because there is limited standardization on manufactured-home loans, borrowers often have difficulties determining the best loan terms on offer.

Retailers often also serve as loan brokers, similar to mortgage brokers in the conventional market. The same concerns over predatory-lending techniques plaguing the mortgage lending industry also manifest themselves in the manufactured-housing finance arena. Retailers serving as loan brokers may earn more on the transaction for charging borrowers higher interest rates, leading retailers to push buyers into higher-cost loans. With the higher interest rates and shorter terms of many manufactured-home loans, cus-

tomers may not realize the production-side cost savings of manufactured housing. Despite the move to rationalize manufactured-housing finance, abuses persist, even as the quality of the product steadily improves.

Some manufacturers are encouraging new models of distribution. It is not unusual for a manufacturer to own retail sites, but others are emphasizing sales directly to consumers and developers. Champion Enterprises Genesis Division is one such model; all units are sold directly to developers, with an emphasis on designs which match existing styles and environments. It is yet unclear if this signifies change in the structure of the industry. Retailers can provide a useful locally based intermediary and problem solver, but as manufacturers develop the capacity to work directly with developers, their role may diminish.

Installation

The installation, or placement of a unit on a site, represents the final stage in the manufactured home distribution chain, and some say is the industry's Achilles heel. The most common installation method uses concrete block piers to support the unit, although some homes are set on complete foundations, including concrete slabs and foundations with crawl spaces of basements. In the case of multisection units, the sections must be married (joined together) and sealed. Once placed, the wheels, axles and hitch are removed, the unit is connected to site utilities, and an installer adds skirting, entry stairs and porches, and often a carport.

The Manufactured Housing Improvement Act was passed in 2000 to begin to better address problems related to installation, such as the frequent shifting of blame that occurs when it is unclear whether the problem resulted from manufacturer or installer error. This new legislation requires all states to adopt a dispute resolution program by December 2005 that will assign responsibility, where appropriate, to the party at fault. Many manufacturers, seeking to reduce exposure to liability, have required their own installers to perform certain tasks or even inspect the units before occupancy.

Placement

Two placement models exist for manufactured housing: placement on owned land and placement in rental parks, or leasehold communities. Homes placed on owned land are increasingly treated like conventional single-family housing units with respect to financing and unit resale. Tenants of rental parks, however, do not generally use conventional loans. Moreover, tenants in rental parks face many of the same risks as other renters, including potential rent increases, poor maintenance of common areas and eviction. Yet, because these renters own their structure, the costs of moving are significant. Moving a manufactured home to a new lot typically costs $3,000 or more, even for a short distance. As a result, tenants may have limited recourse to affordability problems resulting from escalating rental payments for the land on which their unit is installed.

It is not uncommon for residents of manufactured-home communities, particularly those on leased lots, to refer to the community or park as their neighborhood. In fact, with relatively high densities compared to other housing in rural or suburban areas, manufactured-home communities often represent tightly woven social networks more commonly thought of in urban areas. Some social scientists have begun to study the value and significance of these communities, especially among lower-income households. Community development efforts to organize neighborhoods and residents have also begun to emerge in manufactured-home communities (MacTavish and Salamon 2001).

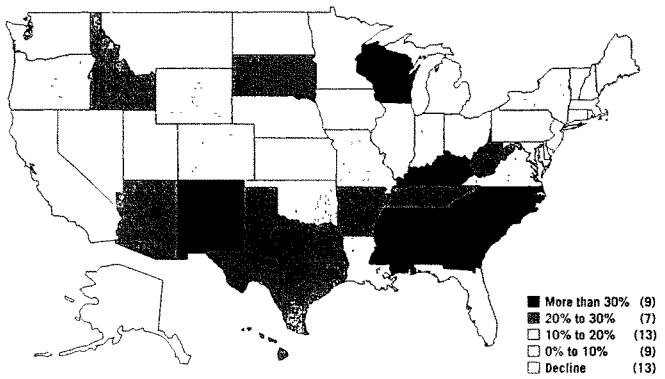
Characteristics of the Manufactured-Housing Stock

The nation's manufactured-housing inventory ranges from smaller, pre-HUD code, poorly maintained, single-section units sited in densely settled "trailer parks" to larger homes with characteristics and amenities that rival comparable site-built housing. While some view this inconsistency as cause for concern, it is also an important reason why manufactured housing remains a flexible source of affordable housing. Housing advocates need to be careful not to paint this housing stock with a broad brush. The issues and strategies related to cost-effective, new manufactured-home development are very different from the significant health and safety issues associated with the oldest stock. However, both sets need to be considered within the context of unhealthy financing markets.

Geographic Distribution

Manufactured housing is growing most rapidly in the South (Figure 2), in large measure reflecting the

Figure 2: Most Rapid Net Increases in Manufactured-Home Ownership Spread Across the South



Source: U.S. Census Supplemental Survey

region's relatively large lower-income, immigrant and retiree populations. Overall the South contains 55 percent of the nation's owner-occupied manufactured-housing units, while the rest of the national manufactured-housing inventory is spread throughout the West (19 percent), Midwest (18 percent) and Northeast (9 percent).

Manufactured housing is an especially important home-ownership option in rural areas. Fully half of all owner-occupied manufactured homes are located outside metropolitan statistical areas, where they comprise 16 percent of the stock of owner-occupied homes. By comparison, just six percent of the stock within MSAs is manufactured. The prevalence of manufactured housing in rural areas is in part a reflection of the costs and logistical challenges of site-built construction on relatively remote and scattered sites. It is also due to rural residents' generally lower incomes, and to the challenge of arranging standard mortgage financing for lots and land uses that do not conform to customary mortgage-underwriting criteria. Part of manufactured housing's appeal, in fact, lies in the ease with which units can be sited, a characteristic that is particularly important in areas lacking well-developed construction and trade sectors. Manufactured housing's popularity in rural areas also results from a lack of affordable-housing options, such as multifamily rental units, which are rarely developed at a cost-effective scale in low-density settings.

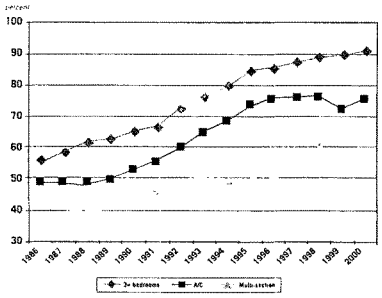
Land-Use Restrictions

In addition to economic factors that favor location of manufactured homes in rural areas, land-use policies also tend to limit the ability of both individuals and developers to place manufactured homes in many urban and suburban locations. Indeed, manufactured housing often meets strong resistance from neighborhoods and towns. This is due to a combination of aesthetic concerns, apprehension over increased demand for municipal services, negative attitudes due to the presence of older trailer parks, and fears that manufactured housing will negatively affect the value of neighboring site-built homes. Existing empirical studies suggest that concerns about the adverse implications of manufactured housing are often exaggerated. In particular, several studies of local housing price data uncovered no noticeable effect of manufactured homes on the sales prices of neighboring properties (Warner and Scheuer 1993; Stephenson and Shen 1997; Hegji and Mitchell 2000). Like all affordable housing developments, the Not In My Back Yard (NIMBY) mentality may not be explained by any economic rationale, but is rather grounded in stubborn social perceptions of low-income families and communities.

Improving Quality and Design

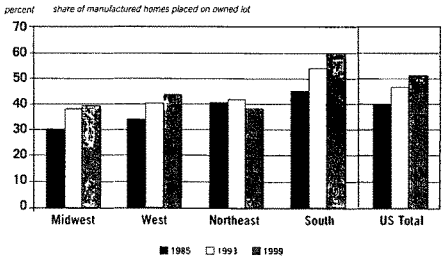
The quality of manufactured housing continues to improve as units get larger and include more amenities. The HUD code was revised in the 1990s to improve energy efficiency, ventilation standards and wind resistance. Since 1986, the share of new manufactured homes with central air conditioning has risen from 49 percent to 75 percent. Over the same period, the share with three or more bedrooms climbed from 55 percent to 91 percent (Figure 3). The dramatic growth in unit size is linked to the increased prevalence of multisection manufactured homes. Manufactured homes' larger scale and innovations like hinged roofing systems and two-story units have added room for amenities and design features similar to those available in site-built homes. Today, manufactured homes are available with vaulted ceilings, state-of-the-art appliances and complete drywall interiors. On-site customizing of garages and porches further enhances the curb appeal of the manufactured product (Stinebert 1998). Increasing numbers of manufacturers are now able to cost-efficiently produce attached porches to units, thereby reducing on-site costs and speeding up on-site completion. Long a hidden consumer burden, operating costs are beginning to be addressed by some manufacturers of Energy Star[1] homes and cost-conscious consumers and developers

Figure 3: Size and Quality of Manufactured Housing Improving Steadily



Source: U.S. Bureau of the Census, Construction Report

Figure 4: Share of Manufactured-Housing Owners Owning Land Continues to Climb



Source: 1985, 1993, and 1999 American Housing Surveys

Manufactured housing and the standards of the HUD code bring into focus the tension between providing affordable shelter for low-income families and high-quality housing for communities. Clearly any building code must trade off the costs and benefits of quality and cost. The HUD code, like other codes, provides standards for safety and health. But as the industry, and consumer advocates, pressure for increasing the required quality standards beyond basic safety, the costs of a minimum HUD-code unit will also escalate. Certainly from a design aesthetic, newer units are more easily assimilated into the conventional housing stock. But these features have a cost, and that affects the affordability of entry-level housing.

Land Tenure and Appreciation

One of the most confounding issues associated with manufactured housing concerns land tenure. As of 1999, just over 50 percent of the total manufactured-housing stock was sited on owned land, up from 40 percent in 1985 (Figure 4). Since 1993, the majority (58 percent) of newly placed units, even among lower-income buyers, have been sited on owned land. Meanwhile, the share of units placed in manufactured-home communities has been falling, from 41 percent in 1993 to 31 percent in 1999.

[1] ENERGY STAR is as voluntary labeling program designed to identify and promote energy-efficient products, in order to reduce carbon dioxide emissions administered by US Environmental Protection Agency with the US Department of Energy. ENERGY STAR has expanded to cover most buildings, heating and cooling equipment, appliances, equipment, lighting, and consumer electronics.

Land tenure is a key and often misunderstood ingredient in assessing the attractiveness of manufactured housing as a dwelling choice and as an investment. The key to such comparisons is carefully establishing the alternative tenure/investment arrangement. Studies considering this issue typically do not carefully control for factors that might incorrectly produce such a result, the most important being the extent to which the land under the structure contributes to the home's value. In virtually all cases it is, in fact, land ownership that drives what is commonly thought of as "house price appreciation."

Figure 5 presents a comparison of the price appreciation of representative manufactured and site-built homes over the past decade. Based on Freddie Mac estimates of price appreciation of a site-built home of constant characteristics, a representative home valued at $100,000 in 1990 would have appreciated in value to $142,499 by 2000, an overall increase of 42.5 percent or an inflation-adjusted increase of 8.2 percent. At the same time, the best available information suggests that over the same period, the cost of constructing this home only increased by 35.6 percent, or 2.9 percent in inflation-adjusted terms. This need not be the case, as real increases in the underlying costs of key factors of production could have increased the cost of constructing a home of constant characteristics much faster than overall inflation. The fact that the inflation-adjusted change in home-construction cost is close to zero reflects the fact that over the decade, improved efficiency in construction techniques almost exactly offset any upward pressure that increased labor or other costs might have had on the total costs of homebuilding.

Figure 5 repeats this analysis for a modest manufactured home valued in 1990 at $27,800. Over the decade, the cost of replacing this unit rose by 33.9 percent, but this represented only a 1.6 percent inflation-adjusted gain. Shown this way, there is little wonder that manufactured homes—by themselves—do not appreciate. Even if a manufactured home is well maintained and in brand new condition, it would not sell on the market for more than the cost of a newly produced unit of similar characteristics. Yet by the same token, as long as homebuilding efficiency continues, then the same will be true for site-built homes: that is, there will be limited opportunity for real increase in home prices (excluding appreciation in land price) as long as the cost of new construction grows slowly in inflation-adjusted terms.

The data in Figure 5 help explain the meaning of a recently completed assessment that compared potential for home-price appreciation (and equity or wealth building) for site-built homes and manufactured homes on owned and rented land. In a study using time-series data from the American Housing Survey, Jewell found that while site-built homes consistently appreciated faster than manufactured homes sited on rented land, there was not a statistically significant difference between appreciation of site-built homes and manufactured homes on owned land (2002). Since land is the key ingredient pushing up the value of site-built homes, it follows that unless sited on owned land, manufactured housing will have little or no potential to increase in value faster than the rate of inflation.

With land appreciation representing the major factor behind increasing home value, these studies point out the importance of expanding the potential for lower-income households to purchase manufactured homes and place them on land that they own. Indeed, for manufactured housing to realize its full potential as an affordable-housing option, expanded efforts must be made to increase the share of manufactured homes placed on owned land. This combination both lowers the cost of financing a home, while still enabling owners of manufactured homes to build wealth at rates similar to owners of site-built housing.

Figure 5: Illustration of Equity Built Through Ownership of Land, Not Structure

Site-Built Home	Value		Percent Change	
	1990	2000	Current $	2000 $
Unit	$75,000	$101,704	35.6%	2.9%
Land	$25,000	$40,795	63.2	23.9
Total	$100,000	$142,499	42.5	8.2

Manufactured Home	Value		Percent Change	
	1990	2000	Current $	2000 $
Unit	$27,800	$37,231	33.9%	1.6%
Land	$10,000	$16,318	63.2	23.9
Total	$37,800	$53,549	41.7	7.5

Source: Authors' calculations of Freddie Mac and NAHB reported data

At the same time, it is important to recognize that it is the absence of the land acquisition price that makes manufactured housing affordable to many low-income people. As a result, while land purchase is necessary to improve appreciation, it may prove to be a "deal breaker" for some. For these families, long-term site control, reduced financing costs and relief from eviction will reduce their costs and risks, but still offer only the value of their structure as a vehicle to accumulate and store wealth. Owning a manufactured unit sited on leased land may be a reasonable alternative to renting for lower-income households, granting them additional control over their living environment, but for those looking to build wealth at rates similar to site-built housing, land ownership is crucial.

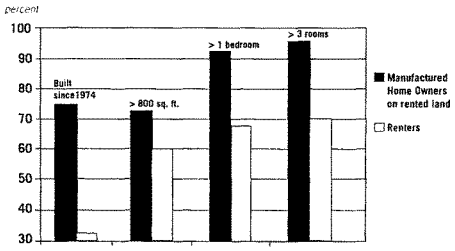
Affordable Rental Housing

Even for those who cannot afford to purchase land, manufactured-home ownership can be an attractive alternative to renting an apartment. Home-ownership tax breaks (deductions for interest and taxes) still apply to manufactured homes, including those on leased land. As Figure 6 shows, manufactured units that very-low-income rural renters occupy are newer, of a higher quality, and have more rooms than the site-built units rented by this sector.

During focus groups with existing manufactured-home owners, as well as prospective buyers, it was common for residents to suggest they preferred manufactured units, even in dense parks, to multifamily housing, due to the increased privacy and greater access to land. They suggested that these units offer them at least the ability to gain from their pay-down of principal—and at the end of the ownership they would have more than the security deposit they would receive in an apartment, even if their unit depreciated dramatically. Others suggested that because they fail to qualify for rental-assistance programs, manufactured housing is the only affordable choice. Most importantly, none of these customers felt that newer, site-built housing was a viable alternative to manufactured housing. They commented that affordable, site-built homes are in poor condition and in undesirable areas. Focus group participants felt they had two choices: rent a low-cost apartment, or buy a manufactured home and lease a lot in a park. Despite strong and honest reactions, it was clear that the buyers of manufactured homes on leased land felt they made the best choice available to them.

Due to basic principal paydown alone, even a depreciating manufactured home on rented land may produce net residual value for a family. For example, a $30,000 home which depreciates at 5 percent annually will be worth approximately $19,000 after ten years. A 15-year loan at 10 percent interest will have a balance of $13,500 at that point in time. Even excluding $3,000 in initial down payment and $1,100 in transaction costs, the family is ahead $1,400 over renting an apartment of similar quality and cost. This is certainly not wealth creation at the level typically hoped for from most home-ownership programs, but this analysis shows that low-income families may be making rational choices given their limited options.

Figure 6: Ownership of Manufactured Housing is an Attractive Alternative to Renting for Very-Low-Income Household in Rural Areas



Note Chart includes only very low income households (<50% of area median) outside MSAs.

Source: 1999 American Housing Survey

Changing Demographic Characteristics of Manufactured-Home Owners

Traditionally manufactured housing has appealed to first-time homebuyers, retired families and lower-income families. However, as the quality of the product has improved, the demographic characteristics of households living in manufactured homes have begun to mirror those of homeowners overall.

Household Income

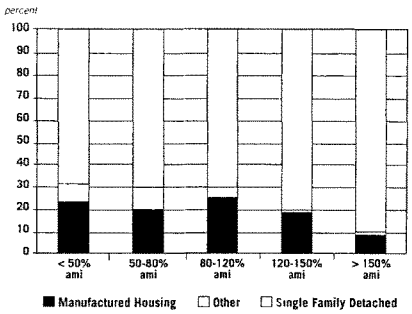
During the 1990s manufactured housing continued its move up-market. In fact, between 1993 and 1999, 18 percent of the growth in home ownership among

households earning 120 to 150 percent of their area's median income came through manufactured housing Even for those earning 150 percent or more of area median, eight percent of home-ownership growth came from manufactured housing. Further, these levels are not far below manufactured housing's 23 percent share of growth in ownership among those with incomes below 50 percent of area median. As high-end manufactured units become increasingly difficult to distinguish from comparable site-built units, manufactured housing's presence in the upscale market is likely to continue to expand.

Age Structure

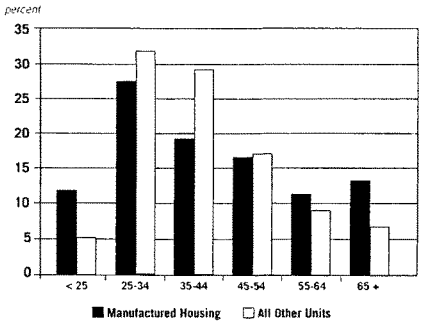
Manufactured-home purchasers are typically younger or older than owners of site-built homes. In 1998 and 1999, 12 percent of manufactured-home buyers were younger than 25, compared with just 5 percent of site-built buyers (Figure 8). Similarly, while more than 13 percent of recent manufactured-home buyers were older than 64, less than 7 percent of recent site-built buyers were. Owning or renting manufactured housing appeals to elderly households in part because these households are less concerned about equity build-up linked to land ownership, and because many prefer to have more wealth available to meet medical and other expenses. Manufactured units also have many characteristics favored by empty-nest households, particularly smaller yards and living space contained on one level. Some manufactured-home communities focus on the needs of older homeowners, even restricting residents to age 55 and older.

Figure 7: Income Characteristics of Owners of Manufactured, Single-Family and Other Housing Types



Note: AMI=Area Median Income. Source. 1999 AHS

Figure 8: Manufactured Housing Serves Young and Old Disproportionately: Recent Buyers of Manufactured Housing By Age Group



Note: Recent buyers are those purchasing homes in 1998 and 1999. Source: 1999 American Housing Survey

The low costs and easy entry favor first-time homebuyers, especially those with limited incomes or savings, such as single-parent households and single females. As manufactured housing gains market share among those in their prime years for housing consumption through improved quality, marketing and design, the age distribution of owners of manufactured homes should converge to that of the overall owner distribution.

Race and Ethnicity

Once largely made up of whites, owners of manufactured housing increasingly reflect the racial diversity of the nation. In fact, the current racial and ethnic distribution of manufactured homeowners for African-Americans, whites and Latinos differs little from that of homeowners overall. This conversion has been driven by the growth in manufactured home ownership by African-American and Latinos that far exceeds that of whites over the last few decades. In fact, Latino and African-American manufactured-home ownership grew at compound annual growth rates of 6.1 and 4.6 percent, respectively, for the 1985 to 1999 period, well above whites' 2.3 percent. If these trends persist, African-Americans' share of all manufactured homeowners (currently 7 percent) will soon exceed their 8 percent share of all homeowners. Latinos, who are currently 5 percent of manufactured homeowners, likewise seem set to surpass their 6 percent share of all homeowners.

II. CHALLENGES OF MANUFACTURED-HOUSING FINANCE

The financing system for manufactured housing consists of two very different markets:

(1) real estate lending, which historically is restricted to units on owned land, and (2) chattel lending, typically units on leased land or not titled as real estate, but instead as personal property. Many low-income buyers, especially those living in leased-land communities, finance their purchase with an chattel loan, more similar to a car loan than conventional mortgage. The potential mobility of leased units (although rarely exercised), and the fact that tenants on leased land have little protection from eviction, have hampered the development of more affordable chattel-loan products. Moreover, it is often difficult to obtain financing for the purchase of an existing manufactured home, especially if it has been moved from its original location. The collateral risks, as well as borrower characteristics, discourage many lenders—including those with public subsidy—from financing manufactured-housing loans. Class stereotypes are pervasive as "trailers" continue to be viewed negatively by real estate professionals and lenders. Nevertheless, owners of manufactured units will have limited potential to build equity if they cannot find an affordable means to finance the purchase, repair, replacement and resale of their homes.

Relaxed credit standards among manufactured-home lending specialists in the mid-1990s led to an enormous rise in loan defaults beginning in the late 1990s and continuing to 2002. A recent estimate suggests 75,000 manufactured homes were repossessed in 2000 alone (Stringer 2001). The industry suffered heavy losses and has instituted tougher lending standards as a result. Nevertheless, manufactured-home financing lags behind the rapidly evolving world of mainstream mortgage lending. From a lender's perspective, manufactured homes placed on leased land, not titled as real property, lack the security of mortgages for site-built homes built on owned lots. Even when the borrower owns the land on which a unit is sited, faulty initial construction or improper installation can shorten the useful life of the home, making long-term financing contracts problematic. While loan products addressing the unique characteristics of manufactured housing exist, the secondary market for these loans is small, thus reducing the volume of loans available and increasing the costs of these loans. Lenders respond to this reduced liquidity, and the added risks, by offering credit at higher interest rates and shorter, more restrictive terms than for conventional mortgages. Higher financing costs offset much of the cost advantages associated with manufacturing efficiencies, and hence undermine the ability of manufactured housing to fully realize its potential as an affordable housing option.

Alternative Mortgage Arrangements

Structure-only, chattel financing is dominated by national consumer-finance companies and manufactured-home lending specialists who work directly with retailers. In these loan contracts, manufactured homes are treated as personal property and financed with a consumer loan in which the lender takes a lien on the home. While the lender does have a secured interest in the dwelling, the process of repossession and resale of a manufactured home can be costly, especially in a market where prices of existing homes are depreciating rapidly.

Land-home or "real estate" financing for manufactured homes is more akin to conventional mortgage lending for site-built housing, but there can be differences here as well. For new units placed on owned lots, acquisition financing may take the form of a "one-write" construction/permanent loan, where several separate draws are taken to cover land acquisition, site preparation, unit acquisition and installation, and permanent financing (Sichelman 2001). In some cases where a new or existing unit on owned land is being sold, the structure/parcel combination may qualify for financing identical to that available to purchasers of site-built housing. The likelihood of this happening often depends on whether the home and lot characteristics conform to secondary-market standards, including mortgage insurer acceptance.

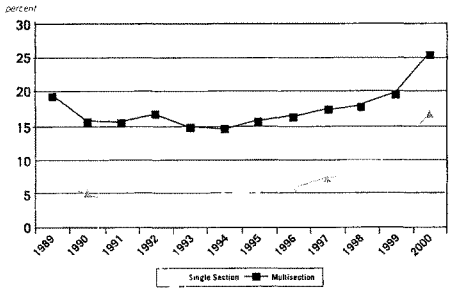
Overall, a majority of manufactured homes are still financed with chattel mortgage loans rather than traditional real estate mortgages, though the share financed with real estate mortgages is climbing as more homes are sited on owned land and titled as real property. In 1989 just 13 percent of new manufactured-home placements were titled as real estate, but by 2000 this share had increased to 22 percent. Depending on the state, multisection manufactured homes are more likely to be titled as real estate and the share rose from 19 to 25 percent from 1989 to 2000. However, the share of single-section homes financed as real estate also increased from 7 to 16 percent over the same period. This trend appears durable, since even during the 1999 to 2000 period, when the industry was in retreat, the share of units

titled as real estate increased steadily. Further, the trend extends to all regions and is growing most rapidly in the South, where the share of newly placed single-section units titled as real estate rose from 6 to 16 percent between 1989 and 2000, and the share of multi-section placements increased from 13 to 20 percent.

Manufactured-home borrowers unable to access the highly competitive conventional home mortgage market frequently have few financing options. Most borrowers simply take the loan package offered by the retailer—often without knowing the retailer receives fees and yield-sharing with the lender involved. This practice has raised concerns that purchasers are unaware of, or are even being actively steered away from, better financing alternatives. Focus group participants reported that lower-income families living in or considering manufactured homes, especially those with spotty credit backgrounds, are attracted by the convenient, quick-approval personal loans, despite the costs involved. In fact, many could have qualified for better loan terms by shopping around. The higher costs they pay can needlessly offset the potential savings that these borrowers might have achieved by purchasing lower-cost manufactured homes.

The typical manufactured-home buyer secures mortgage credit on less favorable terms than similarly situated buyers of comparable site-built housing. According to the American Housing Survey, in 1999 owners of manufactured housing on rented land paid median interest rates of 9 percent. The median interest rate for those who owned their land was 8.7 percent. Both are well above the 7.5 percent median rate for owners with mortgages on single-family, detached homes. Similarly, the typical mortgage term for owners of manufactured homes placed on rented land was just over 15 years, compared with 18 years for manufactured homes on owned lots and over 25 years for owners of single-family detached homes.

Figure 9: Share of New Placements of Single-Section and Multisection Manufactured Housing Titled as Real Estate Rises



Source: U.S. Bureau of the Census, Construction Report

Figure 10 illustrates the toll that more costly mortgage financing can take on the affordability of manufactured housing. For example, consider a 2,000-square-foot, site-built home selling for the national median of $144,728. The median sales price for a manufactured home of similar size and quality located in a land-lease community is far lower, at just $48,960. Even located on a modest owned lot valued at the same amount as the lot included in the site-built example, the total purchase price would be only $84,274.

While the land-lease option results in a substantially lower purchase price and down payment, the interest rate is higher by two percentage points. Indeed, with a monthly payment of $645, the land-lease option is more expensive than the land-home arrangement. The outcome of the two scenarios is even more different, however, because the land-rent component of the monthly payment is likely to increase over time for the land-lease option, while the land under the site-built unit is likely to appreciate while mortgage payments remain stable. Little wonder that advocates continue to highlight the advantages of owned lots for purchasers of manufactured home. Real estate offers the purchaser both lower monthly housing payments and potential equity build-up from land appreciation.

Consumer Protection Issues

Unlike loans for real property, personal-property financing is not governed by the Real Estate Settlement Procedures Act (RESPA), which requires disclosure of settlement costs and prohibits kickbacks or referral fees for mortgage brokers. Some focus group participants argued that manufactured-home retailers, who often play the role of loan brokers, were taking advantage of this situation to earn payments on loan originations, credit life insurance and property insurance with little benefit to the borrower. Since the market peaked in 1998, however, many of the worst loan brokers have ceased operations. Credit life insurance contracts are reported to be rarely sold today, for example.

Defaults are far higher on manufactured-home loans than conventional mortgage loans. Some 12 percent of all manufactured-housing loans end up in default over the life of the loan, a rate that is some four times that of conventional home mortgages (Consumers Union 1998). In the late 1990s, delinquency rates rose for manufactured-housing loans, an increase linked to the easy credit terms that finance companies offered buyers during the mid-1990s. In fact, the extremely high demand for manufactured homes over this period was stimulated by lending to borrowers who in many cases did not have the requisite income, wealth or credit characteristics to take on the financial challenge of home ownership. Consequently, in 2001 alone fully two percent of all outstanding manufactured-housing loans were in repossession proceedings (Walker Guido 2001).

Even as advocates, regulators and lenders alike are mobilizing to ward off the abuses of predatory lending and excesses in the subprime sector of the mortgage-lending arena, manufactured-housing finance remains an area in which the range of permissible loan terms and tactics extends beyond what would pass muster in the conventional mortgage market. As a result, manufactured-home buyers, who are often those with the fewest resources, remain more vulnerable to a variety of unscrupulous practices than borrowers in the conventional market.

Figure 10: Comparison of Financing of Site-Built and Manufactured Homes (2,000 square feet)

	Site-Built on Private Land	Manufactured on Private Land	Manufactured on Leased Land
Construction Costs	$77,140	$38,000	$38,000
Overhead/Finance	$32,274	$6,460	$6,460
Land Costs	$35,314	$35,314	$-
Delivery and Set-Up		$4,500	$4,500
Total Sales Price	**$144,728**	**$84,274**	**$48,960**
Type of Loan	real property	real property	personal property
Interest Rate	8%	8%	10%
Term in years	30	25	25
Down Payment (%)	10%	10%	10%
Down Payment ($)	$14,473	$8,427	$4,896
Closing Costs (4%)	$5,210	$3,034	
Sales Tax (3%)	-0-	$2,528	$1,433
Security Deposit	-0-	-0-	$250
Initial Cash Outlays	**$19,683**	**$13,989**	**$6,579**
Loan Amount	$130,255	$75,847	$44,064
Monthly Loan Payment	**$956**	**$585**	**$400**
Monthly Land Rent	-0-	-0-	$250
Total Monthly Payment before taxes and utilities	**$964**	**$561**	**$645**

Source: Based on model from HUD (1998) Table 23

Refinancing, Home Improvement and Resale Finance

There are few lenders engaged in lending for refinancing or improving manufactured homes, or for the purchase of an existing, previously owned unit not attached to a permanent foundation. Because of the collateral risks and related difficulty in assessing the value of a unit, these loans can be risky. Lenders interviewed for this project suggested that automated appraisals or book values for units are unreliable, and appraisals are difficult. One appraiser admitted she would conduct a conventional appraisal if and only if the unit is permanently installed. Otherwise, she will not estimate a value. Focus groups comprised of current manufactured-home owners suggested they did not know of any way to refinance their loan, except with their current lender. None of the participants in the focus group had tried to refinance their loans, despite paying interest rates near 10 percent. For these same reasons, home-improvement loans for manufactured units on leased lots are much less common than in the conventional market. A few retailers cater to this market by selling manufactured or site-built additions, but in general home improvements are self-financed. Existing owners of manufactured units sited in leased-land communities suggested they would be able to sell their unit, but added it would be more difficult if the sale involved moving the unit. Park owners often require notification of a unit for sale, and must approve the new tenant for the lot lease. Most previously owned units are sold for cash or through seller financing, in part due to the dearth of other options. The lack of a viable financing mechanism for refinance, improvement and resale exacerbates the collateral value risks of manufactured housing. By limiting the marketplace to loans only for new units, the demand for older units is constricted to that segment of the market that can self-finance.

Limited Sources of Mortgage Capital

Until very recently, few banks, savings and loans, or credit unions were willing to finance manufactured homes as real estate, except in cases where the land is owned or a land lease is in place with a length longer than the mortgage loan term.[2] In its *Annual Survey of Manufactured Home Financing,* the Manufactured Housing Institute found that consumer-finance companies that specialize in manufactured-home lending originate the bulk of manufactured-home loans. In recent years, mortgage lenders and government-sponsored enterprises Fannie Mae and Freddie Mac have begun to step up their activity in this market. Given the enormous emphasis on low-income, first-time homebuyers, and on policy efforts focused on opening mortgage markets for these buyers, the lack of attention manufactured-housing finance receives is somewhat ironic. Correcting market failures in manufactured-housing finance represents a crucial way to expand and sustain home ownership.

FHA-Insured Lending and Ginnie Mae Securities

The Federal Housing Administration has several mortgage-insurance programs for loans used to purchase or refinance manufactured homes. FHA Title I can guarantee loans for manufactured homes, for manufactured homes and the property on which they are located, or for loans to purchase a manufactured home lot. FHA Title II can be used where the home is permanently placed on land and treated like real estate. These programs are used for fewer than 10 percent of all manufactured-home placements in a given year, despite FHA's emphasis on serving low-income borrowers. Inefficient administration of these programs, low loan limits and other restrictions create barriers few lenders are willing to confront. FHA's recent increases in insurance premiums and lender standards might begin to revive the struggling, negative cash flow program.[3] In the 1980s, Ginnie Mae issued a limited number of "eagle" certifications allowing lenders to receive a Ginnie Mae guarantee in the secondary market for their pools of manufactured loans. Few lenders use Ginnie Mae's manufactured-home loan programs today, in part because of regulations put in place to stem high losses in this product line in the past. Yet competition among lenders would be enhanced if Ginnie Mae once again supported this program.

Following Ginnie Mae's tightening of secondary-market criteria, for example, units in FHA's Title I program declined in the 1990s from 28,404 loans in 1991 to only 377 loans in 1999 (Genz 2001). As more community banks and mortgage companies enter this market and responsibly underwrite loans, boom and bust cycles could be dampened if FHA provided a consistent source of credit with clear and effective standards.[4] FHA and HUD need to allocate more staff and resources to explore options for supporting this segment of home ownership.

In most states, manufactured units may be classified as real estate. However, over a dozen states do not permit HUD-code units on leased land to be legally defined as real estate.[5] As a result, FHA and other mortgage programs cannot legally participate in mortgage loans on manufactured units in these states. Without changes to state laws, federal policy actions will be moot.

Most states permit classification of manufactured homes as real estate if sited on owned land. About fifteen states, however, will not classify manufactured homes as real estate regardless of land ownership, hindering the integration of manufactured housing into mainstream housing finance and capital markets.

Rural Housing and Veterans Affairs

The programs of the U.S. Department of Agriculture's Rural Housing Service cover new, permanently installed manufactured homes sold by retailer-con-

[2] In 2001, Freddie Mac created a loan product for leased-land units, stipulating the lease term must be five years greater than the mortgage term; Fannie Mae offers a similar product requiring a 10-year differential. These loans offer rates of 3 percent or more below chattel loans.

[3] 24 CFR Parts 201 and 202 in the Federal Register, Vol. 66, No. 216, November 7, 2001, increased the Title I and II premium to 100 basis points and increased the asset requirement for lenders/dealers.

[4] In 2000 the securitization of manufactured-housing chattel loans dropped to half the previous year's levels, despite only a 20 percent drop in the overall shipment of units. Industry analysts suspect the differential in loan volume is made by local lenders making chattel or real estate loans, which they are holding in their own portfolios.

[5] Arkansas, Connecticut, Florida, Maryland, Minnesota, Mississippi, Missouri, Montana, Nebraska, Nevada, New Jersey, South Carolina, Utah, Washington, West Virginia and Wisconsin did not recognize these units as of 1999.

tractors who meet strict agency requirements, but as with the FHA, volumes are low. Nationally, RHS manufactured-home originations amounted to just 487 loans in the Section 502 direct-loan program, and 336 loans in the Guaranteed Rural Housing program, despite the preponderance of manufactured units in rural areas (Genz 2001). Likewise, Veterans Affairs insurance programs, which serve as many as 200,000 borrowers annually, have not served a single manufactured-home buyer in recent years. VA's manufactured-housing finance programs continue to exist, but with effectively zero usage.

State Housing Finance Agencies

A frequent source of mortgage capital for first-time, low-income homebuyers are mortgage revenue bonds issued by state housing agencies. However, nationally there are few manufactured-housing finance programs runs by state agencies. The New York and New Hampshire agencies have financed resident purchases of manufactured-home parks. Maine has offered revenue bond-funded loans on leasehold mortgages since the early 1980s and now self-insures loans on single-section units, including resale homes (Genz 2002). Alaska, North Carolina and several other states have also offered programs for purchase of new units on owned or leased land. Mississippi has offered mortgage credit certificates to provide consumers with a 40 percent reduction in interest rates on purchases of manufactured homes; however, there has been very little volume due to a lack of dealer interest. It seems that state housing finance agencies are also likely allies as advocates and community-development practitioners seek to improve opportunities for manufactured-home buyers.

The Role of the GSEs

Traditionally, Fannie Mae and Freddie Mac have not supported a secondary market for manufactured-housing loans classified as personal property. Recently new products have been introduced for tenants of land-lease communities that, under specific circumstances, allow borrowers to access credit as real estate loans. For example, Freddie Mac's program for financing manufactured homes on leased land requires that units be sited on properties with leases running at least five years longer than the loan term, the homes be built on permanent foundations, and are subject to taxation as real property. Freddie Mac will also purchase loans made to finance entire manufactured-housing parks.

Though Fannie Mae and Freddie Mac have established guidelines for accepting real estate mortgage loans secured by manufactured housing, their participation in the sector has been limited, particularly in comparison with their dominance of the conventional, conforming lending market. HUD estimates that in 1998, the GSEs funded less than 15 percent of all loans for manufactured housing, compared with their 55 percent share of the overall home-mortgage market. Much of the GSEs' current activity is in homes sited permanently on owned land. To the extent that loans for such homes conform to other GSE standards, they are frequently pooled with loans for conventionally built housing, and their status as manufactured homes may be submerged. As a result, precise estimates of GSE market share are difficult to establish.

Recognizing the importance of manufactured housing in meeting the nation's housing needs, HUD's updated Affordable Housing Goals for Fannie Mae and Freddie Mac in 2000 encouraged the GSEs to increase their purchases of loans for manufactured housing. In doing so, HUD cited numerous studies showing that the manufactured-home sector was an important source of low-income housing, and argued that a more active secondary market could encourage lending to traditionally underserved borrowers.

Asset-Backed Securities

Asset-backed securities emerged as a source of capital for manufactured-home lending in the mid-1990s. Although the majority of manufactured-housing loans are traditionally held in portfolio, securitization of these loans has become common. Manufactured housing's share of total asset-backed security issues increased from three percent in 1995 to seven percent in 1999, before declining to four percent in 2000.[6] Considering the inherently higher risk profile of this type of lending, such asset-backed securities require significant credit protection. One sign of this for investors and lenders is that the spread between yield and coupon rates on manufactured-housing securities has historically been lower than for mortgage-backed securities, but higher than for credit-card and auto-loan pools (Davidson 1997).

[6] Other assets securitized include auto and student loans, credit-cards obligations, equipment leases, and collateralized bond and loan obligations.

III. MANUFACTURED HOUSING'S ROLE IN AFFORDABLE HOUSING

Currently very few affordable units are being created for low-income homebuyers. Using one set of mortgage underwriting assumptions, only 44 percent of all owner-occupied units in 1999 were valued in a range that would be affordable to a household earning 80 percent or less of area median income. Of the 540,000 affordably priced new units added to the housing stock from 1997 to 1999, *two-thirds* were manufactured units (Collins, Crowe and Carliner 2000). Manufactured housing clearly plays a crucial role in providing affordable home-ownership options. Yet very few community-development entities or local agencies are actively integrating manufactured units into their affordable-housing development strategies. Recent innovations in design, new installation standards and regulations, existing subsidies, the need for consumer education, and manufactured housing's key role in very-low-income rental markets all indicate the need to re-examine the potential of manufactured housing as part of an affordable-housing strategy.

Innovations in Design

Across the country practitioners are troubled by the boxy and generic design of manufactured housing and its effects on community character and sense of place. Practitioners in New Mexico report that new manufactured-home communities are virtually indistinguishable from their counterparts in South Carolina and do not fit into the local context. Both practitioners and consumers criticize the layout of most manufactured-home communities as too dense, affording little privacy. Practitioners respond favorably to the new designs that are available for manufactured units and published widely by the industry. However, focus group participants noted that in many regions innovative units have yet to be seen on the ground. Similarly, while many retailers sell a variety of models, they often have only a few units on display, making it difficult for consumers to understand the variety of options available.

Single-section units, despite some design improvements, are still rectangular in shape, evoking the old "trailer" stigma and contributing to the ongoing bias against manufactured housing. Moreover, single-section buyers who do not own land may be left with few choices of where to locate other than a rental park. But local resistance to the expansion of creation or parks often results in a shortage of lots and pushes land rents upward.

Advances in design and technology have made manufactured units more suitable for urban infill developments. In addition to savings from production techniques and lower materials and labor costs, factory-built units dramatically reduce security costs and speed up the development process. The Manufactured Housing Institute, in partnership with Freddie Mac and the Low Income Housing Fund, has begun to promote the use of manufactured housing as an urban-revitalization strategy. MHI has reached out to redevelopment authorities and housing agencies to educate them about recent changes and improvements in the industry. In 1996 MHI launched the Urban Design Project in an effort "to illustrate that today's manufactured homes can meet the need for affordable housing and can be aesthetically compatible within existing urban neighborhoods" (Manufactured Housing Institute 2001, 4). Five cities were selected to participate in the pilot project: Birmingham, Alabama; Louisville, Kentucky; Milwaukee, Wisconsin; Washington, DC; and Wilkinsburg, Pennsylvania. The cities and their respective development teams were selected through a request for proposals and evaluated according to criteria such as available funding sources, community involvement, site availability, potential for wider application and impact on the regulatory environment. One of the primary goals of the project was the removal of zoning and other regulatory barriers to the use of manufactured housing in urban areas; consequently the proposed project's ability to aid in this effort was seriously considered.

The projects demonstrated that collaboration between an architect and manufacturer could successfully develop attractive units that were context-specific and factory-built. Focus groups and the use of architectural models helped to educate the public about manufactured housing and helped to reverse negative perceptions. According to project observers, "city officials and the public are more concerned with appearance issues than with the difference between the HUD code and model building codes" (Manufactured Housing Institute 2001, 27). The Urban Design Project provided new insights into the opportunities and challenges of using manufactured housing as an urban infill strategy; however, only three of the five pilot programs were successfully carried out, suggesting a need for other approaches and models.

New Legislation Improving Installation

The lion's share of consumer complaints stems from installation problems. Improper installation undermines the quality, safety and durability of manufactured units. One manufactured-home inspector claims that over 90 percent of the homes he inspected were improperly installed (White 2002). Problems are typically associated with failing to set the unit properly on the piers, using too few piers, using piers made of materials inappropriate for the site, and setting the piers on foundations that cannot adequately support the unit or on ground that has not been compacted. Improper installation causes the piers and/or the unit to settle unevenly, warp, sag, and often crack, and can cause doors and windows to become misaligned, making them difficult or impossible to open and close. Few licensing procedures exist for manufactured-home installation, making it difficult to identify and sanction those with a history of poor performance.

The HUD code does not require manufacturers to provide warranty protection, and while it is a requirement in some states, there is no uniform system to ensure compliance. A typical warranty covers home defects for one year.[7] However, it does not include defects that result from improper transport or installation and often excludes problems caused by improper site preparation. According to Consumer's Union, most problems occur within the first year when the warranty is still in effect; however, consumers often encounter resistance when they call on the manufacturer or retailer to honor the warranty (Consumers Union 1998).

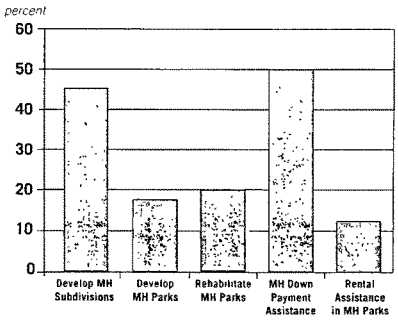
Although many states have adopted a model installation code developed by the American National Standards Institute, it is still often unclear to consumers whether the manufacturers, retailers or installers are responsible for correcting unit defects. The Manufactured Housing Improvement Act of 2000 requires HUD to develop a national model for installation standards, and gives states five years to either adopt these standards or develop an alternative and more stringent set of installation standards. States are also required to adopt a law mandating installer licensing and training, and installation inspections, by December 2005. In addition, the legislation also requires that each state establish a dispute-resolution system that will enhance consumer protection in situations where responsibility for poor product performance may result from some varying combination of manufacturer, retailer and installer error.

The new law potentially reduces the collateral risk lenders face that a unit may be improperly installed or placed on a faulty foundation. While there is hope the new law may signal a future marked by greater innovations in design and finance, in recent years many manufactured-housing lenders and developers have experienced record high delinquencies and repossessions. The next decade will prove if these growing pains can be resolved to form a market that better serves low-income families.

Emerging Use of Home and CDBG Subsidies

Explicitly, there are few prohibitions to using manufactured units in urban areas. However, local administrators and developers often discourage the use of HUD-code units in affordable housing projects. Clearly

Figure 11: Allowable Manufactured Housing Uses Reported by HOME Administrators



Source: Manufactured Housing Institute Survey, 2002

[7] Many warranties cover only "structural" defects and will not cover "cosmetic" problems. Determining which category a problem falls under can be contentious. Extended warranties are available, but they are frequently too expensive for the many manufactured-home residents who have modest incomes.

stating in the administrative rules of existing affordable-housing programs that manufactured units may be used may help overcome resistance. In fact, a recent survey of a sample of HOME program administrators by the Manufactured Housing Institute revealed that in many areas manufactured-housing projects would be eligible for HOME funds. However, it seems few such projects have yet been initiated.

Enormous Need for Homebuyer Education and Counseling

The lure of "no money down" and the immediate gratification that the one-stop shop affords are often overshadowed by the risk of an uninformed purchase. Manufactured-home buyers typically spend less time looking at other homes or attempting to find more favorable loan terms than is typical with site-built homebuyers. Quoted a lower monthly cost than their current rental payment, prospective buyers may sign on immediately, unaware of exorbitantly high interest rates and numerous hidden costs.

Retailers frequently promote the home-purchase transaction as a one-stop shop, arranging for financing with approvals coming in a few hours. While this brings value to the consumer, without question, there is a need for increased homebuyer education and counseling, especially for first-time buyers. There are currently few outside sources of information available to potential buyers and consumers have few places to turn to guide them through the manufactured-home purchase process.

While the Truth in Lending Act provides consumers a three-day cooling-off period during which they can terminate the real estate loan on their homes, a manufactured home financed as personal property rather than real estate does not offer such protection (Genz 2002).

Throughout the home-purchase process, consumers may interact with the retailer, manufacturer, transporter and installer. If something goes wrong it can be difficult for the consumer to discern who should be contacted. It is not uncommon for whoever is contacted to suggest that one of the other parties is responsible. Consumers may feel that the manufacturer is the obvious candidate to contact when problems arise since it was responsible for the construction, and it is likely to have the deepest pockets. Manufacturers, however, do not typically control the retail and installation networks, and therefore have limited influence over practices and promises.

Homebuyer educators and counselors interviewed for this project emphasized that all too often, the contracts and terms of financing have already been negotiated when the buyer begins counseling. Counselors point out that better informed buyers could reduce the number of repossessions, since they would scrutinize the financing terms and actual monthly costs, and be better able to gauge their preparedness for buying a home. The counselors interviewed welcomed opportunities for partnerships with manufacturers and lenders as a way to provide consumers with balanced information and prepurchase counseling earlier in the process.

Counselors are aware that there are dramatic variations in the quality of manufactured homes, but they do not always know how to discern the differences themselves, let alone aid consumers in making an informed decision. Checklists that specify what to look for in a home and what to ask the retailer before signing a contract are invaluable to both counselors and consumers. At present counselors rely heavily on the Internet for information about manufactured housing. They point out that many of the resources, while very helpful, are produced by the industry and therefore not entirely objective. In addition, they want to complement research with practical advice. For example, with respect to estimates of the life of a manufactured home, counselors would like more than a number. They want to know what, if anything, can be done to extend the life and how they can incorporate this information into their education curriculum. Additional topics homebuyer educators suggested for inclusion into a curriculum include the HUD code, financing options, the implications of placing a home on owned versus leased land, maintenance, energy efficiency, ensuring proper installation and property taxes. Each counselor also needs to uncover information on local zoning laws, tenants' rights and housing markets, since this varies by market.

None of the major homebuyer education curricula by Fannie Mae, Neighborhood Reinvestment, AHECI or other sources addresses manufactured housing. A few even incorrectly define these units. Given the preponderance of manufactured-housing purchases among

first-time, low-income borrowers who are often the focus of homebuyer education, this again seems incongruous.

Interviews and focus groups with leading practitioners and intermediaries suggest that creating a whole new curriculum for manufactured-home buyers is not the most effective strategy. Many of the skills and information currently included in conventional homebuyer-education programs are transferable to buyers of manufactured homes. The unique aspects of buying a new or existing manufactured home on owned or leased land could make up a supplement, likely covering one to two hours of material. Equally important is the training the trainers receive, and the materials made available for use by practitioners. Neighborhood Reinvestment Corporation will be offering such a supplement to its *Realizing the American Dream* materials, and integrating the material into its training-for-trainers sessions in late 2002.

A Crucial Part of the Affordable Housing Stock

Even as new manufactured homes get bigger and better, problems in the older manufactured inventory persist. The over 2 million homes manufactured before 1976, when the HUD code was enacted, present the greatest challenges, due to their small size and often advanced state of physical deterioration. While only 26 percent of owner-occupied manufactured units built since 1993 are smaller than 1,000 square feet, two-thirds of those built prior to 1976 are. For renters the gap is even greater, as fully 83 percent of rented units built before 1976 are 1,000 square feet or less, while just 31 percent of rented units built since 1993 are as small.

Problems with older units are more common among rented manufactured homes. While 95 percent of homes built since 1993 are owner-occupied, only 73 percent of those built prior to 1976 are. The very-low-income households that often occupy these older rented units have few housing options, making problems in this section of the nation's housing inventory particularly troubling. Consequently, many of the nation's lowest-income families, both owners and renters, continue to live in deteriorating manufactured units that have long since outlasted their useful life.

These older units are more often rented or sited on leased land, are smaller, physically distressed, and occupied by very-low-income households. However, they are a critical housing source for many low-income people. Strategies are needed to assist the thousands of households trapped in older, structurally inadequate units or locked into land-lease arrangements. If the communities 3.4 million families nationally who own home on rented are deducted from owner-occupied statistics, the national home-ownership rate, it would drop from 68 percent to 65 percent.

None of the practitioners, consumers or industry representatives interviewed for this project suggested many promising strategies for pre-HUD code units. Most expressed surprise that these units have lasted as long as they have, and a few seemed to wish the demise of these units could be accelerated because of the negative stigma they impart on the entire market. These units are replaced, often with state or federal subsidy, when floods or high winds cause damage, but otherwise tend to remain in use. The state of Vermont piloted a program to recycle units for scrap value, but found little economic value in the salvaged materials. There are cases, however, especially in regions with favorable climates, where 1950s-era units continue to be occupied in well-maintained communities.

Strategies are still needed to address the 1.4 million rental units, many of which are in substandard condition. Replacing aging units with better designed and fairly financed housing will help improve the overall appearance of many communities, as well as provide families with safer, more stable housing with increased opportunities for wealth-building.

IV. MODEL COMMUNITY DEVELOPMENT STRATEGIES

Difficult questions persist: What should be done about this housing stock? How can we protect the occupants? How can the cost advantages of manufactured units be used to achieve goals for affordable housing? What role can a community-based organization play?

This section draws on the experiences of five organizations that have begun efforts to address these issues:

- Better Housing for Tompkins County, Ithaca, New York;
- North Country Affordable Housing, Watertown, New York;
- Colorado Rural Housing Development Corporation, Westminster, Colorado;
- New Hampshire Community Loan Fund, Concord New Hampshire; and
- HomeSight, Seattle, Washington.

While these programs are small in scale, they demonstrate that it is possible to tap into federal and local funding sources for the replacement, rehabilitation and development of manufactured units. Innovative programs have traded in dilapidated mobile homes and trailers for more modern manufactured or modular units, and others have attempted to maximize the scrap value of aging units.

Replacement of Aging Manufactured Units

Better Housing for Tompkins County

In 1999 the town of Enfield, New York, received a $400,000 Community Development Block Grant (CDBG) to replace 18 dilapidated and insufficiently winterized mobile homes with units built since 1993. Better Housing for Tompkins County was contracted to administer the project.

To be eligible participants must own the land on which the new home will be placed, and earn less than 80 percent of area median income.[8] Once selected, participants must attend a prepurchase workshop offered by Better Housing. The land serves as the down payment; in addition, households can receive CDBG funds of up to $25,000 toward the purchase of their new unit, in the form of a second mortgage that is forgiven over a 10-year period.

As of January 2002, only two families had completed the program and moved into new modular homes. The program has had difficulty recruiting eligible participants. Stacey Crawford, Better Housing's executive director, explained that many potential participants are wary of assuming debt, while others face issues related to their income, credit history or property title. Some members of the community feel that the program, with its emphasis on replacement, is critical of their housing choice. In an effort to combat this perception, Better Housing has begun to promote manufactured housing as a replacement option.

North Country Affordable Housing

When 1990 Census data revealed that manufactured homes comprise 15 percent of the housing stock in rural Jefferson County, New York, North Country Affordable Housing conducted a survey which indicated that 83 percent of all homes built in the area in the last 11 years required some level of maintenance and repairs. In response North Country began to replace the oldest mobile homes with new modular or site-built homes in order to eliminate substandard housing. Program participants must live in Jefferson, Lewis or St. Lawrence county and earn 80 percent or less of area median income.[9] They must own their homes and the land on which the new units will be sited. A program priority is to replace units destroyed by fire. Potential participants must attend approved home-ownership training programs.

Participants are eligible for grants provided by the State of New York Affordable Housing Corporation and federal HOME funds of up to $20,000, subject to a recapture formula that is forgiven over a 10-year period. Average development costs, net of land, are $62,826 per home, more expensive than HUD-code units, but still cost-effective. Many participants contribute their own sweat equity to further lower costs, and the remainder is financed by local lenders and Rural Development RHS mortgages.

Since the program began five years ago, North Country has completed 55 units, with only one foreclosure. There is currently a waiting list of approximately 50 families interested in participating. However, Barbara Willis, North Country's executive director, estimates

[8] Tompkins County's estimated AMI in 2002 is $53,300. Data available at www.efanniemae.com.

[9] Estimated area median income in 2002 in Jefferson County is $39,400; Lewis County AMI is $38,900; and St. Lawrence AMI is $40,300. Data available at www.efanniemae.com

that only about one in four applicants successfully completes the process. Poor credit history, fear over assuming debt, and the length of the process are all common deterrents. Some participants lose patience with a process that can take up to a year when a new manufactured home could be purchased immediately. Program staff and outside contractors who really understand the program and are willing to work with the families individually are important since each situation is different.

Like Better Housing, North Country has designed its program with a preference for site-built, or in some cases modular factory-built units, over HUD-code units. This is a common approach among community-development practitioners—in some cases based on careful analysis, in others based simply on personal biases and perceptions.

Rehabilitation of Aging Manufactured Units

Colorado Rural Housing Development Corporation
In the late 1980s, Exxon Corporation abandoned an oil shale exploration in western Colorado, leaving behind a stock of empty mobile homes. Colorado Rural Housing Development Corporation saw this as an opportunity to rehabilitate the abandoned homes and provide low-cost housing for families elsewhere in the state.

The first phase of the project transported 12 single-section manufactured homes 150 miles to several scattered lots that were zoned to allow their placement. Once placed, new windows, drywall and insulation were installed, and rooms and garages were added to several of the units. The wheels were removed and CRHDC met with the county recorder's office to purge all the titles and convert the homes to real estate. Most of the program participants were renters, often living with other family members, and had incomes less than 60 percent of area median income. Once they were prequalified, they were placed into groups of six families. Each group worked together on the reconstruction of the homes, adding a sweat-equity component that further lowered total costs. Participants received training in construction techniques as well as extensive home-ownership education.

Phase two of the project relocated 12 multisection manufactured home units to a single site. The multisection units required less rehabilitation than the single-sections and cost about $40,000 per unit, including land.

A typical unit cost was about $34,000, and the sweat equity for each unit was valued at $10,000. The Office of Community Services of the U.S. Department of Health and Human Services and the Colorado Housing Finance Authority financed the project. Grants covered about 50 percent of the costs, while CHFA provided low-interest loans to finance the remainder. The grant contains a 20-year recapture provision. All the units have held up well and have appreciated in value; some residents have refinanced their homes or made additional improvements.

While this program was quite successful, a ready supply of vacant homes is a rare occurrence. Al Gold, CRHDC's executive director, reports that it was difficult to find developable land that was zoned for manufactured homes, given the bias that exists against these units.

Cooperative Park Ownership

Nearly three million families live in manufactured homes sited in "land-lease communities," more often called trailer parks or rental communities, where they pay a monthly ground rent to a landlord in addition to their loan payment for the unit.[10] The park owner typically provides sewerage, water, electrical systems and landscaping, and maintains the roads and other common areas.

Landlord quality is uneven in any rental housing market, but especially in manufactured housing. Tales of frequent rent increases, little or no infrastructure maintenance and excessive rules governing what tenants can and cannot do are common. Moreover, it is difficult and expensive to move a manufactured home (typically costing $1,500 to $5,000), essentially tying

[10] Homes placed in rented parks are financed as personal property because conventional single-family mortgage programs require that the land and property be bundled together to qualify. Conventional single-family mortgages also require that a home be placed on a permanent foundation; however, owners of manufactured housing cannot always afford the higher costs of a permanent foundation.

low-income and low-wealth occupants to a site. Current legislation governing rental park arrangements in some states is weak, giving tenants little recourse in the event of a park sale that will lead to eviction.

In Athens, Georgia, construction has begun on an apartment complex located on the former site of Garden Springs mobile-home park. Garden Springs was home to about a hundred predominately Hispanic families, who were notified in June 2001 that the park had been sold to a developer and that they would have to relocate within 30 days. Many residents could not afford the cost of relocation, and others were prohibited from moving by a local ordinance that forbids relocation of trailers built prior to 1977 (Gallentine 2002). Local church groups and other volunteers rallied to help the families find new housing, and plans are still underway to develop another mobile-home park. The Athens case, which is in no way exceptional, highlights the vulnerability of residents in parks, where tenure is insecure.

In some cases, park tenants have collectively purchased their community as a cooperative. These resident-owned communities allow residents to have control of their community, acquire long-term site commitments, and transform their homes into real assets. Several states have laws providing residents the right of first refusal when leased-land communities are placed on the market.[11] Currently, New Hampshire has 55 cooperatively-owned manufactured-housing parks, California has over 100, and Florida has nearly 500. The state of Vermont has directly acquired parks, through the Vermont State Housing Authority (Bradley 2000). Despite the challenges of management and finance, the benefits of this ownership structure are significant.

The New Hampshire Community Loan Fund

In the movement to convert parks to cooperative ownership, the New Hampshire Community Loan Fund (NHCLF) has demonstrated significant leadership. Established in 1983, NHCLF is a private, nonprofit organization dedicated to creating affordable housing and fostering economic opportunity for low- and moderate-income people. In 1984, NHCLF advanced $42,000 to residents of a rental park in Meredith, New Hampshire, to cooperatively purchase the park. Sixteen years later the Meredith Center Cooperative is not only still in existence but also debt-free. Building on the success of Meredith Center, NHCLF developed the Manufactured Housing Park Cooperative Program to provide technical assistance and management training to potential and current cooperative residents. The program has two objectives: to maximize resident control over mobile-home parks, and to provide membership for the entire community, regardless of income. The second objective is achieved by providing the benefits of membership to residents who pay a low down payment during the acquisition phase and pay the remainder of their membership share in monthly installments (Bradley 2000).

In 1988, NHCLF joined with the Mobile Homeowners and Tenants' Association and successfully lobbied for a law to give residents a 60-day right of first refusal to negotiate the purchase of their park in the event it is put up for sale. This important law changed the dynamic between residents and park owners. About 75 percent of the coops in New Hampshire (about 30 parks) have been acquired directly or indirectly under this law. It has also resulted in negotiated sales by owners who have called NHCLF directly once they decide to sell.

Cooperative ownership stabilizes ground rents and allows profits that once left the community to be directed toward infrastructure and other improvements. In addition, some coops have secured Community Development Block Grant or USDA Rural Development money to make important health, safety and infrastructure improvements. Cooperatively owned parks have kept rents lower than investor-owned parks (Bradley 2000). One co-op in Dover, New Hampshire, actually reduced rents by $10 over the last 13 years, while also making major sewer and road improvements. Cooperative parks have also successfully elected their residents to town boards, thereby increasing their political clout and have regular meetings with the local officials to discuss park issues (Bradley 2000).

Cooperative ownership does present a challenge to those who organize them in terms of paying for

[11] The Washington state supreme court struck down a right-of-first-refusal law as interfering with the right to sell property. New Hampshire and other states have addressed this by utilizing a 60-day notice, wherein the seller has to negotiate in good faith with tenants. States could add protections for estate owners, such as exempting transfers between related entities, restricting the provision to arms-length sales, or trigger the right of refusal only in cases where the property will no longer be used for manufactured housing (a change in use).

ongoing leadership development and management support. Enforcing standards, sustaining member involvement and collecting land rent from neighbors and friends can place pressure on cooperative boards. Some cooperatives have found it worthwhile to contract with a management company. NHCLF helps residents to develop leadership skills and is currently publishing *How To Manage a Manufactured Housing Park Cooperative*, a 300-page guide.

Private banks were initially reluctant to finance manufactured-housing park conversions; however, after NHCLF and the New Hampshire Housing Finance Authority financed several deals, the banks became convinced that it could work. The Federal Home Loan Bank of Boston instituted a fixed-rate lending program with member banks for cooperative residents to purchase parks at loan-to-value ratios of 80 percent or less. Residents contribute what equity they can, typically enough to cover some closing costs, and NHCLF makes up the difference with a fixed-rate, subordinate down-payment loan. To date no New Hampshire coop has defaulted on a loan (Bradley).

Based on the demand for homes in cooperatively owned parks, Paul Bradley, vice president of NHCLF, believes reliable and affordable fixed-rate financing would create a market in which homes will increasingly appreciate.

Developing Affordable Housing with Manufactured Units

Very few nonprofit housing organizations are discussing manufactured-housing projects, let alone developing them. However, concerns over rising land and construction costs may lead some organizations to explore alternatives to their current development practices. HomeSight, a Seattle-based CDC, is an often-cited example of just such a case. Whether the circumstances that led to their decision to use manufactured housing will lead others to follow remains to be seen, but it may be an indication that attitudes are changing and that manufactured housing has wider applications than it once did. The efforts of HomeSight, the Manufactured Housing Institute's Urban Design Project, and NHCLF's Barrington Project provide some insight into the challenges and opportunities of manufactured-housing development, particularly as it pertains to community development.

Noji Gardens

Noji Gardens is a 6.5-acre, 75-unit development of affordable-housing developed by HomeSight in southeast Seattle.[12] Between 1995 and 1999, both construction and land costs in Seattle skyrocketed, with construction costs going up at a rate of 1.0 to 1.5 percent *per month* over the entire period. Typical single-family lots, which had been priced at under $10,000 in 1995, rose to around $65,000 by 1999. HomeSight lowered its costs in a variety of ways; however, nearly every time costs were reduced, the intensifying market diminished the savings. Project economics made it increasingly hard for HomeSight to serve its target market, families earning 60 to 70 percent of area median income.[13]

HomeSight had some experience with manufactured housing through collaboration with the Snohomish County Housing Authority, in which the authority developed a manufactured-housing subdivision while HomeSight marketed the units and provided homebuyer education. Following this project, HomeSight's executive director, Dorothy Lengyel, began discussions with HUD and attended a Manufactured Housing Institute conference which discussed using manufactured housing in urban areas as a way to minimize costs.

The Manufactured Housing Institute provided technical assistance to HomeSight, and put it in touch with Schult Homes, a large manufacturer with a Marlette Homes plant in Oregon. Schult created two-story manufactured housing through an inclusionary process with HomeSight. Noji Gardens managed to avoid some of the stereotypes associated with manufactured housing because the homes look like typical, site-built Seattle homes. Most passersby do not even realize they are manufactured homes. Throughout the process, HomeSight collaborated with the city and community groups, involving them in the process to dispel fears regarding the boxy aesthetic of manufactured housing and to demonstrate the potential of two-story, modern homes. On-site finishing provided ample work for local contractors, minimizing complaints about housing produced outside Seattle.

[12] Fifty-one of the units are manufactured, while the remainder are stick-built.
[13] Area median income for a family in the Seattle MSA in 2001 was $72,200.

Flexibility on issues such as property taxes and property titles were key to the project's success. HomeSight worked closely with the city to amend its property tax abatement program to include the single-family homes at Noji Gardens, which they estimate will save buyers about $15,000 to $25,000 over a period of 10 years. Good relations with all the project partners and the community were critical to the success of the project.

HomeSight used a block grant float loan of $1.2 million at two percent from the city of Seattle, backed by a letter of credit, to secure the site. Infrastructure development was financed by a program-related investment of $500,000 at two percent from the Fannie Mae Foundation. Local Initiatives Support Corporation, through its National Community Development Initiative, provided a construction loan of $3 million at 5.8 percent interest.

HomeSight averaged savings of $10,000 to $15,000 per unit by using manufactured housing, and expects to save even more per unit in the future. For example, logistics planning was a challenge, but costs decreased as efficiencies increased. The first unit took about eight hours to set in place and cost about $2,500 due to the expense of the crane rental. More recently three units were set in four hours, costing about $600 per unit. The major sources of cost savings are labor, materials and the time of construction.

The median selling price for a single-family home in King County was $264,000 in 2001. Home prices at Noji Gardens range from $175,000 to $255,000 depending on the lot size and number of bedrooms.

HomeSight speaks enthusiastically of its first manufactured-housing project, but admits the project was complex. In-house construction management and architects, as well as significant development experience, are prerequisites to tackling a project of this scale.

Barrington Project

The New Hampshire Community Loan Fund's Manufactured Housing Park Program is currently building an affordable home-ownership project of 45 to 47 sites in Barrington, New Hampshire. The development is to be the first manufactured-housing development where all the homes receive the U.S. Environmental Protection Agency's Energy Star rating.[14] HUD's Partnership for Advancing Technology Office is funding the architect, Steven Winters Associates, a leading green architect, and the Ford Foundation funded the predevelopment.

Homes will have a variety of innovative construction features, such as advanced septic systems that emit cleaner effluent than standard systems and allow for smaller leach beds that reduce disturbance to the natural landscape, and propane heat in all homes that will eliminate both the environmental hazard created by outside oil tanks and the extra charge for kerosene in the winter. Homes will also be sited to maximize passive solar gain in winter and natural cooling in summer.

The project will be a clustered development with single-family lots as small as 10,000 square feet, or about four homes per disturbed acre. The clustered development reduces land consumption and lowers the costs of community infrastructure. Other conservation features will include a 50-foot natural buffer zone around all wetlands, and wildlife corridors providing access to and from neighboring sites, including several large conservation tracts.

NHCLF hopes to demonstrate to land-use planners, consumers and others that manufactured housing can be a good choice for affordable home ownership in an attractive, safe and green-planned community. The homes will be financed conventionally and cost between $75,000 and $100,000—impressive in a market where the median sales price is in excess of $235,000.

[14] Energy-efficient new homes that earn the Energy Star label incorporate energy savings in design and construction and use 30 percent less energy for heating, cooling and water heating than standard homes (www.epa.gov/nrgystar/newsroom/newsroom_factsheet.htm).

V. OPPORTUNITIES AND CHALLENGES FOR COMMUNITY DEVELOPMENT

To supplement the quantitative findings and case studies, anecdotal information was gathered from a variety of sources to provide a more complete picture of the opportunities and challenges of manufactured housing, as well as the range of attitudes toward it. Focus groups with community-development practitioners, lenders, manufactured-housing retailers, consumers and homebuyer-education specialists were convened to assess perceptions, knowledge and experience with manufactured housing and to begin to discern what market-based changes and improvements are needed and where policy might intervene. Guiding this research were questions related to the community-development field, namely what, if anything, should community-development corporations be doing about manufactured housing?

One of the first findings of this effort is that the term "manufactured housing" continues to confuse practitioners. The differences between trailers, mobile homes, modular housing and manufactured housing are not easily explained by referring to the performance standards and specifications of the HUD code. The legacy of early mobile homes endures in the negative perceptions of manufactured housing today. Modular and panelized housing elicit more positive reactions and are perceived to be a more acceptable housing choice, despite being such a small portion of housing starts (less than five percent in 2001). Uncertainty persists as to how, if at all, manufactured homes have changed—even if the families occupying them have.

Second, focus-group participants revealed that this market should not be divided into pre- and post-HUD code, as is sometimes assumed by housing economists. Moreover, the tendency to discount the importance of older, low-value units is misleading, as these units are so crucial to low-income housing. The market can be divided into three distinct segments:

(see chart above)

Market Type	Location	Issues and Concerns	Significance
Leasehold Communities (Parks) **(typically single-section)**	Rural and Suburban	• Escalating land rent • Quality of park management • Cost of personal-property loans • Unsafe, aging units with difficult repairs • Location and amenities • Right of first refusal - coop conversions • State laws prohibiting real estate loans • ALTA titling regulations	• Entry-level housing stock • Only affordable rental option in some markets • Offers principal pay-down and space control for tenant not available in apartments • Critical for low-income families
Affordable HUD-Code Units on Owned Land **(mix of single-and double wide)**	Primarily Rural	• Quality and design of units • Cost of personal-property loans • Aging units with difficult repairs • Restrictive zoning • Utility hook-ups • State laws prohibiting real estate loans • Titling on family-owned land • Initial remedial aesthetics vs. affordability • Predatory lending • Uneven appraisal process • Installation and foundation standards • Unfair retailer practices	• Entry-level owner-occupied housing stock • Only way to develop units in some markets due to lack of contractors • Critical for young working families and single-parent households
Newly Placed Factory-Built Units (multisection)	Urban and Suburban, Upscale Rural (metro fringe, resorts)	• Design • Lending and appraisals • Restrictive zoning • Resolving code differences • Installation standards	• Cost-effective, owner-occupied unit development • Fast and secure infill option • Fills gap left by site-builders' movement upscale

Third, attitudes among practitioners are mixed. Perceptions can be characterized along a continuum of:

Industry Advocates

Acknowledge that the industry has made mistakes, but believe the scale and market acceptance can not be ignored. Advocates often view manufactured housing as a building process, rather than as an industry as a whole. This allows them to look beyond the problems in certain sectors, such as finance or installation, to the potential that technology offers on the production side. Advocates often proactively suggest innovations

in design, zoning and finance. They frequently cite the cost advantages that the technology offers, but in an eagerness to shake the trailer-park stigma, they can forget the importance of single-sections in parks for low-income families. This segment seems to rely more for solutions to housing issues on market forces rather than regulatory responses, and views manufactured housing as a housing-policy issue.

Skeptics

Wary of the industry based on past product design and performance, lending practices and questions related to depreciation. Skeptics pragmatically acknowledge that manufactured housing is a neglected issue that deserves attention, but are unsure of how to analyze the issues. Finance, titling, tenant protections, design, installation standards and materials quality are major concerns, as well as local economic impact and political ramifications for unions and local government. Concerns over community development and revitalization often conflict with a desire for affordability. Resistance tends to decrease when they are introduced to the range of high-quality manufactured-housing units currently available, though often with reservations. Community-development entities tend to be in this category.

Antagonists

Burned by shoddy products, troubled by the prevalence of unsightly units in the landscape, and bruised by powerful industry lobbyists, this group views manufactured housing as a destructive force in low-income communities. Antagonists are highly critical and suspicious of the industry; they respond to claims that it has changed with even greater condemnation. Antagonists charge that so long as some manufacturers continue to turn a blind eye to problematic financing, installation and sales practices, they are complicit in this destructive force. Often the sense is that manufacturers, lenders, retailers and park owners have taken advantage of low-income people in such a deceptive way that they should be shut down the same way that producers of fraudulent consumer products have to pull their products from the market. This group tends to gravitate toward regulatory and government remedies, and sees this as a consumer-protection issue or associated with continuing "War on Poverty" work in rural communities. Homebuilders and union members, due to concerns about competition and reduced job opportunities, are often members of this group.

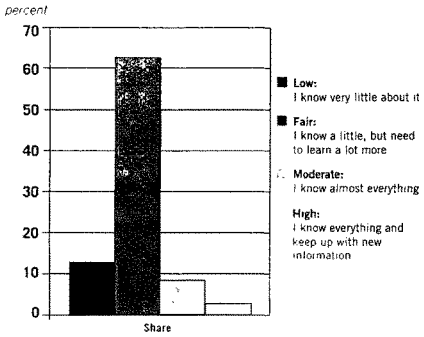
Role for Community-Development Entities

Very few nonprofit organizations are involved with manufactured housing in the areas of development, lending, consumer education and counseling, or park ownership and management. Organizations with programs targeted at manufactured units rarely highlight this work; some only shared their experiences after it was clear such programs were not going to be criticized. Few practitioners embrace all aspects of the manufactured-housing industry, but more are beginning to advocate for product improvements or better financing terms. Others are exploring using manufactured units in their developments or adding sections to homebuyer-education classes on how to buy a manufactured home. Overall, however, community-development practitioners have much to learn, at least based on the results of a Neighborhood Reinvestment survey in February 2002 (Figure 12). Most of those surveyed suggested they knew a great deal about affordable housing issues, but very little about factory-built housing.

Possible roles for community-development entities include:

- owner or manager of traditional leasehold community;

Figure 12: Community-Development Professionals' Knowledge Level Regarding Factory-Built Housing



Source: Neighborhood Reinvestment Survey of 120 professionals nationally

- source of technical assistance or loans to convert leasehold communities into resident-owned cooperatives;
- designer of innovative loan products in partnerships with housing finance agencies and local lenders for the purchase, refinance, improvement and resale of units;
- developer of replacement or recycling programs for severely dilapidated units;
- upgrader of existing units, using HOME and CDBG funds, to better blend into community setting;
- developer of subdivisions of new owner-occupied manufactured housing;
- developer of innovatively designed factory-built units placed in scattered-site infill projects;
- provider of prepurchase homebuyer education and counseling directed at manufactured-home consumers;
- provider of home-improvement and repair loans for personal-property titled units;
- owner or manager of a factory to build housing as an economic-development program;
- advocate for fair housing compliance; or
- advocate for appropriate state and local oversight and regulation, consistent with 2000 law.

Persistent Issues of Concern

Several issues were raised repeatedly in interviews and focus groups across the country:

Finance

The process and cost of securing a loan to purchase a new HUD-code home is well established, and it is evolving to more closely mirror conventional lending. Loans for homes titled as personal property continue to carry increased collateral and default risk, although recent regulations regarding installation and leasehold mortgage loans may begin to address this issue. The most significant shortfall is in the financing of an existing unit for resale, refinance, and renovation or repair. Few lenders are active in these markets.

Repossessions

The market is flooded with repossessed units, which presents opportunities for acquiring low-cost units, but also perpetuates the perceived risks of owning and lending on HUD-code units.

Retailers

Many retailers do add value to the transaction, similarly to a general contractor in a site-built development. However, retailers shirking responsibility for installation problems and rushing contracts are often cited as problems, although new federal requirements for installation standards, installer licensing and dispute resolution should begin to address this. A lack of transparency in pricing and the lack of a public record of sales prices need to be addressed.

HUD-Code Standards

Some newer units with poor materials and workmanship seem to be slipping through. However, it is not clear that this proves that the HUD code is inferior. It is more likely that homes are approved that do not meet the standards. Better monitoring and code enforcement is required.

Rental Park Communities

While land ownership is a preferred arrangement, many households cannot afford land, and will continue to opt instead for rental park communities. New mortgage products do seem to be pushing landlords to extend lease agreements, and state laws offering increased tenant protections are promising. Who owns and controls the land is a critical factor in the quality of life for low-income households, since each new park investor will finance a higher purchase price, which the tenants will ultimately pay for. Cooperative ownership removes the park from the speculative market.

State and Local Regulations

State laws prohibiting HUD-code units from being titled as real estate are a major obstacle. However, most of the 16 states that do this are considering legislation to conform to real estate titling. Zoning and code rules continue to be a major barrier. Factories are increasingly building units to match the needs of localities, rather than trying to bend regulations. However, the vast majority of local governments continue to discriminate against manufactured housing, thereby limiting its potential to meet the need for affordable housing.

Homebuyer Education

Consumers of manufactured housing are not well informed before, during or after the purchase process. They also lack funds to pay for counseling or group classes. Nonprofits play a key role, but reaching consumers before the purchase—before they walk onto a retailer's lot—is a challenge.

CONCLUSION: THE CHALLENGES THAT REMAIN

Recognizing the advantages of lower production costs inherent in manufacturing housing, the challenge for advocates is to work to capture these production efficiencies for the advantage of lower-income clientele. First and foremost, advocates must push for rationalization of the finance process and expansion of options intended to afford manufactured-home purchasers access to credit on the best terms for which they qualify. In addition, state and local installation standards must be made more rigorous and subject to better enforcement, to ensure that the useful life of manufactured homes and the flow of housing services they generate is extended. Similarly, land-use controls must be reformed in order to allow manufactured homes to be placed on lots in a wide range of communities so that owners of manufactured homes are able to reap the equity build-up associated with land ownership. Finally, designers and planners must continue to advocate for manufactured-housing units and subdivisions as acceptable alternatives to site-built housing, while maintaining the affordability advantages that still lie at the heart of the product's market appeal.

Even while working to expand acquisition and financing of new manufactured homes on owned land, equal effort must be devoted to addressing the difficult conditions of many lower-income people— owners and renters alike—living in older, and often deteriorating, mobile homes. While a few of these families and individuals could be relocated to new and better quality homes with the help of existing government subsidies, resource limitations at the state and federal level suggest the urgency of devising cost-effective methods to eliminate both pressing health and safety problems, and upgrading or rehabilitating this very affordable element of the nation's housing inventory.

Although there is a growing body of research on the advantages of manufactured housing, policies and practices in support of it are lacking. A coherent national agenda using both market-based and policy strategies is need to implement the promising efforts that have transformed local markets. Community-development entities can and should play an important role in the dialogue going forward.

There are at least seven reasons community-development practitioners should re-examine their long-held beliefs regarding factory-build housing:

1. New designs offer styles and quality almost indistinguishable from site-built units, at a lower cost.
2. Manufactured unit sales and placements have experienced high growth rates in almost every region of the country.
3. Manufactured units play a growing role in expanding home ownership for low-income and first-time buyers, and play a crucial role in providing affordable rental markets to extremely low-income families.
4. New legislation passed in 2000 requires involvement at the state and local levels in setting standards and oversight of the HUD code.
5. Efforts are being made at reforming the finance of manufactured units, stemming from the collapse of major specialists in this arena; state housing finance agencies and the secondary market are coming up with innovative financing options.
6. Efforts are being made by the industry to change its methods, its image and generally improve its products and delivery system. The recent down turn in the industry has forced it to become more aware of its need to work collaboratively in a variety of environments.
7. There are emerging, exciting models of community-development organizations that have successfully developed programs which overcome some of the historic failings of this housing market.

Practitioners interested in serving low-income communities and families needs to overcome historic biases and resentments towards the industry and take leadership of the future of manufactured housing.

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APPENDIX

Focus Groups Held by Neighborhood Reinvestment

Place	Date	Audience	Number Attending
Las Vegas, NV	May 2001	Executive Directors	18
Washington, DC	August 2001	Homebuyer Counselors	15
Memphis, TN	October 2001	Lenders, Developers, Rural Development Staff, HFA Staff	12
Philadelphia, MS	January 2002	Lenders, Nonprofits, HFA Staff	20
Santa Fe, NM	January 2002	Lenders, Real Estate Brokers, Appraisers, Potential Buyers, Existing Owners	32
Atlanta, GA	February 2002	All of the above	130

Selected Data from the 1999 American Housing Survey Published Tables

Year Structure Built, Owner-Occupied Units (AHS Table 3-1)

	All Owner Occupied	% All Owner Occupied	Mobile Homes	% of All Mobile Homes
1995 to 1999	6,040	9%	1,352	24%
1990 to 1994	5,234	8%	880	16%
1985 to 1989	5,283	8%	631	11%
1980 to 1984	4,297	6%	657	12%
1975 to 1979	7,053	10%	791	14%
1970 to 1974	6,218	9%	810	14%
1960 to 1969	9,483	14%	417	7%
1950 to 1959	8,919	13%	74	1%
1940 to 1949	4,721	7%	10	0%
1930 to 1939	3,387	5%	27	0%
1920 to 1929	2,896	4%	0	0%
1919 or earlier	5,264	8%	0	0%
Median	1969		1985	

Source: American Housing Survey. Data available online at www.census.gov/hhes/www/ahs.html.

Mobile Home Location, Owner-Occupied Units (AHS Table 3-1)

Location	Units	% Total
Inside Metropolitan Statistical Area	2,854	51%
* Central Cities	269	5%
* Suburbs	2,585	46%
Outside Metropolitan Statistical Area	2,795	49%
Total	5,649	100%

Source: American Housing Survey. Data available online at www.census.gov/hhes/www/ahs.html.

Mobile Home Placements in Groups (AHS Table 3-8)

Number in Group	Units	Percent
1 to 6	3,711	66%
7 to 20	235	4%
21 or more	1,704	30%

Source: American Housing Survey. Data available online at www.census.gov/hhes/www/ahs.html.

Mobile Home Site Placements (AHS Table 3-2)

	Units	Percent
First Site	3,869	68%
Moved from another site	1,089	19%
Don't know	370	7%
Not reported	321	65

* Occupied Units Only, number in thousands.
Total mobile homes = 5,649

Source: American Housing Survey. Data available online at www.census.gov/hhes/www/ahs.html.

Current Mortgage Interest Rate (AHS Table 3-15)

	Total	New Construction 4 Years	% of All New Construction	Mobile Homes	% of All Mobile Homes
Less than 6%	897	65	2%	61	3%
6 to 7.9%	24,918	2,644	70%	848	35%
8 to 9.9%	10,316	745	20%	848	35%
10 to 11.9%	1,876	196	5%	375	16%
12 to 13.9%	606	57	2%	169	7%
14 to 15.9%	138	36	1%	55	2%
16 to 17.9%	47	19	1%	24	1%
18 to 19.9%	70	5	0%	17	1%
20% or more	16	13	0%	13	1%
Not reported	0	0	0%	0	0%
Median	**7.5**	**7.4**		**8.7**	

Source: American Housing Survey. Data available online at www.census.gov/hhes/www/ahs.html.

Term of Primary Mortgage at Origination or Assumption

	Total	New Construction 4 Years	% of All New Construction	Mobile Homes	% of All Mobile Homes
Less than 8 years	1,020	106	3%	310	13%
8 to 12 years	1,353	94	2%	296	12%
13 to 17 years	8,008	589	16%	717	30%
18 to 22 years	2,604	362	10%	405	17%
23 to 27 years	1,362	130	3%	113	5%
28 to 32 years	23,238	2,431	64%	488	20%
33 years or more	860	22	1%	13	1%
Variable	438	45	1%	66	3%
Median	**29**	**7.4**	**29**	**16**	**16**

Source: American Housing Survey. Data available online at www.census.gov/hhes/www/ahs.html.

LITERATURE REVIEW

I. COMMUNITIES

[DESIGN, MANAGEMENT, OWNERSHIP AND CONDITIONS]

Allen, George F.
1998. Managing the manufactured housing community. *Journal of Property Management* 53(3):42.
Managing manufactured-housing communities can be challenging. While older manufactured-housing communities had small lots and predictable design, newer sites feature curved streets and angled home sites. Property managers must also maintain common areas and supply water, sewer, electricity and heating fuel to residents. Other challenges include the tendency for manufactured-housing communities to be more regulated than apartment complexes and the strong territorial feelings many manufactured-home residents may develop. Management income is generated from base rent, per-capita charges, service and home repair.

Bergman, David
1991. New visions for manufactured housing. *Urban Land* 50(11):36-37.
Bergman discusses an infill project in Oakland, California, that achieved 17.5 units per acre with lots perpendicular to the street and using zero-lot-line placement, emphasizing that site placement is the key to making an attractive community. Using different retailers who buy from different manufacturers can help the community to look less homogeneous. Bergman advocates for local planning and zoning officials to be more open-minded to possibilities for inner-city infill housing projects.

Bradley, Paul
2000. Manufactured housing park cooperatives in New Hampshire: An enterprising solution to the complex problems of owning a home on rented land. *Cooperative Housing Journal* 22-32.
The article describes the infrastructure in New Hampshire that led to and supports the current trend of converting manufactured-housing parks to cooperatives, the structure and financing vehicles employed, the benefits and challenges of cooperative ownership, and a vision for a cooperative manufactured-housing park system in New Hampshire.

Gentry, Carol
1999. Mobile-home residents find strength in numbers. *The Wall Street Journal* September 8.
This short article describes the formation of cooperatives by owners of manufactured homes in New Hampshire. Several quotes in the article support the argument that a co-op is a better deal than a traditional rental arrangement.

Halpern, Sue
2001. The trailer park revolution. *Mother Jones* May/June.
"Owners of what used to be called 'mobile homes' are forming cooperatives—putting landlords and lenders on notice that they're not going anywhere." This short article includes quotes from several co-op members and mobile-home owners, describing this arrangement as a way to make ownership possible for people who otherwise could not afford it.

Manufactured Housing Institute
1999. *Play It Safe: How to Safeguard Your Community, Save Lives and Minimize Damage From Disasters.*
This resource provides managers and residents of manufactured-home communities with the information they need to work together to develop and implement a disaster plan that is up-to-date, realistic and tailored to specific community needs. It provides relevant information on all the different types of natural and manmade problems that can affect a community, and offers concrete steps to minimize the impact these disasters can inflict. Topics range from organizing a residents' disaster-planning committee, to what needs to be included in emergency supplies, to what to do with family pets during times of disaster.

Rowe, Randall K.
1998. Investing in manufactured housing communities. *Urban Land* 57(6):80-81.
The 1993 initial public offering of a Manufactured Housing Community led to three public offerings, leading many to question whether these manufactured-housing REITs were an appropriate investment.

Positive attributes (most stated in comparison to ownership or investment in an apartment complex):

- Low maintenance: Homeowners are responsible for all maintenance on their homes. When the home is sold, arrangement for repainting or other repairs are made between the buyer and the seller.
- Stable rent stream: Because homeowners are responsible for all the maintenance on the properties, downtime is minimal at the time of turnover and there is less chance of a month of lost income.
- Low turnover rates: Two to four percent average, compared to over 50 percent for an apartment complex.

Negatives:

- Small size: Fewer than 40 owners own more than 3,000 home sites each, which means the majority are small portfolios. They typically trade for prices between $2 and $10 million, with relatively high transaction costs.
- Fragmented ownership: Many owners, few with really big holdings.
- Potential obsolescence: Many of the old communities contain only single-section units, and are soon to be in need of updating. Redevelopment and reconfiguration to accommodate multisection homes will be costly.
- Communities take much longer to stabilize (four to eight years) than apartments (generally less than one year).

Sanders, Welford
1993. *Manufactured Housing Site Development Guide.* Chicago: Manufactured Housing Institute and the American Planning Association.
This guide is intended to help builders and developers interested in developing manufactured-home communities understand the latest trends. It covers the entire development process, from initial project planning and feasibility analysis, to project financing, regulatory concerns, home design, proper siting techniques and marketing. Case studies of successful manufactured-home communities are used to identify effective product design and development standards.

Warner, Kate and Robert Johnson
1993. *Manufactured Housing Research Project.* Ann Arbor, MI: University of Michigan.
***Report 4: Manufactured Housing Impacts on Adjacent Property Values,* Kate Warner and Jeff Scheuer.**
The report focuses particularly on manufactured-home rental communities (parks). It is mainly a review of existing studies, supplemented with three case-study comparisons. It concludes that rental manufactured-home communities do not appear to have a significant positive or negative effect on adjacent residential property values, in terms of the private market or in terms of how public tax-assessment officials established valuation levels.

The case studies include two in which subdivisions were developed after the manufactured-home park had been developed, and one where the park development occurred after that of the site-built residential subdivision. The researchers looked at the percent change in average sales prices of homes sold in the adjacent subdivisions over a five- to six-year period, and compared this with homes sold in comparable subdivisions not near manufactured-home parks, or homes located in the case-study subdivision but not near the park.

***Report 6: Alternative Ownership and Innovative Uses,* Kate Warner and Victoria Basolo.**
In describing alternative ownership, state and local governments, usually in concert with community nonprofit groups, have facilitated the purchase of manufactured-home parks by residents or a public or quasi-public entity. Ownership of the parks could be in a cooperative form, as illustrated by the Colorado example, or could involve individual resident purchases of park lots through a lease-purchase program.

Manufactured housing is not just restricted to rental communities or rural sites. Innovative uses include manufactured-home subdivisions, projects with a mix of manufactured and site-built homes, urban infill development, and the use of manufactured homes in rural areas to replace homes where the homeowner owns the land but cannot afford to replace the structure.

The report stresses that manufactured housing plays a key role in the provision of affordable housing in a number of communities.

II. DEMOGRAPHICS

[OCCUPANTS, GEOGRAPHIC AREAS, CONSUMER SATISFACTION]

American Association of Retired Persons.
1999. *National Survey of Mobile Home Owners.* Washington, DC: National Family Opinion Research for AARP.
A survey of 933 mobile-home owners who had purchased new mobile homes within the past eight years was conducted to document the extent to which homeowners have experienced problems with the construction and/or installation of their mobile homes, and to explore how they dealt with and resolved these problems. Structural and installation problems appear to be pervasive, with only a few attributed to daily wear and tear by the owners. The data suggests that although most problems emerge within the first year of ownership, while warranty coverage is still in effect, many people have difficulty invoking warranties for various reasons. Those surveyed did not seem

very critical of the structure of their homes, but satisfaction with construction dropped dramatically when problems appear. Findings included:

- 77 percent of mobile-home owners reported at least one problem with the construction, installation, systems or appliances of their homes.
- The most frequently named problems were improper fit in doors or windows, interior fit or finish, and problems with actual construction, such as cracks or separation of walls.
- 61 percent of the problems of greatest concern occurred during the first year of ownership.
- 81 percent of homes were installed on blocks or piers with anchors or tie-downs.
- 15 percent experienced problems with set-up or installation of their homes, this more frequently occurring in newer and more expensive homes.
- About half of the problems of most concern led to out-of-pocket expenses to homeowners, which aver aged $1,140.
- Homeowners were unsuccessful in their attempts to use warranties to resolve problems 40 percent of the time, while about 35 percent of the problems of most concern were repaired under warranty.
- Homeowners' satisfaction with the quality of construction of their homes averaged 4.0 on a 5 point scale where 5 is highest.
- About half of all problems reported had less-than-satisfactory outcomes in attempts to resolve them.

Beamish, Julia O., et al.
2001. Not a trailer anymore: Perceptions of manufactured housing. *Housing Policy Debate* 12(2):373-392.
This article reports on a statewide study that profiled Virginia residents of single- and double-section manufactured housing, and compared their perceptions with the perceptions of other community residents. The authors found that:

- Double-section residents had more education and higher incomes and were more likely to own their home and its land than were single-section residents.
- Community residents had persistently negative opinions about the impact of manufactured housing on their community, and these perceptions tended to be based on older stock than on newer, multisection stock that was harder to differentiate from site-built housing.

Canner, Glenn B., Wayne Passmore and Elizabeth Laderman **1999. The role of specialized lenders in extending mortgages to lower-income and minority homebuyers. *Federal Reserve Bulletin* November.**
The specialized mortgage lenders in the title consist of prime, subprime and manufactured-home lenders. The article describes a shift in credit toward lower-income and minority borrowers due to the expansion of activity by subprime and manufactured-home lenders. Graphs show changes in borrower and applicant characteristics over time.

Foremost Insurance Group of Companies
1999. *The Market Facts*. Caledonia, MI: Foremost Insurance Group.
This study contains data compiled from a survey about who owns manufactured homes, how and where they live, finding that the average owner is 53 years old, married, employed and has an income of $26,900. The study includes data on age, income, household size, music and reading preferences, perceptions of manufactured homes and of the features and value of manufactured homes.

Geisler, Charles C. and Hisayoshi Mitsuda
1987. Mobile-home growth, regulation, and discrimination in upstate New York. *Rural Sociology* 52(4):532-543.
The recent surge in manufactured housing within the nation's rural housing stock reflects the accelerating costs of single-home alternatives in the U.S. In both 1970 and 1980, mobile-home growth in rural areas surpassed that in urban areas. This paper uses 1980 census data and current zoning ordinance listings for 92 towns in northern New York state to examine the influence of community social-class composition on discrimination against such housing. The positive influence of population growth on mobile-home occurrence is shown to be conditioned by intercommunity social-class composition. Social class overshadows population pressure as a factor contributing to the formal regulation of mobile homes.

Hill, Ingrid
1999. A poetics of trailer park class. *Peace Review* 11(2):225-230.
This article discusses social changes in the evolution of "trailer living." While post-World War II trailers were tiny, today's manufactured housing units are larger and look more like site-built homes. Trailer parks have given way to mobile-home "villages." Costs and features of manufactured homes are discussed. The author asserts that today's manufactured-home occupants are mostly divorced women and their children who suffer from personal and financial dislocation, similar to post-WWII trailer occupants.

Housing Assistance Council
1996. *Manufactured Housing in Nonmetropolitan Areas:* A Data Review. Washington, DC: Housing Assistance Council.
This study examines available data on manufactured homes and their occupants in nonmetropolitan areas in the U.S. It includes data on economic characteristics of residents, comparative costs of manufactured housing, consumer satisfaction with manufactured homes and neighborhood opinion data. It concludes with recommendations for further research.

Jovan, Wendy and W. Benoy Joseph
1997. Industry corner: The outlook for manufactured housing in the United States. *Business Economics* July.
The article describes the increasing design options and appeal of manufactured homes among both low-income buyers and more affluent empty nesters and retirees. It discusses the areas of high demand for manufactured housing and its market share.

The authors predicted that due to rising lumber and labor costs, manufactured-housing costs would rise an average of 3 percent annually from 1996 to 2001, compared to a projected 4 percent annual increase for conventional housing.

Installation costs are significantly higher for a multisection home than a single-section one, due to the added complexity of joining the sections and the connection of the wiring between the floors. Average square footage of a multisection home was predicted to rise to over 1,700 square feet by 2001.

In 1996, individuals earning over $40,000 accounted for 20 percent of the market share and represented the fastest-growing income group for the industry. The South is the largest and strongest regional market for manufactured housing, due in part to more favorable zoning laws; rising labor and materials costs which can be controlled somewhat in the factory setting; and population demographics (such as lower incomes, retirees and buyers of second homes).

The top eight producers account for 65 percent of all sales. They are Fleetwood Enterprises, Champion Enterprises, Oakwood Homes, Clayton Homes, Skyline, Schult Homes, Cavalier Homes and Fairmont Homes. There has been considerable consolidation activity that has increased market domination. Because low price is the primary competitive advantage, big producers are favored because they can negotiate for lower materials costs by buying in high volume.

The retail end, on the other hand, is highly fragmented, with an estimated 6,000 retailers, though increasingly manufacturers are attempting to gain greater control of a market by controlling the retail end as well. In 1996, eight states (Alabama, Florida, Georgia, Mississippi, North Carolina, South Carolina, Tennessee and Texas) accounted for 5,000 retailers. Retailers typically own the units and then sell them to buyers. They often prepare the land and provide the installation, and many provide financing as well.

Kochera, Andrew
2001. *Issues in Manufactured Housing.* Washington, DC: Public Policy Institute, American Association of Retired Persons.
This brief report (available online at research.aarp.org) outlines the significance of manufactured homes as a source of housing for people age 50 and older, and also discusses construction and safety standards, as well as practices in manufactured-home parks.

In 1999, about 6.8 million manufactured homes were occupied as primary residences, around 2.8 million (41 percent) of which were owned or rented by a person age 50 or older. Nearly 750,000 had a household head between 65 and 74 years old, while 620,000 had household heads over 75. Thirty-nine percent of these 50-plus households were single-person households. In addition, about 1 million manufactured homes were held as a second home in 1999; about two-thirds of these were owned by a person aged 50 or older. In 1999, 348,000 manufactured homes were purchased, representing about 19 percent of all new, single-family housing. About 31 percent of these new manufactured homes were purchased by someone age 50 or older.

The median income for 50-plus households in manufactured homes was around $20,000. Limited financial resources make residents of manufactured housing particularly vulnerable to increases in park rents and unexpected home-repair costs. Manufactured homes are typically smaller and less expensive than site-built housing: the median size for a manufactured home owned by a 50-plus person was around 1,000 square feet in 1999. The most commonly cited reason that 50-plus purchasers chose a manufactured home was "financial."

Older residents are more likely to own and live in the South; 91 percent of 50-plus households living in a manufactured home are owners and 52 percent lived in the South. Forty-seven percent of 50-plus owners of manufactured homes were located outside of metropolitan

areas, compared to 27 percent of 50-plus owners of conventional, single-family homes. About 44 percent of manufactured-home owners aged 50 and older reside in a manufactured-home park.

So-called "mobile homes" typically do not move again once they leave the dealer's lot. Moving them is expensive and can cause extensive damage. It is also difficult for residents of manufactured-home parks to find alternative space to rent. Consequently, manufactured-home owners who rent lots in parks find it very difficult to move when a landlord engages in unfair practices. Unfair practices may include frequent or excessive rent increases, inadequate park maintenance, requirement that residents buy from a certain home dealer, lack of a written or long-term lease and unreasonable park rules. State legal protections for residents vary widely, and at least 15 states have no manufactured-home statutes at all.

Luken, Paul C. and Suzanne Vaughan
1999. Community Development on Wheels. Paper presented at the Society for the Study of Social Problems.
Oral histories of two women's experiences of buying, moving to and living in mobile homes, along with contextual materials on manufactured housing, is used to document one aspect of the transformation of the housing institution under late capitalism. The paper's objective is to demonstrate institutional ethnography as a method for documenting the changing gender, class and race relations within the institution of housing in the twentieth-century U.S.

Owens, W. Joseph
1996. Who's buying manufactured homes? *Urban Land* 55(1):21-23.
Manufactured-housing buyers are no longer conforming to the cliché "newly wed or nearly dead." This is due in part to housing that provides a better range of options and is bigger, but with a price tag that gives it a competitive advantage over site-built homes. For impatient buyers, another benefit of the manufactured home is the quick move-in time. For similarly priced homes, the manufactured home will almost certainly be ready for occupation before the site-built one.

Secomb, Dorothy Margaret
2001. Retirement in mobile and manufactured housing on the north coast of New South Wales, Australia. Dissertation, University of New South Wales. *Dissertation Abstracts International* 62(1):345-A.
The study considers four relocatable home environments as alternative housing for retirees: caravan parks, mobile homes in mixed parks, manufactured homes in mixed parks and manufactured-housing estates. Data is based on 778 questionnaires completed by residents of 34 parks/estates, and additional interviews and case studies. The results suggest that residents of relocatable homes tend to retain affiliation with organizations joined prior to relocation and are not reliant on their new neighbors to integrate in their communities. Residential satisfaction was most influenced by interactions and perceptions of residents; psychological adjustment is influenced by a positive attitude toward self and neighbors. Internal dwelling space affected satisfaction, adjustment and community integration. External space affected privacy and safety.

Shelton, Gladys G. and Kenneth J Gruber
1997. The Perceived Demand for Manufactured Housing in Nonmetropolitan Communities in North Carolina. Paper presented at the Southern Rural Sociological Association.
This paper surveyed 303 local community officials and housing professionals in 87 nonmetropolitan communities in North Carolina regarding their perceptions of the role of manufactured housing in their communities. Survey results indicated that communities with unfavorable zoning conditions tended to report less demand for existing manufactured housing than favorable-zoning communities. However, both types of communities showed a similar receptiveness to manufactured housing. Unfavorable zoning did not seem to reflect attitudes of local officials or indicate a barrier to manufactured housing as affordable housing.

Turner, Carolyn S. and Gladys Vaughn
1998. Satisfaction with manufactured housing. *Journal of Family and Consumer Sciences* Fall.
This study compared characteristics of residents of single-section and double-section homes and their satisfaction with their units. The study included six rural counties representing three regions in North Carolina. Respondents included 158 single-section occupants and 115 double-section occupants. Analysis revealed that single-section residents had lower incomes, were younger, tended to rent the units, and lived in older units. Double-section residents reported significantly higher satisfaction with space, design and ease of use. Both groups of residents reported high satisfaction with outside appearance, layout and design, and overall space of their units. Areas of concern for both groups of residents were storm safety, storage space and durability of the units.

Warner, Kate and Robert Johnson
1993. *Manufactured Housing Research Project.* Ann Arbor, MI: University of Michigan.
Report 5: Manufactured Housing and the Senior Population, Kate Warner and Azza Eleishe.
This report examines the size and characteristics of the senior population nationally and in Michigan, and sets out the common housing needs and design requirements of the older population. It then describes a survey conducted in one of Michigan's manufactured-home communities for seniors, designed to evaluate how well manufactured homes and senior manufactured-home rental communities were meeting the needs of the seniors living in them. Resident evaluations were found to be positive with regard to the locational and neighborhood qualities of the manufactured-home community. Residents' greatest worries were economic, particularly increasing lot rents and the values of their homes for resale.

Which of these Homes is a Manufactured Home?
1998. Washington, DC: Fannie Mae.
Currently, about 50 percent of buyers of manufactured housing also own their lots. In 1997, almost one in four single-family housing starts was manufactured housing. Most homes come with a warranty ranging from 12 to 60 months, depending on the manufacturer. In 1996 the total economic impact from manufactured housing was $32 billion. Five states (Alabama, Georgia, Indiana, North Carolina and Texas) received over $2.5 billion each in economic impact.

The report cites a study conducted in Petaluma, CA, that compared the cost of building a 1,250-square-foot, single-family unit with the same materials in a factory versus on-site. They found that manufactured housing had a 20 percent lower cost per square foot. The costs accounted for in the study included all installation, transportation, foundation, land-developer overhead, financing and management fees, marketing, landscaping, driveways, walks and site construction of a garage.

III. DESIGN

[AESTHETICS, INNOVATIONS, ENGINEERING]

Blair, John
2001. PATH Ways. *Urban Land* 58(3):78-79, 82-83.
Advances in manufactured housing have come to the attention of a new federal program, the Partnership for Advancing Technology in Housing (PATH), a public-private initiative to expand development and use of new technologies to improve safety, durability, comfort, maintenance and efficiency of American homes. PATH unites several federal agencies and is charged with identifying and publicizing innovation in the homebuilding industry, testing new housing technologies in the field, and promoting development of housing technology through research. The Manufactured Housing Institute (MHI) is a member of PATH's coordinating council, which is made up of housing organizations. Several manufactured-housing technologies and models are featured in the PATH program's best practices: a self-contained heat pump/air handler, new foundation systems, tilt-up roof technology, and other features that have demonstrated that HUD-code housing can be as appealing as site-built housing. Lido Homes in Newport Beach, CA, and New Colony Village in Jessup, MD, are featured as manufactured-housing sites used as models by PATH. The author is PATH's director of communication and concludes by saying that the manufacturing-housing industry has a lot to gain from working with PATH.

Burns, Carol
2001. It's not your father's trailer anymore. *Architecture Boston* 4(1):34-35.
This short article provides a brief overview of the evolution of manufactured housing. The author argues that compared to mobile homes of the past, manufactured-homes units built today vary widely in appearance, can look just like site-built housing, are comparable to site-built homes in terms of maintenance, wind safety, fire safety and thermal efficiency, and appeal to diverse household types seeking affordability. "Recognized as a realistic option by both those who build them and those who buy them, manufactured housing continues to become evermore indistinguishable from conventional dwellings," Burns asserts. Interesting facts pointed out include:

- Manufactured homes comprise 25 percent of new homes, and are one of the fastest-growing segments of the U.S. housing market.
- They are only types of housing that is built in compliance with a federal building code that pre-empts state and local codes.

Burns, Carol and studio students
1996. *A Manufactured Housing Catalog.* Cambridge, MA: Harvard University Graduate School of Design. (Studio catalog and Web site designed by Charlie Cannon.)
This advanced design studio, sponsored by the Joint Center for Housing Studies, addressed physical design, communicable knowledge and informational expertise.

The Web site and catalog include an illustrated timeline of the evolution of manufactured housing and asserts that manufactured housing should be regarded as a genuine housing innovation that satisfies real needs in twentieth-century America.

Coaldrake, William H.
1987. Manufactured housing: The new Japanese vernacular. *The Japan Architect* 62(1):58-62.
Coaldrake asserts that conditions peculiar to the Japanese economy and environment stimulated the development of industrialized technologies in housing, and that this development has really been a combination of new tradition and old technology. Coaldrake concludes this series of studies by saying that "solutions to the problem of how to produce safe, durable, affordable houses range from closed system rigid-frame factory prefabricated units to open systems made of steel frames clad with wood or lightweight ceramic panels, to structural panel construction." He discusses the potential for export of these ideas, using the automobile industry as a possible model for housing exports, with local factories producing components appropriate for the region, and standardized main components shipped from Japanese factories. He believes manufactured homes are part of the new vernacular of postindustrial society and that the Japanese industry is built upon a firm industrial base, dedication to customer service and the need to compete in the world economy.

Dean, Edward
1984. The new foreign import: Manufactured housing systems. *Journal of Architectural Education.* 37(3&4):12-19.
Dean expresses concern for the housing crisis in the U.S., but maintains that methods of producing and constructing housing have not changed for 30 years; expensive, labor-intensive, energy-inefficient techniques are still used. He states an objective of developing a housing-construction process which minimizes costs in labor and time, minimizes prices of competed units, uses high-quality materials and construction, is energy efficient, achieves good indoor air quality and is an adaptable and variable system. Dean then states that these objectives have already been achieved by a numbers of foreign countries, including Sweden, Denmark, Finland and Japan. He then details the innovations and development of the Swedish manufactured-housing system, particularly the Borohus modular-design system.

Grogan, Bradley C.
1999. Curb appeal. *Urban Land* 58(3):70-73, 80-81.
Two-thirds of manufactured homes are being sited on private lots rather than in rental parks. Many exteriors are enhanced on-site. In Texas, for example, it is common to apply a brick faáade. Roof tiles are also frequently applied on-site. The innovation of hinging the roof results in more traditional pitched roofs while still allowing the unit to be transported under bridges and underpasses. The integrated wood-and-steel chassis means that the home can now be sited without pier support, which helps it to look even less like a trailer.

Many rental-park operators are upgrading their communities, trading in the mobile homes of the 1960s and '70s for more modern multisection manufactured homes. Fannie Mae was apparently impressed by the results of the Washington, DC, urban-design demonstration project and is now advocating manufactured infill housing in central-city areas. High urban land costs make manufactured housing a particularly attractive affordable-housing choice. Sales in California were up 38 percent in 1998.

Heavens, Alan J.
2002. Home builders develop affordable alternatives to mobile homes. *The Philadelphia Inquirer* February 3.
Construction foreman Chad Garner is interviewed about the growing popularity of manufactured housing in the affordable sector of the residential market, and conventional builders' response to it. His project is sited on the grounds of the National Association of Home Builders Research Center in Maryland, and includes four single-family, detached houses described as "marketable, affordable, durable and entry-level," called MADE homes. The plans for these houses were part of HUD's 2000 report, "Homebuilders' Guide to Manufactured Housing." The homes are intended to demonstrate the ability of site-built builders to use emerging technologies and innovative building techniques. The homes are stick-frame construction, built on basement lots and containing about 1,800 square feet of expandable living space. Several money-saving ideas were implemented, such as using open, multiuse living areas and eliminating the wasted space of hallways. Garner discusses how he shopped around for affordable ways to create energy efficiency, a security system, and an expandable wiring package.

Henkenius, Merle
1999. Housing hits the highway. *Popular Mechanics* 176(7):110-121.
This article offers a look at the latest in prefabricated housing technology, asserting that factory-built housing might sometimes be better than site-built housing, if not necessarily cheaper. Site-built housing involves many

more difficult-to-control variables, including weather, shortages of skilled labor, a decline in lumber quality, and problems with job management. Most of these problems are much more manageable in a factory environment, making some factory-built homes better quality than even up-market, site-built homes. The author defines the difference between manufactured housing (built to the HUD code) and factory-built housing (built to the Unified Building Code) and asserts that although manufactured homes are a popular and viable affordable housing option, factory-built housing simply fits more comfortably within the realm of local real estate. They are seen as real property that appreciates in value, while manufactured homes are often viewed as personal property, which depreciates in value. The article goes on to discuss types, features and uses of factory-built housing, including modular homes, insulated panels, post-and-beam construction and log homes, as well as site-preparation requirements.

Keyes, Peter A. and Steven Winter
1996. The manufactured home: Design and construction. *Urban Land* 55(1):27-31, 73.
Post-Hurricane Andrew, HUD revised the Federal Manufactured Home Construction and Safety Standards and designated three wind zones where homes would have to be constructed to withstand winds of 100 to 110 miles per hour, bringing them in line with their site-built counterparts. In 1994, HUD adopted new thermal performance standards that have greatly enhanced energy performance. Ventilation standards have also greatly improved since the 1980s. Manufactured housing tends to fair better in earthquakes, as it is designed for bumpy travel along the highway. The estimates of useful life for a manufactured home have risen significantly, from earlier estimates of 19 years, for homes built in the 1970s, to 55 years put forth by researcher Carol Meeks of Iowa State University.

Manufactured housing tends to follow trends in the building industry with respect to design features. Due to the limitation of the box, when a successful design enters the market, competitors are quick to imitate it. There is a tendency to ignore architectural rules about proportion in an effort to disguise the box with excessive ornament. Any site-built elements are subject to local codes. After living in the home for a while many owners choose to add a room for extra storage, an extra bedroom or a verandah. Ceilings are now up to 10 feet high in the more expensive units. The cost of wood has resulted in experiments with steel-frame construction. Site-built developers argue that if the chassis requirement is lifted, then manufactured housing should be subject to the local codes. Finally, the authors discuss the problems of design for infill housing in historic neighborhoods.

Krigger, John
1994. *Your Mobile Home: Energy and Repair Guide for Manufactured Housing.* Helena, MT: Saturn Resource Management.
This guide is geared toward those who own, repair, inspect or weatherize manufactured homes. Its focus is primarily on mobile-home construction, repair and weatherization. It contains information on heating, cooling, air quality, insulation, moisture control, plumbing, electrical, windows, roofs, doors, walls and ceilings, and includes over 200 illustrations.

Krupka, John
1996. Rethinking manufactured housing: A graduate level design studio. (University of Wisconsin-Milwaukee.) *Crit* 37:43-46.
Responding to the serious housing shortage in Milwaukee's inner city, with over 2,000 vacant, abandoned or neglected lots, this studio focused on the design of affordable manufactured housing for low-income families. Site conditions were examined and an anticipated owner profile was completed for a 60-square-block area of the inner city. The students determined that current occupants of homes remaining in this area were paying high rents for substandard homes and should qualify for mortgages on the new units. The studio then focused on the design and construction of the housing units. Manufacturing would incorporate HUD-code manufactured housing and modular units. The manufacturing facility would be located close to the study site, as a source of jobs for residents. Designs included HUD-code double-wide, stacked and nested modular units, and panelized systems. The article includes photos of unit models.

Link, Joseph E.
1998. Breaking out of the box. *Urban Land* 57(6):82-84, 90.
New Colony Village is located in Howard County, MD. The county has the lowest percentage of affordable housing of all the jurisdictions in the Baltimore/Washington corridor, at around four percent.

The developers, working with housing consultants, developed a HUD-code-approved chassis that allows transport and stacking capability to create two-story homes. The chassis is a combination of lumber and steel and is an integral part of the floor system. New Colony homes are

two-, three- and four-section configuration over a basement foundation and range in size from 1,005 to 1,535 square feet. Transportation charges ran from $2,000 to $3,300, depending on the house type. Homes were priced at $109,990 to $132,440—well below the county average of $273,000. The net density of the development will be 14 units per acre.

The community is gated and contains walking trails and a central community facility with a fitness center and meeting rooms. Monthly fees cover property taxes and lawn maintenance, and range from $370 to $440. Annual increases will be tied to the Consumer Price Index.

Maxman, Susan and Muscoe Martin
1997. Manufactured housing urban design project. *Urban Land* 56(3):49-51.
The Manufactured Housing Institute initiated the Urban Design Project to demonstrate the potential for manufactured housing in urban areas. Susan Maxman Associates, a Philadelphia-based architecture firm, managed and designed the project in collaboration with local firms in each of the six cities chosen for the project. The cities, Milwaukee, Denver, Louisville, Birmingham, Washington, D.C. and Wilkinsburg, PA, were chosen through a request for proposals. In each of the areas, two to 10 units were built and sold at market rate.

The urban market and its development and financing methods were unfamiliar to many in the industry. In addition, community participation was built into the process, which was definitely unfamiliar territory. The architects worked to understand the character of the neighborhood and to design manufactured housing to fit the context. The authors state that there was a positive reception from many community residents, particularly the elderly, who like the idea of one-story living as it could allow them to remain in the community and while not having to climb so many stairs.

Moffett, Marian
1994. Manufactured housing: The TVA experience. *Arris: Journal of the Southeast Chapter of the Society of Architectural Historians* 5:31-37.
As a necessary adjunct to dam-building, the Tennessee Valley Authority provided worker housing for its construction camps. TVA architects created a series of designs for economical, demountable houses, all of which exploited the potential of off-site manufacture in sectional units. This article explores the TVA's "refinement of the design and manufacturing of demountable houses and the ideals that underlay them."

TVA records note the superior portability of sectional housing over panelized construction, and the lower cost involved in transport and assembly. Despite these advantages, the TVA's prefabricated housing did not find a postwar market. The very qualities that made it advantageous for defense work—small size and minimum cost—may have made it unappealing to a general public looking for a more expansive lifestyle after years of shortages and rationing. While TVA designers saw buying a demountable house as a smart consumer decision, analogous to buying a used car, American homebuyers thought differently. In the Tennessee Valley today, the cheaply made double-wides scattered in rural areas flourish as "the most prominent descendants of an innovative experiment in manufactured housing."

Sanders, Welford G.
1995. Expanded role for manufactured housing. *Urban Land* 54(7):19-22.
Sanders discusses some of the advances in the industry, such as "developer series" homes, which are indistinguishable from their site-built neighbors; hinged roofing systems that allow 5/12 roof pitches and are made with shingles rather than galvanized steel; and energy-conserving features such as double-glazed windows that are now standard.

The state of California is notable for its legislation that permits manufactured housing in traditional suburbs. Port Development, located in San Pablo, CA, has placed more than 50 manufactured units on infill sites in the Old Town District. In Oakland, Paul Wang and Associates developed a 30-unit manufactured-housing project called Laurel Courts aimed at low- and moderate-income residents.

Sanders maintains that new manufactured housing may be less costly in many cases than rehabilitating dilapidated housing. He also cites fewer short-term maintenance problems with the new units. Sanders also favors inner-city housing factories, and cites examples in Los Angeles and Indianapolis. He recommends testing the market with a pilot project that will educate the local population about the realities of manufactured housing. Factories, he argues, could also produce component parts such as cabinets, doors and floor trusses. This would expand the market (components could also be sold to site-built developers) and increase skills training.

Sanders estimates the extra cost of the chassis requirement at $3,000 to $4,000. Some of the resistance to lifting the requirement comes from traditional home-

builders, who see the removal as an unfair advantage (assuming manufactured housing were still kept under the HUD code).

Sokol, David
2002. Feast or famine? *Architecture* 91(43):29.
The brief article announces the National Association of Home Builders Research Center's tour (beginning April 2002) of two MADE homes at the NAHB Research Home Park in Maryland. The "marketable, affordable, durable, and entry-level" demonstration project, with construction costs of $55 to $60 per square foot, is intended to provide an alternative to multisection manufactured housing, which has an average fabrication cost of $32.18 per square foot, according to the Manufactured Housing Institute. HUD funded the creation of a manual containing the prototype standards.

The building plans for MADE prototypes should be available for sale in June 2002 through the NAHB and HUD. Sokol notes that while MADE homes' potential success may help the construction industry, it will not benefit architects because of the availability of preexisting plans; home developers may not need to turn to professional designers.

IV. ECONOMICS

[APPRECIATION, MAINTENANCE, USER COST, TAXATION, INSURANCE]

Allen, George
1994. The manufactured home community metamorphosis. *Journal of Property Management* 59(3):34.
The article reports on a survey of state manufactured-housing trade associations which named three significant problems still plaguing the manufactured-housing industry despite its growing popularity: local governments' discriminatory rule-making; zoning-related issues; and taxation of manufactured-home communities. However, managers of the 50,000 manufactured-home communities in the U.S. still have lower operating expenses than apartment managers. The national average operating expense ratio (OER) for conventional apartments is almost 52 percent, while the average OER for manufactured-home communities is only about 37.8 percent.

Berg, Sanford V. and Christopher Taylor
1994. Electricity consumption in manufactured housing. *Energy Economics* 16(1):54.
Data is presented regarding the factors that determine the consumption of electricity in manufactured homes. The study was conducted using a random sample of over 400 Florida electricity consumers, and includes information on socioeconomic characteristics, housing features and monthly electricity consumption. A model is constructed that explains over 40 percent of the variation between customer usages. Interesting suggestions are made for thermostat settings, site orientation and conservation investments.

Boehm, Thomas P.
1995. A comparison of the determinants of structural quality between manufactured housing and conventional tenure choices: Evidence from the American Housing Survey. *Journal of Housing Economics* 4(4):373-391.
This study employs data from the 1985 to 1989 AHS to compare the cost and perceived structural quality of owned manufactured housing with traditional rented and owner-occupied housing alternatives. In general, manufactured housing is found to compare favorably to traditional alternatives because of its low cost and households' perceptions that its structural quality is relatively high. An ordinal-probit model is used to examine the way in which specific structural attributes affect households' ordinal ranking of overall structural quality. Results suggest that the same factors are important across all tenure types in influencing perceived structural quality, and that under the right circumstances, manufactured housing could be a cost-effective way to improve the quality of housing for low-income families who currently rent. The low percentage of minorities utilizing manufactured housing is discussed and potential reasons explored. Finally suggestions are made regarding policy options and future research.

Boers, Ted
1991. Do manufactured homes appreciate or depreciate? *Manufactured Home Merchandiser.*
An extensive database on value trends exists for Michigan, where Datacomp Appraisal Systems Inc. has specialized since 1987 in appraising manufactured housing using the comparable-valuation approach, appraising 8,000 units a year. Boers analyzed 88,000 resales from this database, identifying reasons for appreciation and depreciation.

—. 1997. Appraising manufactured homes: A step in the right direction. *Manufactured Home Merchandiser.*
Factors in appraisal were location, obsolescence and inflation. Values of identical homes in comparable parks varied by up to 24 percent, showing the importance of local market preferences.

—. 1998. Does collateral matter? *Manufactured Home Merchandiser.*
Paying too high a purchase price is correlated with decreasing value. The cost and availability of land-lease sites also affects values over time. High rents were correlated with low resale value. Where sites for new homes were in short supply, values of used homes increased. The supply of alternate forms of housing and the presence or absence of an organized resale network also affected resale values examined in the Michigan study.

Burnside, Kevin
1999. *Buying a Manufactured Home: How to Get the Most Bang for Your Buck in Today's Housing Market.* San Francisco, CA: Van der Plas Publications.
Geared toward prospective buyers and written by a former Realtor, this guide argues that newer manufactured homes are far better than the original trailer homes and are a viable housing option with realistic financing. Topics covered include choosing a home, financing, finding a dealer, locating a home, materials and construction, home options, and tips for staying in control of the home purchase.

Carroll, Jeff
1997. Manufactured housing update. *Urban Land* 56(3):43-47.
Manufactured housing is a $9.5 billion business. In 1995, there were 340,000 shipments of manufactured-housing units, a 100-percent increase over four years. The manufactured-home-community industry (as opposed to manufactured-housing production) is fragmented. The top 10 operators control only about 6.88 percent of the estimated 2.8 million lots in the U.S.

Manufactured-home loans are moving closer to traditional mortgages. Manufactured-home loans typically carry a 10 to 14 percent rate with a 95 percent loan-to-value ratio. The loan terms typically range from 20 to 25 years. The average manufactured-housing capitalization rate for all community types comes to 10.19 percent. In 10 years it is expected to fall 27 basis points, to 9.92 percent. The focus on increasing home ownership has helped the industry considerably. Decentralization has also increased demand, as it is a more acceptable form of housing away from the central city.

The assumption that retirees are increasingly migrating to Arizona and Florida is not entirely accurate and has led to overbuilding of retirement communities of manufactured housing. A study by the American Association of Retired Persons demonstrated that many retirees prefer open-age communities and prefer, when possible, to stay in their own home.

An affordable manufactured home in a rental park, assuming a 95-percent loan financed at 10 percent rate for 20 years, including the cost of moving in (down payment, security deposit and first month rent) is $2,245 and then $548 monthly for the house payment and land rent. This compares to a site-built starter home with a 9 percent rate for 30 years having a monthly payment of $726 plus $179 per month for property tax (assuming 1 percent of the value), totaling $805. Land-lease rents are expected to rise faster than apartment rents; however, lower monthly costs ($200 to $250 vs. $500 to $1000) means they can sustain 3 to 5 percent yearly increases for longer.

Connors, John
1996. A profitable option. *Urban Land* 55(1):6.
Connors lists as the primary benefits of the manufactured home quality control, the ability to strictly control costs and to accurately predict production time.

Hegji, Charles E. and Linda G. Mitchell
2000. The impact of manufactured housing on adjacent site-built residential properties in two Alabama counties. *Southern Business Review* Fall.
This study used 1997 and 1999 property valuations from Montgomery and Lee counties in Alabama to assess the impact of proximity to manufactured housing on site-built property values. Methodology used was similar to that used by Stephenson and Shen (1997), including a spatial analysis using GIS and scattered and clustered manufactured-housing properties. Average annual appreciation rates and weighted average annual appreciation rates were calculated for manufactured and site-built properties. The results partially contradict existing studies that show slower appreciation in site-built homes near manufactured homes and show this negative impact happening in one of the counties, but not the other.

- The appreciation rates of individual manufactured-housing units in both counties were comparable to those of site-built properties.

- In both counties, clustered and scattered manufactured-housing properties appreciated between 1997 and 1999. The appreciation rate for the latter was higher.
- For both counties, proximity to manufactured housing did not appear to be a significant determinant of property values of site-built residential housing, but the study found that while there was no negative impact observed in Lee county, a negative impact on the appreciation rates of adjacent site-built properties did exist in Montgomery county.

Sclafane, Susanne
2000. Challenges ahead for mobile home insurers. *National Underwriter* 104(19):28.
Recent years have seen high growth rates in the industry, but some market players expect challenges ahead. Falling interest rates in recent years have made purchase of regular suburban homes a viable option for some buyers who would otherwise have bought manufactured housing. There are also concerns over the large inventory of homes. The article quotes various people in the industry regarding their concerns.

Stephenson, Richard and Guoqiang Shen
1997. *The Impact of Manufactured Housing on Adjacent Site-Built Residential Properties in North Carolina.* Greenville, NC: East Carolina University.
This study used GIS to investigate manufactured housing's impact on values of site-built residential properties in close proximity, looking at both scattered manufactured homes and clustered manufactured-home communities in four counties in North Carolina. The researchers used the counties' two most recent residential property valuations conducted by the tax assessors' offices. The researchers found:

- There was no clear negative correlation discovered between the overall appreciation rate of site-built residential properties and the presence of manufactured housing in close proximity.
- Manufactured homes with a fixed foundation or listed as real property appreciated at comparable rates to site-built residential properties.
- In one county, manufactured housing listed as personal property depreciated; in another it appreciated, although at a lower rate than site-built housing. This reflected differences in how counties made their property valuations—with some automatically depreciating the value of manufactured housing if considered as personal property.
- On average, the newer a manufactured home, the higher its appreciation rate; multisection homes appreciated at higher rates than single-section ones.

Stringer, Kortney
2001. How manufactured-housing sector built itself into a mess. *The Wall Street Journal* May 24, B2.
"Easy credit led to repossessions and oversupply, as lenders then shied away." This brief article describes the rise and recent sharp fall in sales of manufactured homes (including a graph).

U.S. Department of Housing and Urban Development
1998. *Factory and Site-Built Housing: A Comparison for the 21st Century.* Washington, DC: NAHB Research Center.
A comparative study of the site-built, manufactured and modular sectors of the housing industry, detailing recent growth trends and identifying efficiencies in the manufactured-housing sector that can be applied to conventional site-built or modular home construction. It includes an extensive set of figures and tables.

Historically, manufactured homes built to the pre-emptive federal HUD code have not competed directly with site-built housing because of substantial differences between the two types of homes. However, recent trends suggest increasing market overlap, particularly in the entry-level, affordable-home market. Not only has the output of manufactured homes more than doubled from 1991 to 1996, but the units are larger, better equipped, and often similar in appearance to conventional ranch-style houses. Most new manufactured units are now being placed on privately owned land rather than on rented sites, and the development of two-story, HUD-code homes is underway. HUD-code and site-built producers are also forming partnerships that may point to future changes in the housing industry.

While most producers of manufactured and modular housing focus on the construction of the housing unit itself, site-built producers often must address issues including land development, zoning, subdivision planning, provision of utilities and other infrastructure, arrangement of financing and marketing.

The regulatory systems governing manufactured, modular and site-built housing differ based on the jurisdiction that oversees production. Site-built and modular homes must conform to state and/or local codes, while manufactured homes must comply with a federal code that pre-empts state and local code requirements. The report assesses

the potential impacts of differences in code requirements on the cost of producing different types of housing. It compares and contrasts the regulation of housing-unit construction in each sector of the industry, including approval, design review and inspection; land development, site work and installation; and building, electrical, plumbing and energy requirements. For a variety of reasons the federal system regulating design and construction of manufactured housing appears to be more efficient and less costly to administer than the corresponding state and local systems regulating site-built and modular housing.

The study analyzes and compares the relative costs of site-built, modular and manufactured homes using three approaches. A detailed analysis contrasts the selling prices and production costs of each type of housing. Factors contributing to differences in selling prices and production costs include:

- Factory-production economies of scale and purchasing power of producers;
- Presence or absence of land in the transaction;
- Type of foundation system;
- Inclusion of design amenities such as garages and fireplaces;
- Building materials used for construction of floors, roofs, walls and other elements; and
- Regulatory systems and technical requirements for design and construction.

The cost comparison indicates that the manufactured homes analyzed are less expensive than the site-built or modular homes due to lower square-foot production costs, even after adjusting for major factors such as land, square footage and difference in foundation costs. The cost comparisons also examine up-front cost and monthly housing payments from the buyer's perspective under several scenarios.

The report makes regulatory and technical recommendations for site-builders and production builders, showing how conventional home-building firms can improve their operations, learning from the experience of manufactured-housing producers.

U.S. House of Representatives Banking Finance and Urban Affairs Committee. 1990. *Manufactured Housing Construction and Safety Standards.* Washington, DC.
This 946-page report was prepared for the May 1990 hearing before the Subcommittee on Housing and Community Development to examine the status of and possible need for changes to federal manufactured-housing construction and safety standards. It includes substantial statistics on mobile-home fires, deaths, injuries and property damage, and characteristics of residents of 32 mobile-home parks, estimated impacts of these parks on the local economy, mobile-homes sales, and comparative housing costs from 1980 to 1989.

Warner, Kate and Robert Johnson
1993. *Manufactured Housing Research Project.* Ann Arbor, MI: University of Michigan.
Report 2: Manufactured Housing Costs and Finance, Robert Johnson and Jeff Scheuer.
This report investigates the cost or affordability characteristics of manufactured housing, including the initial cost obligation and cash outlay for the housing, and the ongoing annual and monthly housing costs. Five prototype manufactured-housing options are examined and contrasted with comparable site-built housing alternatives.

Manufactured housing shows significantly lower initial capital costs, due to the economies of scale arising from the manufacturing process, resulting in much lower construction costs per square foot; building-systems innovation resulting from sensitivity to quality and cost; and the fact that land is less expensive for those manufactured-housing consumers who rent rather than purchase lots.

Manufactured housing is shown to have affordability advantages given the lower amount of mortgage principal and interest incurred, along with lower tax and operating and maintenance payments. But rent is a significant and rising cost in terms of affordability of both manufactured housing and comparable rental apartments.

Historically, manufactured housing has been financed as personal property on an installment basis; this includes all homes located in rental-park communities. The conditions of such loans have been evolving to resemble more closely, in terms and interest rates, those of conventional-mortgage financing. Mortgage loans can be obtained on manufactured housing placed on private property. Both forms of financing offer the consumer different interest rates, fees and loan maturities that are associated with different ways that lenders have developed for managing risk, and both have advantages and disadvantages for the consumer.

The research concludes that manufactured housing compares favorably with site-built housing as an option for affordable housing.

Report 3: Manufactured Housing Values.
Kate Warner and Jeff Scheuer
Trends in market value in Michigan were determined through analysis of sales of 40,000 new and pre-owned manufactured-housing units from 1987 to 1990. Statewide, regional and county average sales prices of manufactured housing were compiled and analyzed by the size and location of the home. Price changes of specific manufactured homes sold twice during the three-year period were examined by the size and location of the home. Findings include:

- Manufactured housing, like site-built housing, can be viewed as an investment with probabilities of appreciation and equity accumulation.
- The average sales prices of previously owned manufactured homes show a varied pattern by regional housing markets, but generally indicated appreciation.
- Examining the values of homes sold twice, overall, average sales price change 3.7 percent. The average percent change in sales prices of homes purchased new and resold was —1.5 percent; for previously owned homes that sold twice it was 5.0 percent.
- Findings indicate that the value of manufactured housing, like other forms of real estate, is dependent on local market conditions rather than the type of housing-production processes used.
- The authors recommend employing appraisal techniques that emphasize more traditional real estate concerns such as comparable sales, home location, local housing-market demand and price structures, and housing availability.

Wubneh, Mulatu and Guoquiang Shen
2001. The impact of manufactured housing on residential property values: A GIS-based approach. Working paper. Cambridge, MA: Lincoln Institute of Land Policy.
This study tries to answer the question of whether manufactured housing negatively affects adjacent site-built housing property values. Using regression analysis, the study revealed that structure variables and degree of urbanization have an important influence on property values.

V. FINANCE

[MORTGAGE, PERSONAL, PARK DEVELOPMENT]

Allen, George
1996. Developing and financing in rental parks. *Urban Land* 55(1):35-39.
In a rental park, homebuyers own and maintain their homes, while the landowner owns and maintains the site, along with any common facilities or amenities. Monthly rent is collected to cover costs of land, not the building. There are 50,000 to 55,000 manufactured-housing communities in the U.S., the majority of which are land-lease. In 1993 and 1994, four large manufactured-housing community owners went public, attracting the attention of Morgan Stanley and Merrill Lynch: "The manufactured home community is a potentially powerful tool for generating cash flow and a valuable investment annuity. Once the property is fully leased, it generally enjoys high occupancy with a minimum of turnover."

However, Allen claims that only when communities near 100 sites do they "begin to enjoy significant economies of scale in management and operation." Other facts:

- Once installed, 90 to 95 percent of manufactured homes do not move; owners will instead sell and leave them behind.
- The national turnover rate for rental parks is 10 to 15 percent, compared to 55 percent for apartment complexes.
- Rent hikes in a rental park can be instituted annually, but are typically done at tenant turnover.
- Staffing requirements and maintenance demands are less for rental parks than for apartments.

Local credit loans are characterized by:

- Personal guarantees with recourse.
- Amounts at 70 to 75 percent of project cost, including land at fair market value (80 percent if the borrower is particularly strong).
- Available interest rate tied to a published index.
- Terms of 24 to 36 months with a possible extension.

Berenson, Alex
2001. A boom built upon sand, gone bust: Trailer owners and Conseco are haunted by risky loans. *New York Times* November 21, Section 3, p. 1.
The article's focus is on the 1990s "good times" for trailer homes and the large role of Green Tree Financial, now Conseco Finance. Green Tree stimulated demand for

manufactured homes and made loans to borrowers who had little chance of repayment, many of whom have defaulted.

Bradley, Donald S.
July 1997. Will manufactured housing become home of first choice? *Freddie Mac SMMOnline*.
Financing is one area where the costs born by manufactured-housing owners has been higher. According to Bradley, only 10 percent of all manufactured-housing transactions are financed with mortgages secured by the underlying property. The interest rate on a personal-property loan financing a manufactured home is about 3 percentage points higher than a typical 15-year, fixed-rate mortgage. A secondary market has emerged that could help to pump more capital into manufactured-housing financing. The secondary market packages manufactured-home sales-contract receivables into securities and sells them to investors.

Bradley cites Standard & Poor's rating service that demonstrated that investors are interested in manufactured housing bonds for the following reasons: lower loan losses (repossession rates decreased by 24 percent from 1993 to 1996); lower prepayment risk (due to smaller average loan size); and real estate mortgage investment conduit (REMIC) eligibility.

Building a foundation in manufactured housing. 1995. *America's Community Banker,* September.
Manufactured-home loan rates are typically 300 to 400 basis points higher than traditional home mortgages and can therefore be profitable for lenders. The article consists mainly of tips regarding manufactured-home loans and brief quotes on the subject from lenders and insurers.

Collins, Brian
2001. Freddie working to reduce rates, costs of manufactured homes. *National Mortgage News* 25(36):18.

—. 2001. Freddie effort may pave way for lower-rate MH loans. *Origination News* 10(10):14.
Both brief articles announce that buyers of manufactured homes will soon be able to obtain mortgage loans at lower rates than traditional manufactured-housing financing because of a new product from Freddie Mac. Along with the Manufactured Housing Institute, Freddie has developed a template for a residential ground-lease agreement so that a manufactured home on a leased site can be titled as real estate and qualify for conventional mortgage financing.

- Less than 20 percent of new manufactured homes are titled as real estate each year.
- Personal-property loans, which finance most manufactured-home purchases, carry interest rates 300 to 400 basis points higher than conventional mortgages.
- Guidelines for these mortgages can be found at www.freddiemac.com/sell/expmkts/mhle.html.

Conseco uses its dealer ties to dominate mobile home market. 2000. *National Mortgage News.* 24(17):12.
Conseco Finance Corp. (St. Paul, Minnesota) has been able to maintain its market dominance in the manufactured-housing lending business through its ability to create and maintain strong dealer relationships, a report by Fitch IBCA notes. Yet increasing competition for these loans caused an unexpected rise in prepayments starting in 1996, forcing a $190 million write-down in that year's earnings.

Conseco Finance originates loans through approximately 3,000 manufactured-housing dealers. "Prior to 1995, there was limited competition and the company was able to focus on loan quality," Fitch IBCA said. In fact, the report goes on to say, loan quality for originations between late 1994 and 1996 was lower than in other periods at the company. During 1994 and 1995, Conseco Finance relaxed its credit criteria by lowering the cutoff credit score. Senior credit managers also had the authority to override the scoring system and approve a loan that did not meet the minimum score. These exception loans, as well as loans made to customers who were "unscorable" because of a lack of credit history, have poorer performance than those that met the minimum score. Conseco Finance implemented remedies to this situation starting in 1997. It reduced the number of originations that do not meet the minimum score, plus it cut back on the percentage of loans to unscorable borrowers. It also tightened underwriting standards through the use of dealer-trend scorecards. These track default rates by dealers, which is a factor considered in the loan-approval process. To deter borrowers from making lower down-payment loans, the rate on a loan with 5 percent down is much higher than for one with 10 percent down.

Davidson, Steven. 1997. Financing manufactured housing. *America's Community Banker* November.
Manufactured-housing loans carry higher yields than traditional, first-mortgage loans. The loans are priced as a hybrid between consumer and mortgage loans, with rates typically 200 to 400 basis points above comparable site-built residential mortgages. The typical loan size is smaller. As a consequence, rising rates have a smaller

dollar impact on the monthly debt service on these loans, and there is a smaller dollar benefit in refinancing in a falling rate environment. Thus manufactured-housing loans also tend to experience significantly slower prepayment speeds in declining-rate environments. Manufactured-housing niche lending is dominated by aggressive, specialized non-depository finance companies (accounting for two-thirds of all activity) and is characterized by more credit risk than traditional home-mortgage lending.

The industry has experienced sharp cyclical swings over the last 25 years. Average manufactured-home prices are increasing, but the cost is still less than site-built for a comparable unit: "According to 1996 Census Bureau data, the monthly cost, excluding insurance and taxes, to purchase a manufactured home is $580 (assuming a typical mortgage of 15 years) compared to $1,350 for the average site-built home (assuming a 15-year mortgage)."

Although the majority of manufactured-housing loans are held in portfolio, securitization of manufactured-home loans has experienced significant growth since 1992, when the first security was issued. Davidson predicts a continued trend of securitization. Over the past five years, $20 billion of manufactured-housing asset-backed securities (ABS) have been issued. According to CS First Boston estimates, the annual issue volume has increased from $2.5 billion in 1993 to an estimated $8 billion in 1996, and the manufactured-housing share of total security issues has increased from 3.8 percent in 1995 to 6.2 percent through the first half of 1996.

Considering the inherently higher risk profile of this type of lending compared to traditional mortgage lending, such asset-backed securities require significant credit protection in a subordination structure. Recent manufactured-housing asset-backed securities have required about 20 percent of subordination to achieve an AAA rating, with lower levels of subordination required for lower investment-grade securities. The spread between yield and coupon rates on manufactured housing ABSs historically has been lower than home-equity issues, but higher than credit card and auto loans. Only issues supported by loan pools that have relatively strong credit quality can be sold in the institutional investor marketplace. The weighted average yields run from 10 to 12 percent and the weighted average term is slightly less than 10 years.

Fannie Mae to see if manufactured housing pilot will fly. 2000. *Origination News* 10(1):18.
Recognizing potential in the manufactured-housing market, Fannie Mae has approved a pilot program for its financing. In the first deal growing out of the program, Fannie Mae and Birmingham-based Collateral Mortgage have provided $116 million in initial funding for a credit facility for Chateau Communities of Greenwood Village, Colorado, a real estate investment trust (REIT) that is an owner and manager of manufactured-home communities. Fannie Mae purchased seven first-mortgage loans funded by Collateral Mortgage, a Fannie Mae-delegated underwriting and servicing (DUS) lender—secured by seven separate manufactured-housing communities comprising 4,467 sites in California, Florida and Michigan—and used them to create a fixed-rate, mortgage-backed security.

Susanne Hiegel, director of multifamily capital markets at Fannie Mae, said, "Fannie Mae approved the program because we saw that there was a niche in the market that we were not serving and that looked like a very sound investment, and it promoted affordable housing and was a natural progress. Fannie's goal is to disburse as much as $250 million of financing for this market segment during the pilot phase."

Ms. Hiegel noted that while the manufactured-housing market presents a "different risk" than the usual multifamily loan, it is not necessarily riskier. In this case, the GSE has a lien on the land rather than the house. The homeowner in a manufactured-housing community typically pays "pad rent" to allow the house to sit on the pad and for the use of community facilities. Also, Ms. Hiegel said, there is about a two- to five-percent rate of resident turnover in a manufactured-housing community, whereas the turnover in a typical apartment complex is higher.

Healthier outlook for manufactured housing? 1985. *Urban Land* 44(2):24.

- Manufactured homes account for one-third of new single-family homes sales.
- Manufactured homes account for more than 75 percent of homes sales under $50,000.
- The Secondary Mortgage Market Enhancement Act should encourage the development of the still-new secondary market for conventional manufactured-home loans.
- Higher financing costs make manufactured homes less affordable than their sale prices suggest.

- Most manufactured homes are financed with 10- to 15-year consumer installment loans with larger down payments and higher interest rates than conventional mortgages.
- Ginnie Mae has been the vehicle for nearly all secondary-market activity.
- Freddie Mac and Fannie Mae have begun buying conventional loans on manufactured homes classified as real estate and placing them in pools of ordinary single-family mortgages
- Congress has granted both Freddie Mae and Fannie Mae authority to purchase loans on manufactured homes classified as personal property, if they are principal residences. Foremost Financial Services Corp. and Northwest Mortgage Corp. have issued pass-through securities backed by pools of manufactured-homes loans.

Manufactured Housing Institute. (Annual.) *Manufactured Housing Financing.* Arlington, VA: MHI.
This annual report on mobile-home consumer financing, by type of lending institution, with loan characteristics and methods of repayment, reports on the previous year's survey results as well as general trends. Data come from responses to MHI's annual survey of lending institutions and from the National Conferences of States on Building Codes and Standards.

Sichelman, Lew
2001. Manufactured called opportunity. *National Mortgage News* 25(22):7.
Manufactured houses are financed in one of two ways: either as a house only or as a combination of house and land. Home-only financing is dominated by national finance companies that work directly with the dealers for whom they also carry inventory financing. Since many units are not permanently fixed to the sites, they are treated as personal property and financed with a consumer loan in which the lender takes a lien on the title, much like an automobile lender. While 30-year financing is available, these loans frequently carry rates that are 300 to 700 basis points above conforming mortgage rates, largely because "there are no Fannies or Freddies. And as a result, the cost of financing is so high that the affordability is taken away."

Land-home financing is more akin to traditional mortgage lending. But there are some significant differences. For one thing, in cases in which the buyer leases the site, the lender takes an interest in the lease, which often is five to ten years longer than the mortgage. For another, purchase-money mortgages for new units usually require a four-draw construction loan. The first draw covers the cost of the land plus the 10 percent of the price of the house the retailer must advance to the manufacturer. The second covers the cost of such improvements as the foundation, well and septic tanks to make the site ready to receive the house. Draw number three comes when the house is delivered to the site and covers the remainder of the cost less 10 percent for the final draw, which covers the final inspection.

Mortgage lenders who ignore manufactured housing could be missing 25 percent or more of the single-family market. Homes built to the national HUD code accounted for about one in four housing starts in the 1990s and 30 percent of all sales, according to Michael O'Brien of the Manufactured Housing Institute.

The urban in-fill market holds huge potential for builders and lenders. Other business opportunities include scattered-site transactions; fee-simple subdivisions where there is no other way for builders to meet their price points; and long-term land-lease projects for land developments.

Walker Guido, Daniel
2001. Manufactured mess. *Builder* 24(13):51-52.
Manufactured housing continues to buckle under the glut of repossessions caused by the easy credit terms that finance companies offered thousands of manufactured-home buyers in the mid-1990s. Currently, about two percent of all manufactured-housing loans are in repossession proceedings, according to the Manufactured Housing Institute. Many economists expect that figure to grow as more blue-collar workers join the unemployment rolls as companies cut jobs in the economic slump. The repossessed units compete with new-home sales, depressing prices and forcing manufactured-housing companies to scale back production.

Declining sales have forced many manufacturers to close production facilities. Champion, a Michigan-based manufactured-home builder, has recently closed 19 locations, with 49 remaining. Finance companies are being pummeled by the rising tide of bad loans engulfing them. Indiana-based Conseco, an insurance and finance company, recently reported a second-quarter loss of $30 million as delinquency rates rose on its manufactured-housing loans.

Until recent years, most manufactured homes were bought and placed on rental lots, and financed with subprime loans rather than traditional mortgages. But as sub-

prime loan rates increased (to about 14 percent at this writing), many homebuyers bought land to put their homes on and applied for land-and-home mortgages. By doing this, they were able to take advantage rates for traditional loans (currently less than 8 percent). Last year, 22 percent of the manufactured homes sold were financed by mortgages, compared to only 9 percent in 1994, according to MHI figures.

This shift to "safer" mortgages means things could start looking up for this beleaguered sector of the building industry. Although the industry expects to see another 70,000 repossessions next year, that number will drop to 60,000 in 2003 and about 50,000 in 2004, says Colleen Bauman, assistant vice president for investor relations at Champion. MHI concurs with the improvement trend. "We expect an increase in sales and a decline in repossessions starting in the second quarter of next year," says Kami Watson, MHI's spokeswoman.

VI. MARKET

[PRODUCERS, RETAILERS, INVESTORS, INDUSTRY TRENDS]

Allen, George F.
1997. Winning the manufactured housing game. *Journal of Property Management* 62(4):14-16.
The article calls manufactured housing and the rental park the hottest affordable-housing option of the day. The increased popularity of this option has created an array of property-management opportunities. Investors find the favorable operating-expense ratios of manufactured-housing communities attractive. Issues affecting the market include a severe shortage of capable and experienced mid- and executive-level property managers, too few new manufactured-housing communities being built, replacement or rehabilitation of older manufactured homes and communities, and avoiding rent control and landlord-tenant legislation.

Benman, Keith
2002. Manufactured homes industry starts to rise out of slump. *South Bend Tribune* January 13.
Manufactured-home dealers and manufacturers have suffered through almost two years of severely slumping sales, but things seem to be picking up now, in part because many empty-nesters in their 50s see manufactured homes as a way to get more bang for their buck. The first half of 2001 saw declines in manufactured home shipments of more than 40 percent. Manufacturers that survived the downturn will be pulled out of recession by several factors: low inventories at dealers' lots mean they will have to replace every unit they set; fewer companies are making manufactured homes than two years ago, leaving more market share available; and very low interest rates on home mortgages and land-home financing are helping to perk up sales. This last factor is especially important in northern states, where manufactured homes often have basement foundations, a key criterion for qualifying for a mortgage or land-home financing.

Datres, Nancy
1991. Manufactured housing: Industry still somewhat haunted by negative image. *Central Penn Business Journal* 7(8):13.
The article begins by defining manufactured housing and explaining the 1976 passage of the National Manufactured Home Construction and Safety Standards Act, or HUD code. It reports that despite federal uniform building and safety standards, as well as contemporary designs, energy efficiency and safety features, manufactured housing continues to be misunderstood and often maligned. Although many modern manufactured homes are nearly indistinguishable from conventional homes, site availability and zoning remain restricted in many states and many people continue to hold a "not in my backyard" attitude toward manufactured housing. The author concludes that while some progress is being made on the public image of manufactured housing, setbacks still occur, such as the maligning of manufactured housing by other factory-built housing industry members who do not want their products confused with manufactured homes.

Fanjoy, Rob
2000. Manufactured mansion to house first family. *Professional Builder* 65(12):50.
Champion Enterprises, Inc., of Auburn Hills, Michigan, donated a three-bedroom, two-bath manufactured home to the Arkansas Governor's Mansion Association in an effort to raise awareness and change the public's outdated perceptions of manufactured housing. The home will house Arkansas Governor Mike Huckabee and his family while renovations are being done to the mansion. The home, chosen by first lady Janet Huckabee, was specifically designed to fit the needs of the baby-boomer market. Its selling price is $99,000.

Gillette, Becky
1999. Manufactured homes well built, more popular than in the past. *The Mississippi Business Journal* 21(18):1-2.
The article discusses the improved safety standards and designs of modern manufactured homes and their attractiveness as a quality, affordable-housing option. The director of the Mississippi Manufactured Housing Association is interviewed, and says that the life expectancy of manufactured homes built today averages 55 years. In Mississippi, about 21,000 manufactured homes were built in 1998. The industry employs about 4,500 people statewide and had an estimated economic impact of $1.1 billion in 1998.

Horsburgh, Scott D.
2001. Fleetwood Enterprises, Inc. *Better Investing* 50(9):56.
Fleetwood Enterprises, the leading producer of manufactured housing and recreational vehicles in the U.S., reported a huge net loss in the quarter ending January 2001, after manufactured-housing revenues fell 38 percent and RV sales fell 42 percent for the quarter. Eighteen months earlier, Fleetwood Enterprises had been featured as the undervalued stock selection. Since then, the stock has not fared as badly as it could have, but at this point it is probably existing shareholders and bold investors with a long-term horizon who are most interested in Fleetwood. Fleetwood's volume of manufacturing units has decreased more sharply than its major competitors and than the industry as a whole. The short-term outlook remains bleak.

Juarez, Macario Jr.
2000. Low-price alternative catching on slowly. *The Arizona Daily Star* January 16.
This article discusses a manufactured-home show that took place that week in Tucson and other Arizona cities. It briefly discusses the past growth and future prospects of manufactured homes.

Levy, E.
1999. Manufactured housing research initiative. *Urban Land* 58(3):75-77.
There is great industry fragmentation in the site-built industry. There are more than 100,000 site builders who construct on average fewer than 10 homes each per year. By contrast, in 1998, 89 manufactured-home builders shipped 372,800 homes to all states except Hawaii, which is an average of 4,200 homes each per year. The top five companies accounted for 57 percent of total annual production.

Manufactured home prices should drop.
2000. *Journal of Property Management* 65(2):6, 96.
This brief article reports that the prices of manufactured homes should be dropping in the range of 10 percent, according to the Pappas Report on Manufactured Housing. Increased manufacturing capacity, high inventory levels and too many retail outlets have combined to send the industry into a period of readjustment. Shipments are also expected to decrease by at least 10 percent in the coming months.

Manufactured Housing Institute
1999. *Understanding Today's Manufactured Housing.* Arlington, VA: MHI.
This 20-page report gives a basic but comprehensive snapshot of manufactured housing. It includes cost and size comparisons between manufactured and site-built housing, basic information on factory-built housing, the HUD code, the system of inspection for manufactured homes, the demographics of manufactured-home owners, siting and placement, impacts on property values, design innovations and financing. The tone of the report is positive, presenting manufactured housing as an opportunity for the home-building industry. It includes the American Planning Association's guide to manufactured-housing policy. The report stresses that manufactured homes can match site-built homes in appearance, fire safety and vulnerability to damage. Manufactured housing is presented as a tool for community revitalization and increased home ownership, and as a product that satisfies customers and will appreciate at the same rate as other homes in the same neighborhood.

Manufactured Housing Institute
(Monthly) *Manufacturing Report.* Arlington, VA: MHI.
This monthly report presents detailed data on manufactured-home production and shipment trends, nationwide and by state and census division, with shipment details for single- and multisection homes, and comparisons to trends in single-family housing building permits, starts and sales Reports are issued approximately two to three months after the month of coverage. Each issue contains approximately 30 detailed tables and several charts along with two summary tables and brief analysis.

MBA offers course on mobile homes
2001. *National Mortgage News* 25(29):21.
This brief article announces that the Mortgage Bankers Association of America, in partnership with the Manufactured Housing Institute, is offering an online course on manufactured housing for real estate professionals. The course is offered through

www.campusmba.org, which also provides detailed information about factors contributing to the increased demand for manufactured homes.

Meeks, Carol B.
1999. *Price Elasticity of Demand for Manufactured Homes: 1978-1997.* Arlington, VA: MHI.
This report outlines how cost increases and decreases affect the demand for manufactured housing. The findings show that while single-section homes are price sensitive, multisection homes are not.

Nkonge, Japhet H.
2001. *A Review of Key Trends in the Domestic Environment of Manufactured Housing Marketing and Their Implications for International Involvement of the Industry.* Greensboro, NC: North Carolina Agricultural and Technical State University.
This paper discusses industry trends, such as manufactured housing's growing share of the single-family housing market, as well as the economic and social environment.

- In 1998, the top 25 manufacturers accounted for 92 percent of the total shipments.
- The top 10 manufacturers accounted for 78 percent of that number.
- The industry is becoming more vertically integrated as manufacturers take over retailers and financial services, thereby becoming more involved in sales, financing and installation.
- In 1997, multisection units outsold single sections (representing 58 percent of all units sold).
- Loan terms for manufactured-housing buyers are improving; a buyer can put as little as 5 percent down and take out a loan for 15 to 30 years with interest rates two to three percent higher than traditional loans.
- Alabama, Florida, Georgia, North Carolina, Tennessee and Texas accounted for 40 percent of all manufactured home sales in 1996. In 1997, Texas was first in sales, followed by Florida.

Nkonge asserts that the time is ripe for a new managerial mindset in the industry to make it more responsive to global marketing forces. He also expresses some concern that manufactured-home builders and retailers are going to continue to go after the higher-end market, and that lower-income groups, who have benefited for so long from this affordable-housing choice, will become less important to the industry.

Southall, Brooke
1995. Manufactured home market sheds its "box" image. *Central Penn Business Journal* 11(7):12.
Pennsylvania ranks as the seventh largest producer of manufactured homes in the nation, producing more than 13,000 HUD-code homes annually. Approximately 6,500 of that total is shipped out of state, and the total economic impact from the sale and manufacture of factory-built homes is over $2 billion annually. The article outlines the modernization of manufactured homes, the growth of the industry, their attractiveness as a quality, affordable option, and the growing interest of financing institutions in the industry.

Stinebert, Chris S.
1998. New products, new markets. *Urban Land* 57(6):77-79.
In 1997, 353,000 manufactured homes were produced. Approximately one in four single-family housing starts was manufactured, and the overall market share increased 32 percent. Multisection homes accounted for 58 percent of all manufactured homes sold in 1997. Total sales have more than doubled over the last six years. Depending on the region of the country, manufactured housing costs 15 to 40 percent less than a similar site-built product. The national average is $38,400, or $27.83 per square foot.

Manufactured homes are increasingly energy-efficient and relatively inexpensive to heat. Improved financing has resulted in more competitive pricing and significant developments in the secondary-mortgage market for manufactured homes. Fannie Mae and Freddie Mac have established guidelines for accepting real estate mortgage loans secured by manufactured housing. Finally, zoning barriers have eased considerably in some areas, and manufactured homes are no longer relegated to the least desirable lots.

Major developers such as Pulte, Centex and Zaring National Corporation's HomeMax have begun to incorporate manufactured housing into their developments. Often, it helps with the affordable component of a development. Manufacturers are now reaching out to developers and also housing agencies and redevelopment authorities.

Vermeer, Kimberly and Josephine Louie
1997. *The Future of Manufactured Housing.* Cambridge, MA: Joint Center for Housing Studies.
This comprehensive report first gives an overview of the evolution of manufactured housing and then describes

the current environment using demographic and industry data. The report concludes that because of demographic trends, affordability and continuing improvements in stock quality and appearance, the manufactured-housing industry is well-positioned for continued growth. Also discussed are obstacles to this growth, such as regulatory and zoning issues.

VII. POLICY

[COMMUNITY DEVELOPMENT, LEGISLATION, LOW-INCOME HOUSING]

A/H bill passes Congress; Awaits president's signature. 2001. Multi-Housing News 36(1):5.
This very brief article reports that the American Homeownership and Economic Opportunity Act of 2000 had been passed by the House and Senate and was awaiting the president's signature. The act includes incentives to produce safer manufactured housing. Then-HUD Secretary Andrew Cuomo is quoted as saying the act strikes a balance "between protecting consumers' interests and encouraging the development of safe and affordable housing."

Gann, John L. Jr.
2001. Mainstreaming factory housing. *Urban Land* 60(6):18, 20-21.
The city of Robinson, Illinois, adopted a new policy that would abolish the city's zoning regulations for mobile homes. Factory-built residential units now are subject to all city zoning regulations for site-built homes. In addition, mobile-home parks are to be governed by standards for conventional subdivisions. New factory housing in effect is being "mainstreamed." This addresses demands from the industry for nondiscriminatory treatment of manufactured homes. Six manufactured-home parks are located in Robinson, with five to 80 homes each. To date, no manufactured homes have been allowed outside of the parks. For the new regulations, two kinds of single-family homes were defined, based on what they are like, not on where they were produced. "Conventional detached dwellings" are homes on permanent foundations that conform to the appearance typical of site-built homes. "Alternative detached dwellings" include everything else, both manufactured and stick-built structures. The Robinson regulations permit conventional, detached dwellings on individual lots in all residential districts. Alternative detached dwellings are allowed in urban and suburban residential locations only in developments of five or more units, with heavy buffering on all sides.

The regulations are the same for both kinds of homes with regard to the following: zero lot line development, standards for private streets and nonconformities. To earn the same zoning rights as conventional homes, the city's committee said, in effect, that manufactured homes must assume the same responsibilities. The new rules give flexibility to the city and to the property owner. Given the progress in the law and in the product of the factory-housing industry, mainstreaming may be the most reasonable option for other communities as well.

Genz, Richard
2001. Why advocates need to rethink manufactured housing. *Housing Policy Debate* 12(2):393-414.
In this literature review and position paper, Genz points out the importance of manufactured housing to the U.S. home-ownership rate and asserts that many issues important to these households are neglected because of bias. The article discusses vulnerabilities of manufactured-home owners, who are typically lower-income, and the isolation of manufactured housing from housing finance, which contributes to depreciation. Genz believes that advocates should be working to clear up misconceptions and stereotypes about manufactured housing so that the nonprofit development community can "help reinvent manufactured homes as quality, wealth-building, affordable housing."

- The U.S. home-ownership rate would decrease by almost 5 percent if owners of manufactured homes were excluded.
- Seventy percent of new manufactured homes are placed on the homeowner's land.
- "It should be possible to incorporate the cost advantages of manufactured homes into nonprofit housing developments."

Research should identify factors contributing to appreciation, and mainstream mortgage lenders should enter the market to offer cheaper, more transparent financing. Education would help consumers navigate the marketplace. By incorporating manufactured housing into consumer-orientated, wealth-building developments, nonprofits could take the lead in offering buyers real value, not just low price. Advocates' skills in finance, development and policy can help people make the most out of a fundamentally viable housing choice.

The author describes some necessary measures already being taken, such as:

- Grassroots owner organizations strong in California, Florida and Michigan.
- In New Hampshire, California and Vermont, advocacy for resident ownership of parks. In Vermont, state law gives tax benefits to park owners who sell to residents and gives tenants the right of first refusal to buy.
- The FHA's financing programs for purchasing or refinancing manufactured housing, including homes titled as personal property. But little used as industry's retailing system favors its own finance programs, and most conventional housing lenders have opted out.
- RDA— small loan amounts limited to new units sold by dealer-contractors who meet strict agency requirements.
- Government-sponsored enterprises including Fannie Mae and Freddie Mac in 1998 funded less than 15 percent of all manufactured-home loans. HUD is trying to stimulate GSE participation.

Advocates should focus on several areas which are not being adequately addressed: financing problems, unnecessarily high interest rates, relationship between value and price, lack of buyer education, lack of landlord-tenant protections, condition of older homes, personal-property financing which contributes to depreciation, and policy barriers to housing subsidies and tax benefits.

Hood, John
1998. Factory-built housing: The path to ownership? *Consumers' Research Magazine* August 1998.
The article discusses the emergence of the manufactured-housing industry and describes it as both profitable and innovative. It concludes by asserting that consumers will benefit if policymakers can free factory-built homes from punitive regulations and inaccurate stereotypes.

Hullibarger, Steve
1996. Manufactured homes in single family subdivisions. *Urban Land* 55(1):42-44.
California law (section 65852.3 of the government code) passed in 1980 requires California cities and counties to allow the placement of HUD-code housing on any lot zoned for residential development, providing that certain conditions are met. These conditions typically concern a permanent foundation and that the design be architecturally compatible with the surrounding housing.

—. 2000. Affordable Seattle: How one developer is taming the high cost of infill housing. *Modern Home* May.
HomeSight a nonprofit housing corporation that has used HUD-code homes in its 75-home development, Noji Gardens, in Seattle's Rainier Valley (four miles southeast of the central business district). With 1999 median home prices in Seattle of $234,000, Noji Gardens was able to offer housing at $155,000 to $225,000. Schult Homes Corporation built the homes in Oregon. Two-story homes make the development of expensive city land more feasible. Since affordable-housing subsidies are generally targeted at rental housing, nonprofits and for-profits who wish to build affordable housing must increasingly look for ways to cut costs, and manufactured housing is looking increasingly attractive. The HUD-code homes were completed in two to three months, but HomeSight estimates that with experience it will be able to get it down to 30 days. The hinged roof has an 8/12 pitch. There is a general feeling that with projects like this one, and others such as New Colony Village in Elkridge, Maryland, and Lido Peninsula Resort in Newport Beach, California, perceptions about the product will begin to change.

Hullibarger, Steve and Paul Wang
1998. Building fast and easy: Manufactured homes have revitalized many Oakland, CA, streets. *Urban Land* 57(6):87-89.
This article discusses the urban decline of Oakland and the surrounding "flatlands" or lower-lying, lower-income neighborhoods in the late 1970s. Starting in the late 1970s, the California legislature and the city of Oakland began to consider whether the obstacles to the rebuilding of inner-city neighborhoods could be overcome by using manufactured housing. In 1980, the city and state threw out regulatory barriers that would have prohibited manufactured homes in residential zones, declaring that they would be permitted if made architecturally harmonious with the neighborhood. Shortly after the statutes were enacted, entrepreneurs began purchasing the vacant lots and bringing in specially designed manufactured homes. The current standard manufactured home was still too boxy to fit in architecturally, so builders began experimenting with add-on styling and other changes such as roofline extensions, tile roofing, attached garages and porches. This phase of industry development has made it easier to transform manufactured homes into single-family dwellings compatible with neighborhoods
In the past, the city had difficulty disposing of vacant properties because they were too costly to improve; now, since so many urban lots have been developed here, the city has become comfortable in helping small groups of individuals acquire them for manufactured housing. The typical deal involves the city selling or often giving the lot to parties with a good performance record, sometimes

with a subsidy. In exchange the parties agree to place a new home, affordable to low- and moderate-income families, on the lot modified to fit the neighborhood physical context.

Knack, Ruth
1995. House-in-a-box. *Planning* 61(8):10-13.
Knack cites the 1994 National Commission on Manufactured Housing, which called for equal treatment of all types of housing in financing, public services, federal housing subsidies and zoning. Knack discusses several innovative projects:

- Elder Cottage Housing Opportunity (ECHO) was a $13-million demonstration project and part of the Section 202, Supportive Housing for the elderly program. ECHO used manufactured housing for low-income elderly people that were sited temporarily on family members' lots. It was based on the "granny flats" model used in Australia.
- In South Carolina, dilapidated housing for low-income residents was replaced with double-wide manufactured homes. It was estimated that the infill housing was about half the cost of a similar site-built home.

Knack presents proponents of the idea to bring manufactured-housing factories and homes to the inner city. She quotes Don O. Carson, editor and publisher of Automated Building magazine, "After the disturbances that followed the Rodney King beating in Los Angeles," he says, "it occurred to us that we ought to start building housing factories in the inner city that would employ local people and teach them skills" (p. 11).

New alliance develops affordable housing for urban areas. 1998. *Freddie Mac News Archives* online, October 14.

Nickerson, Craig S.
1999. Housing partnership. *Urban Land* 58(3):74-77.
Both articles discuss the Manufactured Housing Alliance formed by Freddie Mac, the Manufactured Housing Institute and the Low-Income Housing Fund to promote manufactured housing as a tool for revitalizing urban communities by increasing home ownership. Freddie Mac committed to provide financial assistance to LIHF to help nonprofit housing developers cover predevelopment and development costs of pilot projects. MHI would bring in members of the industry to complete the projects, which would begin in at least five cities initially. Freddie Mac would identify lenders to finance the mortgages once the homes were ready for sale, then purchase these mortgage loans from those lenders. The alliance evolved from the Urban Design Demonstration Project, initiated by MHI in 1997.

Lessons learned include:

- Work closely with local government, community organizations and area residents to promote acceptance and enthusiasm for the product.
- Design homes to fit the neighborhood context.
- Move quickly in order to hold neighborhood support.

Residential property: Manufactured housing
1999. *Assessment Journal* 6(3):80.
This brief report outlines the case of Miner and Miner v. Story County Boards of Review (1998), in which the Court of Appeals initially rejected any notion that the district court or the court of appeals is without authority to make its own fair market valuation. However, the court of appeals found that the assessments given by the expert witnesses presented by the taxpayers were not credible. The court of appeals found an analysis by the county assessor factoring in sales of manufactured homes to be the best indicator of the fair market value of the property, and reversed the district court's decision that the initial review board's assessment of value had been excessive.

Stephenson, Richard and Guoquiang Shen
1999. *Identification and Measurement of Zoning Barriers Related to Manufactured Housing: A Location and Accessibility Analysis.* Greenville, NC: East Carolina University.
This study examines what impact zoning has on manufactured-housing placement, along with its proximity to "positive" versus "negative" public facilities. For the purposes of the study, "positive" facilities included environmental, health and emergency rescue services; cultural, recreational and education services; and auto, food, shopping and other business services. "Negative" facilities include landfill and solid-waste sites and other similar uses. Findings include:

- Manufactured housing is located farther from "positive" community facilities, which is especially significant in the area of life-safety services.
- Manufactured housing is located closer to "negative" public facilities such as landfills and solid-waste facilities.
- Zoning districts where manufactured housing is a permitted use have a higher percentage likelihood of being located in flood zones.

The general conclusion is that many of the negative perceptions of manufactured housing are in fact self-fulfilling prophecies perpetuated in part by the limited placement opportunities created through local government's zoning actions.

White, S. Mark. 1996
State and federal planning legislation and manufactured housing: New opportunities for affordable, single-family shelter. *The Urban Lawyer* 28(2):263-292.
White maintains that the fact that only one in four low-income households in inner cities is a homeowner leads to the deterioration of urban neighborhoods and contributes to urban sprawl. While providing affordable shelter, manufactured-housing communities can also accommodate local planning concerns relative to neighborhood preservation, community character, open space and environmental protection through innovative site design. Misperceptions of the quality, safety and compatibility of manufactured homes have stifled the siting and construction of this form of shelter in some communities.

- In 1994, 339,601 manufactured homes were shipped in this country, representing an 80 percent increase over the number shipped in 1990.
- The average cost per square foot to produce a manufactured home in 1994 was only 46 percent of the average cost to produce a site-built home.

The article provides an overview of recent state planning legislation and its impact on manufactured housing. Exclusionary zoning litigation and antidiscrimination legislation provide useful tools for removing unnecessary barriers to the construction of manufactured housing. However, comprehensive planning legislation provides a basis for quantifying the need for housing among various income levels in a community, and accordingly the removal of barriers that lead to expensive and antagonistic litigation. This article describes how manufactured housing is used to accommodate local affordable-housing needs within the context of a comprehensive plan.

Wilden, Robert W.
1995. Manufactured housing: A study of power and reform in industry regulation. *Housing Policy Debate* 6(2):523-537.
The article describes the importance of manufactured housing as an affordable-housing alternative, and also the regulatory system that manufactured housing is subject to. The information is presented through a case study of the National Commission on Manufactured Housing and its attempts to reform the regulatory system. It chronicles the ultimate failure of regulatory reforms and shows that while the short-term prospects for reform are not good, the long-term prospects are better. Manufactured-housing placements account for approximately one in five of all single-family completions plus manufactured homes installed each year.

Prospects for long-term reform are better because (1) a few large manufacturers are upgrading warranties, (2) states are improving their oversight of installation, and (3) there is reason to believe that regulatory functions will be moved away from HUD and given back to the states.

VIII. STANDARDS

[QUALITY, CONSTRUCTION, DEVELOPMENT, SAFETY, PERFORMANCE]

de Alessi, Louis
1996. Error and bias in benefit-cost analysis: HUD's case for the wind rule. *Cato Journal* 16(1):129-147.
The author asserts that benefit-cost analyses conducted by third parties which resulted in the July 1994 adoption of the wind rule by HUD were inherently flawed. Limitations of the analyses include that the choices used to structure and conduct the analysis were guided by the preferences and constraints of the individuals managing the analyses, rather than by those of the individuals affected by the rule, so the findings disregard the distribution of gains and losses. The study also assumed that the proposed rule would work perfectly as implemented in practice. In addition, the benefit-cost analysis itself, even within these limitations "is riddled with errors."

Dream home...or nightmare? 1998. *Consumer Reports*, February; available online at
www.consumerreports.org/main/detailv2.jsp?CONTENT%3C%3Ecnt_id=18967&FOLDER%3C%3Efolder_id=18151&bmUID=1029787914016.
The message of the article is that manufactured housing has come a long way, but there are still some dangers for consumers in the market. In a two-year examination of the industry, including a national survey of 1,029 consumers and tours of factories, dealer lots and mobile-home communities, Consumer Reports found that problems arise most often in lower-cost mobile homes. They also found that HUD regulations have improved overall quality but that gaps in regulation exist, particularly regarding installation. Findings included:

- Manufactured housing can last as long as site-built housing. More expensive mobile homes have fewer problems. Cheaper models typically have lower-quality materials that wear out quickly or are easily damaged
- Eighty-two percent of survey respondents reported that they were largely satisfied with their home, but a majority—even those whose home was less than five years old—also said they had had at least one major problem.
- Consumers who lease the land on which their manufactured house sits, including just under half of the survey respondents, are vulnerable to sudden, and sometimes dramatic, jumps in the rent on their lots. Those who cannot afford the increases or who lose their lease have few options other than to bear the expense of having their home moved. Or they can sell —often to the landlord at a distress price.

Installation: Manufactured homes are commonly set on piers and tied to the ground with steel straps. State and federal regulators say manufactured homes are often installed incorrectly, accounting for more than half the problems consumers report.

The buyer's maze: Ten manufacturers, each building homes configured in a range of floor plans and interior decors, account for nearly three-fourths of all factory-built housing units made. But most dealers who sell manufactured homes have only a narrow selection from a few makers on display, making it difficult to compare brands and models side by side.

Siting: Many municipalities discriminate against manufactured housing through restrictive zoning. Some park owners try to pressure buyers who want to lease a site in their community into buying from a retail outlet they own. If the prospective homebuyer wants to lease land in a park that has few vacancies, he or she may be pressed into buying a home that is already on the site. Of the consumers surveyed, 61 percent bought their home from a dealer, 22 percent bought from the previous owner, and 7 percent bought from a park.

Costly financing: Loan terms for manufactured-home buyers are superficially similar to those of conventional mortgages. Putting as little as 5 percent down, a borrower can take out a loan to be repaid over a period of 15 to 30 years. Government-backed FHA and VA loans are available to buyers who qualify. Like owners of site-built homes, consumers who reside in their home are permitted to deduct interest payments from their federal income taxes. But in other major respects, financing a mobile home is more like taking out a car loan. Overall, interest rates on mobile-home loans typically run some two or three percentage points higher than those for a conventional mortgage.

Dealers typically work with a handful of lenders, and they try to steer the prospective buyer to one of them so they can close the deal before the customer leaves the lot, effectively eliminating the opportunity to shop for better terms. The nation's largest mobile-home lender, Minnesota-based Green Tree Financial Corp. (now Conseco), for example, says it can extend conditional loan approval to would-be buyers within an hour of receiving an application through a dealer. Some manufacturers, such as Clayton Homes and Oakwood Homes, operate their own retail outlets and proprietary finance companies.

Defaults: Lenders justify the higher rates by pointing out that borrowers who buy manufactured homes are more likely to default than are traditional mortgage borrowers. Some 12 percent of all manufactured-home loans end up in default over the life of the loan, a rate that is four times higher than that for conventional home mortgages. But default rates may also be high because many mobile homes, especially those installed on a leased lot, lose value over time.

Insurance: Homeowners insurance on manufactured housing is also costlier than for a traditional home because mobile homes are more vulnerable to storm damage.

Parks: There are about 50,000 mobile-home parks throughout the U.S. Four publicly traded companies - Chateau Communities, Manufactured Home Communities, Sun Communities, and United Mobile Homes - operate 300 parks. One of the biggest makers of factory-built housing, Clayton Homes, owns 67 parks. Others are managed by dealers.

Insecure leases: Tenants are vulnerable to the vagaries of landlords. Even in the 34 states that provide tenants with some legal protection, regulations lack much enforcement bite.

Gordon, Jeffrey and William B. Rose
1998. *Code Comparison Study: MHCSS vs. CABO One- and Two-Family Dwelling and Model Energy Codes.* University of Illinois at Urbana-Champaign School of Architecture.
This study compares the applicable requirements of standards for construction of a home built to the federal

Manufactured Home Construction and Safety Standards (HUD code) with the CABO One- and Two-Family Dwelling Code and Model Energy Code. The comparison concludes that while in some areas the HUD code requirements are more restrictive, and in other areas the CABO codes are, on balance the two codes are comparable, resulting in houses that perform similarly.

Meeks, Carol B. 1995. *Manufactured Home Life.* Arlington, VA: Manufactured Housing Institute.
This report estimates the full-time occupied life and overall housing-stock life of manufactured homes.

—. 1998. *Manufactured Home Life: Existing Housing Stock Through 1997.* Arlington, VA: Manufactured Housing Institute.
This study is an update to the 1995 study, and found that recently built units have a useful life of 55.8 years.

Meeks used manufactured-housing shipment data from 1945 to 1997 (as reported by NCSBCS to the Census Bureau), adjusted for differences in data collection over time, and estimated inventory using the American Housing Survey to adjust for seasonal and vacant units. Expected Habitable Life Estimates derived from the rate of attrition between the number of manufactured-housing shipments and the estimated inventory. The loss rate was based on the last 20 years. Year-round occupied life was estimated based on the age distribution of housing by year as reported in the 1995 AHS. The results of the study include:

- A habitable life expectancy of 71.4 years was calculated for manufactured housing.
- A year-round occupied life expectancy of 57.5 years for new manufactured homes produced in 1995 was estimated.
- Thus manufactured-housing home life is observed to have increased over the four decades of data.

Sanders, Welford
1996. Regulating manufactured housing. *Urban Land* 55(1):46-49.
The HUD code does not regulate installation, but about half of the states have adopted regulations. The following states prohibit exclusion and unfair regulatory treatment of manufactured housing: California, Colorado, Connecticut, Florida, Indiana, Iowa, Kansas, Maine, Michigan, Minnesota, Montana, Nebraska, New Jersey, New Mexico, North Carolina, Oregon, Tennessee, Vermont and Virginia. Additionally, California, Iowa, Kansas and Minnesota require parity of treatment.

Frequently, manufactured homes can only be sited in manufactured-housing communities. When they are allowed alongside site-built homes, the design standards tend to be more rigorous. Also, a typical manufactured-home community has small lot standards, which increase density and therefore affordability.

- Six to eight units per gross acre is fairly standard, and densities are often higher.
- Some area is generally given over to common space.
- Twenty-foot setbacks from the front are often required, and four to eight feet from the side of lots is common, although some communities allow zero-lot-line zoning.
- Ten to twenty feet of separation between homes is typical.
- Landscaping is especially important in high-density developments.
- A common requirement for a single-family dwelling unit is two parking spaces.
- Many rental parks employ rent control, often due to concern for elderly residents with fixed incomes.

—. 1998. *Manufactured Housing: Regulation, Design Innovations, and Development Options.* Chicago, IL: Manufactured Housing Institute and the American Planning Association.
This report examines development standards for manufactured housing and discusses land-development provisions which allow HUD-code homes to be used in neighborhoods. Development standards in communities are compared, and regulatory issues such as location restrictions, appearance standards and installation requirements are covered. It includes a detailed discussion of design innovations and case studies illustrating best practices. MHI's Urban Design Project case studies are also featured, illustrating how manufactured homes can meet compatibility standards of existing neighborhoods. This document is useful for those seeking to find a way to make manufactured housing part of the local housing stock. It includes a guide to drafting reasonable and effective local regulations.

Schriever, W.R. 1977. Wind forces on mobile homes. *Canadian Building Digest* 188, June.
The author reported that there were 200,000 mobile homes in Canada and that number was rapidly increasing. In 1974, 21 percent of single-family detached homes constructed were mobile homes. Wind damage to mobile homes comes not just with extreme weather events; thunderstorms can push an unanchored home off its blocks, a cause of concern to residents,

insurers and building-code authorities. Most codes require anchoring, but are often not enforced. The article describes the types of ties against wind forces and illustrates them with sketches. It concludes that municipal authorities, builders and owners should be aware of the potential hazard of wind damage and should ensure that all single-section mobile homes are properly anchored.

Tully, Gordon and Steven Hullibarger
2000. *Manufactured Home Producer's Guide to the Site-Built Market.* Steven Winter Associates, for the HUD Office of Policy Development and Research.
This guidebook includes chapters on negotiating finance and design issues, construction and production details, and manufacturer and developer agreements as well as case studies. Design and construction information is detailed and includes illustrations.

U.S. Department of Housing and Urban Development.
2000. *Homebuilders' Guide to Manufactured Housing.* Washington, DC: NAHB Research Center.
This guidebook is written for conventional builders and land developers, and provides an introduction to manufactured housing. It highlights the differences between manufactured and conventional homes that are likely to be encountered in practice.

—. (Biennial.) *Report to Congress on the Manufactured Housing Program.* Washington, DC: HUD.
This biennial report on HUD administration of the National Manufactured Housing Construction and Safety Standards Act of 1974 covers manufactured-home standards development, enforcement activities of state administrative agencies and primary inspection agencies, research, accidents, and structural deficiencies. Data are drawn primarily from the National of States on Building Codes and Standards, Consumer Project Safety Commission National Electronic Injury Surveillance System, other federal and state agencies and various private sources. Publication began with an annual report for 1975, suspended for the 1982 to 1983 period and resumed in 1988 to 1990.

Warner, Kate and Robert Johnson
1993. *Manufactured Housing Research Project.* Ann Arbor, MI: University of Michigan.
***Report 1: Manufactured Housing Quality,* Robert Johnson.**
This report finds that manufactured housing has effectively demonstrated reasonable performance in the areas of structural durability, maintenance, wind safety, fire safety and thermal efficiency. It states that while there is room for improvement in some areas, "the manufactured home has essentially become equivalent to that of conventional housing."

It discusses the technological and production advantages of manufactured housing. In comparing the HUD and BOCA codes, it finds they are similar and that in some cases the HUD code is more restrictive. Johnson argues that the inspection systems for manufactured housing are more comprehensive than for site-built housing.

Johnson cites other research showing that there are no major quality differences between manufactured and site-built homes in terms of structural performance and maintenance and repair problems. Insurance-company data indicate that manufactured-home plumbing fixtures and roof problems generated the greatest number of complaints. Other findings include:

- There has been a drop in fire incidents in manufactured homes since the HUD code was instituted. Research suggests that manufactured-home fire safety is no different from that for site-built homes.
- Manufactured homes that use wind-stabilization systems or are located on permanent foundations suffer damage similar to site-built houses and show no additional vulnerability.
- There has been a demonstrated improvement in heating and cooling characteristics of manufactured homes since the HUD code was instituted.

JUN 1 0 2004

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20410

Established in 1934, Title I is FHA's oldest program. The program's presence in the marketplace has shifted since its inception, as lenders and borrowers have opted to take advantage of more cost effective financing options available through FHA's Title II programs and conventional programs, such as Home Equity loans. As a result, the Title I programs have experienced an overall decline in volume and significant financial losses. To address these issues, in November 2001, FHA issued a new regulation, "Strengthening the Title I Property Improvement and Manufactured Home Loan Insurance Programs and Title I Lender Approval Requirements." The Department also established a working group of FHA managers and staff who have been engaged in ongoing policy discussions and meetings to address programmatic weaknesses. Finally, FHA secured an independent contractor to undertake a business process improvement study (attached) to evaluate and identify ways to improve the Title I programs

The contractor was asked to assess whether FHA's Title I programs represent a feasible and attractive alternative to conventional market products and whether the programs needed to be modified to better meet the needs of borrowers and lenders. To answer these questions, the contractor conducted a comprehensive market analysis, which included surveys with Title I lenders, meetings with FHA managers and staff administering the programs, and general market research. The findings and recommendations presented in the final report identify features of the programs that pose unnecessary risk to the FHA and that represent barriers to lender and borrower participation.

The attached report, "The Federal Housing Administration (FHA) Final Title I Business Process Improvement (BPI) Report," represents an assessment of the Title I program performed by an independent contractor for the Department of Housing and Urban Development (HUD). The findings, recommendations, and conclusions published in this report do not represent the policy position of the Department nor serve as an indication of the Department's policy direction. The information provided to HUD in this report was intended only to inform the Department of changes in the market and industry, and to help HUD evaluate how to improve the program to better meet the needs of borrowers and lenders.

Any potential policy changes would be proposed in the rulemaking process, affording the public an opportunity to comment on proposed program changes, a process that can take twelve months or longer to complete. Such a process, if pursued would not begin until the beginning of FY2005.

June 6, 2003

Ms. LaVerne L. Hall, GTR
U.S. Department of Housing and Urban Development (HUD)
451 7th Street, S.W., Room 2220
Washington, D.C. 20410

Reference: Contract Number: C-FTW-00376
Document Number: BPR-001-028

Subject: *Final Title I Program BPI Report*
U.S. Department of Housing and Urban Development (HUD)
Title I Business Process Improvement (BPI)

Dear Ms. Hall:

Enclosed please find the Final Title I Program BPI Report deliverable. This report represents the contract document numbered BPR-001-028, encompassing the final improvement considerations for both Property Improvement and Manufactured Housing.. Frontline appreciates the opportunity to support your process reengineering needs, and looks forward to working with you in the future.

If you have any questions, please feel free to call me at 703-256-7040, or send an electronic message to jrodgers@front-line.com.

Sincerely,

/signed/

Janice Y. Rodgers
BPR Title I Program Manager
Frontline Systems, Inc.

cc: Mary Worthy
Ruth Roman

Enclosures

U.S. Department of Housing and Urban Development (HUD)
Federal Housing Administration (FHA)
Office of Single Family Program Development

FEDERAL HOUSING ADMINISTRATION (FHA) TITLE I BPR

FINAL TITLE I PROGRAM BPI REPORT DELIVERABLE

Document: BPR-001-028

June 6, 2003

Contract C-FTW-00376

Frontline Systems, Inc.
7617 Little River Turnpike
Suite 960
Annandale, Virginia 22003

FEDERAL HOUSING ADMINISTRATION (FHA) FINAL TITLE I PROGRAM BPI REPORT

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1 EXECUTIVE SUMMARY

The Office of Single Family Housing (Program Development) in the Federal Housing Administration (FHA) has undertaken a Business Process Improvement (BPI) Project to improve loan lifecycle processes in Title I insurance for property improvement and manufactured housing (titled as personal property) loans. In support of this effort, Frontline conducted process analysis and benchmarked industry best practices to develop several possible implementation options. The overall purpose of these options is to improve program viability by modernizing Title I Program operations and utilizing automation to streamline paper-intensive processes.

Modernize Title I Program Operations

Title I Program modernization involves improving the policies and the processes that support the Title I Program based on current market conditions and industry best practices. FHA should consider focusing resources on key improvements that increase loan volume, reduce program complexity, and reduce the Department's risk. Key improvements developed from this study are listed below and are organized into Title I Insurance changes (policy changes and insurance structure modifications) and underwriting clarifications:

- Policy Changes: Update Property Improvement and Manufactured Housing Program characteristics to respond to changing market conditions, take advantage of the Title II insurance structure and mitigate risk. Options include:
  - Modify Property Improvement characteristics to include eliminating multifamily properties; baring dealer and investor participation; re-implementing equity requirements; requiring a minimum loan amount; raising loan limit ceiling; and modifying credit criteria.
  - Modify Manufactured Housing characteristics to include raising loan limit ceiling; eliminating lot only loans; modifying credit criteria; clarify homesite and installation requirements; and modifying appraisal requirements.
- Insurance Structure Modifications: Evaluate changing the conditional co-insurance structure to the Title II insurance structure to increase competitiveness of the loan product, increase lender participation and simplify program administration.
- Underwriting Clarifications: Update and clarify underwriting guidelines to improve loan quality and mitigate the inherent risk associated with moving the program towards the Title II insurance structure.
  - Review developing a Title I automated credit scoring model that would identify key risk areas and lead to development of a tailored scorecard.
  - Review the sufficiency of current underwriting guidelines, analyze the need for additional guidelines, and develop and document these guidelines through updated program handbooks.

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- Develop and implement Title I training for FHA staff and industry partners to communicate underwriting and program characteristics.

Automate Paper Intensive Processes

By reengineering its loan processes and leveraging best practices, FHA can realize processing efficiencies by implementing key automation improvements. Several of these improvements can be modeled after FHA's Title II Program to leverage the current infrastructure of Title II and the various risk management initiatives designed and implemented into the systems. These automation improvements will enable FHA to simplify the program, automate risk management, and improve program oversight and quality control. The following automation improvements support these benefits:

- Simplify the Program
  - Update loan documents to reflect industry standards
  - Enable lenders to electronically submit Title I loan data via FHA Connection
  - Track Title I underwriters in FHA systems
  - Update active Title I lenders on the U.S. Department of Housing and Urban Development's (HUD's) website
  - Integrate the Title I origination and claims systems into Title II's systems
- Automate Risk Management
  - Implement an automated scoring model
  - Implement Title II's portfolio scoring concept that reassesses risk on a regular basis
- Improve Program Oversight and Quality Control (QC)
  - Collect additional data on the borrower and transaction prior to endorsement
  - Implement Quality Control database to track loan participants and performance
  - Develop targeted reports/decision support system to identify and track trends throughout the loan lifecycle

In this document, Frontline presents implementation strategies to realize the program modernization and automation improvement options outlined in this Executive Summary. Section two of this BPI focuses on program modernization. It presents improvement options organized into policy changes, insurance structure modifications, and underwriting clarifications. Additionally, it details the specifics of implementing those options, by defining the actions to be completed, estimating the time needed for each action, explaining the benefits, and discussing the risks associated. Section three of this BPI centers on process automation. It presents automation improvements that simplify the program, automate risk management, and improve program oversight and control. This section also details the specifics of implementing those options, by defining actions to be completed, estimating time needed for each action, explaining the benefits, and discussing the risks associated. For additional information on the rationale for the BPI's improvement considerations please refer to the appendices of this report.

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2 MODERNIZE TITLE I PROGRAM OPERATIONS

As FHA moves forward in improving the policies and procedures of the Title I Program, FHA should consider modernizing several program components. Modernization of these components is based on current market conditions and industry best practices. The findings of this BPI suggest that improvements should focus on increasing loan volume, reducing program complexity, and reducing the Department's risk. Key improvement options to support these objectives are listed below and are organized into Title I Insurance changes and underwriting clarifications.

2.1 Title I Insurance

The Title I co-insurance structure is a conditional portfolio program. FHA maintains a reserve fund on behalf of each approved financial institution equal to 10 percent of the cumulative amount of the principal balance of all Title I loans in its portfolio. If the borrower defaults on the loan, FHA pays a claim to the lender equal to 90 percent of the net unpaid principal balance plus accrued interest, uncollected court costs, attorney's fees, and recording costs up to the amount of funds available in reserve. The conditional nature of this insurance structure coupled with the 10 percent limitation on lender claims, provides extensive risk protection for FHA. Although this protection exists, it is overly complex, requires separate maintenance procedures/systems and limits the participation of the lending community. Within this structure, if lenders do not follow all program requirements during the underwriting, servicing and claims processes, claims will not be paid.

The purpose of this structure is to incorporate accountability for the lender, who assumes a portion of the risk. Title I has utilized this structure since its inception due to the high-risk nature of the types of loans insured in this program. Since the market has changed considerably since Title I was developed, lenders now have more conventional options and have become far less likely to use a program that does not give them a guaranteed claim, or a program which is overly complex with respect to administrative procedures, (i.e., paper processes and time to finalize the loan). Additionally, secondary markets have become less likely to buy loans without the same assurance. This perception by the financing community led to a dramatic decrease in lender and secondary market participation in Title I lending. As loan volume declined, liquidity became unstable, which further contributed to a high-risk loan portfolio. Further evidence of this history can be analyzed by reviewing the program's endorsements, insurance in force and claim data in the actuarial overview in Appendix E.

To address the need to simplify the administration of the program and to revitalize lender and secondary market participation, FHA should consider two key improvements, which would dramatically revise the Title I Program. The first improvement suggests implementation of several policy changes to the program. These changes range from statutory, regulatory, and process actions, and offer program modernization solutions that serve to minimize risk and simplify administration. The second improvement FHA should consider is altering the conditional insurance structure. This requires changing the structure to offer 100 percent loss

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reimbursement (Title II Insurance). Both short and long term considerations are included in this alternative, and implementation of either action requires a complete program impact analysis. The following sections detail these key improvements as well as provide high level timelines, implementation actions, and associated risk and mitigation points.

2.1.1 Policy Changes to the Program

In order to simplify administration, mitigate risks, and support future changes to the insurance structure of the program, FHA should consider several Title I policy changes. To implement these changes FHA must seek statutory authority, regulatory changes, and process changes. The following initial program modifications are introduced below and separated by property improvement and manufactured housing:

PROPERTY IMPROVEMENT: The Property Improvement Program enables borrowers to improve their property if they qualify for the loan. The following statutory, regulatory and process changes are listed below for the Property Improvement Title I Program.

1. Statutory

- **Eliminate Multifamily Properties.** Few multifamily loans are made (about 100 per year), and multifamily rules are vague, often causing complex issues to arise. The current definition of a multifamily property eligible for a Title I loan is limited to "a loan to finance the alteration, repair, improvement, or conversion of an existing structure used or to be used as an apartment house or a dwelling for two or more families. The multifamily structure may not be owned by a corporation, partnership, or trust, unless the prior approval of the Secretary is obtained for an exception to this requirement." FHA should consider eliminating multifamily participation in the Title I Program, as these loans are usually made by investors and subject to greater instances of fraud and abuse. Other FHA programs such as 203(k) allow for multifamily improvements and have stricter definitions and corresponding oversight procedures.
- **Eliminate the Dealer Program.** Dealer participation in the Property Improvement Program dates back to The Great Depression and was intended to create employment opportunities during this time period. Traditionally, it has been the portion of the program with the most fraud and resulting negative publicity. With the introduction of the 2-party check (Title 1 Letter-473), the number of dealer loans has dropped drastically. In recent years, the Dealer Program has served primarily as a marketing tool. The Dealer Program is considered by much of the lending industry to be archaic and inefficient. It also presents an increased risk to the insurance fund. If FHA considers providing lenders with a revised insurance structure for Title I loans, this incentive should be sufficient to encourage participation and self-market the Title I Program, hence eliminating the need for and risk associated with this third party participant.
- **Bar Investors from Using the Program.** Investors leave the program open to fraud and abuse, and allowing their participation no longer seems to be in line with the purpose of the program, which is to provide financing options for borrowers with few options in the conventional market.

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- **Mirror Conventional Home Equity Loans for all Property Improvement Loans.** FHA should consider requiring equity on all property improvement loans. This change would help to mitigate risk by strengthening FHA's ability to foreclose on a property, thus improving Title I's asset recovery rates. FHA should base its loan structure on the current conventional Combined Loan to Value (CLTV) structure.
- **Require Minimum Loan Amount.** Currently, the Title I Property Improvement Program has no minimum loan amount. FHA should consider requiring a minimum loan amount of $5,000. This would serve to limit use of the program to borrowers requiring larger repairs that may have few other financing options. As industry analysis suggests, borrowers requiring funds below this proposed minimum loan amount have many alternatives in the conventional market.
- **Raise Loan Limit Ceiling.** FHA should seek statutory authority to change the property improvement loan limit to 20 percent of the maximum mortgage amount allowable for Title II mortgages. This should also eliminate the need for the high-cost allowance for Title I loans. Implementation of this recommendation would provide greater program flexibility and allow a faster reaction time should FHA determine in the future that the current loan limits are no longer sufficient to meet borrower needs.

2. Regulatory

Modify Credit Criteria. FHA should consider utilizing an automated scoring model to improve the quality of loans in the Title I portfolio. A method similar to the Title II Scorecard should be considered, to establish the appropriate debt ratio and other credit criteria for Title I. This consideration would enable FHA to mirror industry and internal best practices. In the interim, FHA should consider industry interviews that suggested lowering the current debt ratio from 45 percent to 35 percent.

3. Process

- **Utilize a Direct Endorsement (DE) Underwriter Tracking System Similar to the Underwriting Report System (URS) Used by the Home Ownership Centers (HOCs).** FHA should consider using this URS to help mitigate risk and improve underwriting quality in the Title I Program by allowing FHA to track, monitor and sanction Title I underwriters.
- **Develop a Title I QC Database.** FHA should consider using a QC database (currently in the planning stage for Title II Programs) to determine whether the key participants (e.g., lender, loan officer, and underwriter) in the Title I transaction have been involved in previous FHA Title I loans that resulted in serious monitoring findings and/or significant losses to the Department. In support of this database, additional data would need to be collected on the participants in the transaction. The two major benefits of this database are to give lenders access to possible fraudulent participant activity and to allow FHA to monitor participants and track trends in loan performance based on findings.

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MANUFACTURED HOUSING: The Manufactured Housing Program enables qualified borrowers to obtain affordable manufactured housing that is titled personal property. The following statutory, and regulatory changes are listed below for the Manufactured Housing Title I Program.

1. **Statutory**

   - **Raise Loan Limit Ceiling.** FHA should consider raising current Title I Manufactured Housing loan limits because, based on today's sales prices, current loan limits only allow Title I borrowers to purchase singlewide homes. In today's market, singlewide homes have become unpopular and are prone to more rapid depreciation. Also, market data suggests over one-third of all manufactured homes sold today are multisection. To set the new loan limit ceiling, FHA should consider using the average price for a mid-range multisection as an appropriate and useful loan limit to finance the structure only, for a chattel-type loan. For home and lot loans, loan limits should match Title II home and land loans, to enable more sufficient financing for homes with land that cannot be titled as real property.

   - **Eliminate Lot Only Loans from Title I.** FHA should consider eliminating lot only loans from the Title I Manufactured Housing Program. Currently, manufactured home park communities that are undergoing co-operative conversions find borrowers using Title I lot loans to purchase their share of the community land. Shares in a cooperative association cannot be appraised, repossessed and resold in the event of a default in the loan payments. In order to file a claim on a share-type loan, it is treated as a lot loan that requires the appraisal and resale of the property prior to filing a claim.

2. **Regulatory**

   - **Modify Credit Criteria.** FHA should consider utilizing an automated scoring model to improve the quality of loans in the Title I portfolio. FHA should consider using a method similar to the Title II Scorecard to establish the appropriate debt ratio and other credit criteria for Title I. This consideration would enable FHA to mirror industry and internal best practices.

   - **Clarify Homesite and Installation Requirements.** FHA should consider modifying the placement certificate to include greater detail, to ensure the home is compliant with manufacturers' specifications. This consideration could aid considerably in protecting the home's value as well as the homebuyer since the most frequent consumer complaints from manufactured homeowners center around problems resulting from poor installation of the structure. Minimizing unnecessary deterioration of the structure due to poor installation clearly contributes to these homes holding their value. Additionally, upfront evaluation of the site certification will ensure, for example, that individual well and sewer facilities are available and appropriate for the structure. For those structures that are placed in manufactured home park communities (land-lease), the same site certification should be required, to ensure that the structure is properly connected to facilities that adequately support the community. Comparatively, the Title II Program encourages permanent site selection by providing architectural specifications to install enclosures around the structure, for example. For a Title I loan lot combination, FHA may consider

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applying the same requirements, to discourage moving the structure, and to further enable the home to appreciate in value.

- **Modify Appraisal Requirements.** FHA should consider, for those loans that are structure only, to allow state-licensed or certified personal property appraisers using the National Automobile Dealers Association (NADA) cost approach value guide to conduct the appraisal (no NADA approval required). Current FHA regulations require a NADA appraisal on an existing (used) manufactured home to establish the value of the home so that a determination can be made as to how much the required down payment should be when the financing uses the Title I Program. This change will alleviate the appraisal problem of the inability to obtain legitimate comparable sales data. Also, it will eliminate the problem of the costs and wait time associated with finding and hiring a NADA-approved appraiser. FHA should also consider, for those loans that are structure and lot combinations, requiring FHA appraisers who have added the certification of the 669 course, to ensure the home is appraised accurately by a real estate appraiser that is qualified to assess land value. This change could contribute to stabilizing the depreciation that has historically plagued the industry.

2.1.2 Insurance Structure Modifications

Findings suggest that modifying the Title I Program to provide 100 percent loss reimbursement to insured lenders (the Title II insurance structure) and modifying program components to simplify the program, mitigate risk and align it with the conventional market (as discussed in Section 2.1.1) will provide the greatest impact toward rebuilding the program to self-sustainability (though not a requirement), and equip borrowers with a more valuable loan product. This structure has proven to be effective in FHA's Title II Program, and thereby serves as a best practice to Title I.

If FHA considers changing the conditional coinsurance structure of Title I to 100 percent full insurance, FHA must seek statutory authority to make this change. This change is considered a long term action and would require a full separate analysis of the risks and benefits involved, premium structure impacts, and indemnification policy changes (See Appendix I for the Title II Indemnification Policy). This change would require several years to implement. In the interim to achieving this 100 percent full insurance, FHA should consider changing the insurance structure to guaranteed but keep the coinsurance structure in tact. Lenders and the secondary market would be assured of claim payments, but would continue limiting claim payments to 90 percent per claim and 10 percent per portfolio. This change could be implemented in the short term and it would only require a regulatory change. This interim solution would serve to keep premium rates at a reasonable level and limit FHA's exposure to risk while the full insurance option is explored and further analyzed.

2.1.3 Timeline

The estimated timeline for implementing the Title I Insurance changes (policy changes and insurance structure modifications) is extensive. The timeframe estimate is three years. A high-level action list is included in the section below. A significant planning effort would need to take

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place to identify a complete list of statutory, regulatory, and process changes to implement this option.

The Revise Title I Insurance Project Schedule is depicted in Figure 2.1 below. The schedule shows the major actions necessary to complete this project and the estimated length of time for each action. To fully understand how this consideration will fit within the context of the other considerations identified in this report, refer to the BPI Project Plan in Appendix M.

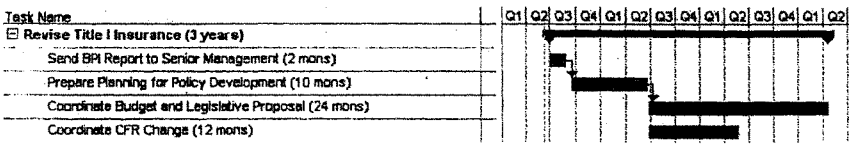

Figure 1 Revise Title I Insurance Project Schedule

2.1.4 Actions

1. Send BPI Report to Senior Management for approval to explore implementing the statutory and regulatory changes. **(2 month)**
2. Prepare planning for policy development. **(10 months)**
   - Organize team of program officials from Title I and Title II
   - Read BPI Report and discuss policy change modifications
   - Develop draft considerations for change (statutory, regulatory, and policy) based on planning meetings
   - Finalize considerations and send to Senior Management for approval to involve FHA Commissioner
   - Send to FHA Commissioner for approval
   - Develop plan to implement the policy changes as appropriate
3. If the decision is made to pursue a statutory change for 100 percent full insurance, FHA needs to coordinate the budget and legislative proposal submission. **(24 months)**
   - Develop costs and benefits proposal for budget call
   - Send budget call draft proposal to FHA Commissioner for approval
   - Finalize proposal for next budget call
   - Budget and Legislative Submission is submitted to U.S. Office of Management and Budget (OMB) for approval.
   - OMB submits to the Hill and proposals are voted on and approved as appropriate.

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4. If the decision is made to pursue a regulatory change for guaranteed insurance with the reserves in tact as an interim solution, FHA needs to coordinate internal actions necessary for a code of federal regulations change. **(12 months)**

2.1.5 Benefits

- Ensure program is modernized to current market conditions.

  Implementing key policy modifications that include statutory, regulatory and process changes will enable FHA to update the Title I Insurance Program, reduce risk to the Department and simplify the program.

- Ensure claims will be approved upfront encourages lender participation.

  Currently, lenders do not know if a claim will be approved until it is filed, essentially putting all of the risk on the lender if compliance to FHA underwriting standards is unclear. Many Title I lenders have not participated in recent years because of the difficulties they've had getting claims approved. The reserve system has traditionally caused confusion in the lending community.

  Additionally, the reserves system that currently supports Title I has proven to be restrictive for many lenders to continue to do business. "For both property improvement and manufactured housing," claimed one HUD representative, "a lot of claims are not paid because reserves are used up." This is usually because the lender has not conducted prudent underwriting.

- Encourage secondary markets to buy loans.

  Government Sponsored Enterprises (GSE) that were interviewed for this study concluded that their challenges with Title I were due to the constant change of the program, and the resulting impact on their investment. As purchased loans would go into default, GSEs would attempt to locate the lender to sell back the loan, often without success. A revised insurance structure will minimize the effect of this type of event, as GSEs will be able to recover the loss.

  Additionally, Fannie Mae re-allocates reserves to provide coverage back to its lenders that have no reserve balance, as a means of maintaining the lending operations of their business partners. One-hundred percent insurance will eliminate the need for reserves, which will terminate this additional burden of managing reserve balances for lenders and GSEs.

- Make Title I more competitive.

  Migrating the program away from reserves, toward 100 percent insurance will create a viable alternative for lenders who currently select conventional private mortgage insurance because of the complexity of the reserves in Title I.

2.1.6 Risks/Possible Controversies

- There are many risks when making the policy changes suggested in this report. Since these policy changes mostly suggest changing the program to protect FHA and improve the viability of the product, most risks are attributed to industry's acceptance of the changes. If

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FHA decides to implement these changes, careful consideration must be taken for lender and secondary market communication and impact.

- From an organizational standpoint, the insurance changes suggested would greatly impact the responsibilities and work processes completed by the Financial Operations Center (FOC). A complete review needs to take place on what future processes the FOC would be responsible for and how to better leverage their extensive knowledge of the Title I Program under the new structure.

- The increased risk imposed upon FHA to provide 100 percent upfront coverage may result in lenders applying less stringent standards in their underwriting practices. More explicit underwriting guidelines and loan data, which can be approved during loan origination, will serve to mitigate this risk. However, the greatest risk to FHA from such a change to the financial structure is likely to be the transitional impact resulting from operational and system modifications to support Title I.

2.1.7 Mitigation

For manufactured home loans, lender capitalization requirements would serve to mitigate the increased risk of 100 percent insurance. Though a large percentage of Title I manufactured home loans are originated and serviced by large lending institutions or manufactured home conglomerates, they are not the lenders generating the loans that GSEs have the opportunity to purchase. One GSE representative indicated that his institution would strongly consider purchasing Title I loans if they were originated by an FDIC-insured bank.

Additionally, a transition plan would be required to properly support existing operations as Title I changes are implemented to support 100 percent insurance. All actions listed with this recommendation should be applied prior to FHA conducting any operational transition activities.

2.2 Underwriting Guidelines

Even though Title I is a participant-administered program, which means FHA has delegated responsibility for program operations to lenders who are responsible for establishing loan terms and interest rates, servicing loans, and monitoring the contractors, appraisers, and related parties that participate in loan transactions, respondents to this process improvement study noted that clear, explicit underwriting guidelines from FHA are critical to increasing the use and value of the Title I Program. Many of the comments from industry indicated that FHA underwriting requirements were open to too much interpretation. As coverage is conditional, lenders could not be sure that their claim would be paid until submitted, and would rather have precise requirements that would ensure their coverage. One GSE representative mentioned that "HUD has very limited credit criteria, 'Prudent underwriting' just does not help lenders," referring to the interpretive nature of HUD guidelines to lenders.

Lender confusion of Title I is partially a result of the bundling of two very distinct programs. The nature of the Title I loan product is somewhat similar, in that property improvement loans

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and manufactured housing loans do not typically have land as equity, and therefore can be administered under a conditional loan insurance program. However, findings indicate that those lenders that originate property improvement loans would not typically be financing manufactured homes as well. As the markets are different, so are the industries that serve them.

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2.2.1 Description

Findings suggest that updating and clarifying the underwriting requirements is necessary to improve the viability of the Title I Program. This improvement can be realized through various initiatives: comparing Title I underwriting guidelines to Title II, developing an automated scoring model for Title I loans, developing training for lenders and FHA personnel on program and eligibility requirements, and implementing changes to program documentation as changes occur (web based on-line handbooks). These initiatives will enable FHA to modernize the Title I underwriting guidelines, clarify and communicate program requirements to FHA staff and industry participants, and further simplify the program. If the 100 percent loss reimbursement insurance structure is adopted as outlined in Section 2.1.2, updating and clarifying underwriting guidelines will be key to successfully implementing a change to the insurance structure of the Title I Program and mitigating the risk associated with the implementation.

Compare Title I Underwriting Guidelines to Title II. One of the most important resources of best practices should be within FHA itself. The Title II Program is one of the most responsive, market driven, needs driven program in the mortgage banking industry. In order for Title I to improve its viability, it is important for each aspect of the program to be analyzed for improvement and action. The key area that needs this analysis is Title I's underwriting guidelines. FHA should consider reviewing Title I underwriting guidelines in respect to Title II to coordinate program administration and maintain underwriting policy consistency.

Develop Automated Scoring Model. A Title I mortgage scoring model should be developed to improve credit quality and update the underwriting criteria for the program. As is quoted from a previous KPMG Title I Study: "A statistically based and empirically derived Title I mortgage scoring model would allow the Department to strengthen its underwriting criteria based solely on its experience with Title I loans. A modeling effort could identify the key areas of risk statistically; and a tailored scorecard could be developed accordingly. This approach is scientific and consistent with the Department's approach to automated underwriting for FHA single family loans. In addition, this approach relieves the Department of the arbitrary decision on setting minimum borrower credit score thresholds."

Develop Training for FHA and Industry Partners. Since the Title I Program has stood as a separate program from Title II, it has not realized the infrastructure support and maintenance as other programs. There is no consistent Title I Program training for FHA staff and no training for participating or prospective lenders. Since loan volume has diminished over the last 10 years, monitoring has decreased as well as staff to administer the program. Few FHA employees are knowledgeable on the many complexities of the program and the risk of losing these employees to retirement is high. A comprehensive training program needs to be developed to train FHA and lenders on the program history, current direction, and underwriting guidelines.

Update Handbooks. Like all FHA Single Family loan programs, constant update of policy with changing borrower needs and market conditions is key if the programs are to continue to serve its intended purpose. To effectively communicate Title I (property improvement and manufactured housing) requirements and procedures to their respective audiences, separate and updated

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handbooks should be developed to provide consistent documentation and clear guidelines for lenders. The industry has evolved dramatically since the last Title I handbooks, HUD Handbook 1060.2, *Title I Property Improvement and Manufactured Home Loan Regulations*, and HUD Handbook 4700.1, *Title I Property Improvement Loan Operating Handbook*, were updated in June, 1996 and September, 1983 respectively. By updating these handbooks as policies change, clear guidelines will be communicated and the confusion and frustration that some lenders deal with while using the program will be minimized.

2.2.2 Timeline

The estimated timeline for updating the Title I underwriting guidelines is extensive. This timeframe estimate is one year. A high-level justification and procedures list to update the guidelines are included in the actions section below. However, significant planning would need to take place to identify a complete list of changes necessary to implement this option.

The Clarify Underwriting Guidelines Project Schedule is depicted in Figure 2.2 below. The schedule shows the major actions necessary to complete this project and the estimated length of time for each action. Some actions identified for this consideration can be completed in parallel depending upon resource and time constraints. To fully understand how this consideration will fit within the context of the other considerations identified in this report, refer to the BPI Project Plan in Appendix M.

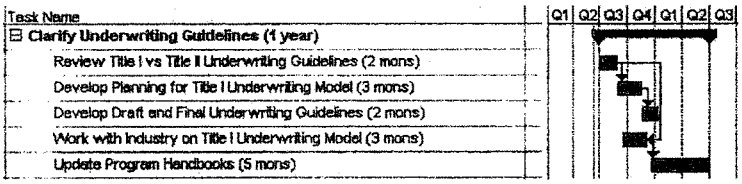

Figure 2 Clarify Underwriting Guidelines Project Schedule

2.2.3 Actions

1. Compare Title I underwriting guidelines to the Title II Program. **(2 months)**
   - Compare and contrast underwriting guidelines (accept and adopt appropriate standards from Title II based on risk analysis)
   - Develop DE specific underwriting changes (as appropriate)
   - Review guidelines for Title II Scorecard and review Title I applicability
2. Develop Planning for Title I underwriting model. **(3 months)**
   - Develop Team to review underwriting model
   - Obtain Industry involvement for model

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3. Develop Draft and Final Underwriting Guidelines (with approvals). **(2 months)**
4. Work with Industry on Title I Underwriting Model **(3 months)**
   - o Solicit input from industry on test for model
   - o Develop and run model tests
   - o Review and analyze feedback
5. Update Program Handbooks. **(5 months)**
   - o Finalize updated guidelines
   - o Produce updated handbooks
   - o Implement Web Update

2.2.4 Benefits

- Reduce Risk to FHA

  Clarity and accessibility of updated and explicit underwriting criteria is required to effectively implement 100 percent loss reimbursement for Title I. Additionally, the ability to capture and analyze loan data up-front enables FHA to ensure that loans have met underwriting guidelines at the point of origination, as well as providing real-time program performance data.

  By incorporating automated risk models to improve credit quality and the ease of analysis of market conditions, FHA can utilize modern technological innovations used throughout the industry to more accurately assess borrower risk and improve loan quality.

- Simplify the Program

  Simplify the program by leveraging existing assets within Title II: benchmarking credit quality analysis on the Title II Program and reusing several tools already in place to facilitate this analysis.

  Enable lenders and other program participants to easily understand program policies and credit criteria, which will, with proper oversight, encourage better loan quality and performance.

2.2.5 Risks/Possible Controversies

- Modifying the underwriting criteria for Title I will likely reduce the number of eligible borrowers. Careful consideration must be taken when revising the underwriting criteria for impact to the borrower and the resulting loan quality.

- Developing extensive guidelines might limit lender participation. If lenders are no longer able to interpret credit policy, additional program oversight might be necessary to ensure compliance with new policies and procedures.

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2.2.6 Mitigation

Explicit underwriting is necessary to simplify the program and provide 100 percent loss reimbursement which should encourage lenders to use the program. The restrictive nature of more prohibitive underwriting is necessary at this stage of Title I's operational lifecycle to rebuild the program to a viable level.

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3 AUTOMATE PAPER INTENSIVE PROCESSES

If the Department wishes the Title I Program to become an important provider of property improvement and manufactured housing financing opportunities for low, moderate and middle income families not adequately served by the private sector, it should consider innovative approaches to improve customer service, to reduce overall program risk, and to implement key eGovernment initiatives. Key automation benefits noted in this BPI Plan to achieve these goals come from several technological innovations developed for the Title II Program that would expand FHA's capabilities in managing risk and automating paper-intensive processes.

The key reason to automate Title I processes in line with Title II processes is to simplify the program and improve participation, administration, and program maintenance. It also enables FHA to leverage the infrastructure and process improvements currently being implemented in the Title II Program. These innovations include simplification of administrative procedures, automation of risk management components, and improvement of program oversight and quality control. Listed below are high level areas of improvement from Title II as applied to Title I.

3.1 Description

As was mentioned above, the key business and system improvements to be leveraged from Title II are in simplifying administrative procedures, automating risk management, and improving program oversight and quality control. Currently these areas within the Title I Program are either non-existent or exist as reactive actions to fraudulent claims or General Accounting Office (GAO)/Inspector General (IG) findings. There is no comprehensive plan in place for Title I that significantly modernizes its business processes and improves key program concerns. The comprehensive plan outlined below significantly improves current processing and systems use as well as aligns them with Title II to allow for improved coordinated program oversight and quality control.

Simplify Administration. Administrative procedures can be simplified by standardizing the Title I forms with industry standards (loan manifest, claims, etc.), tracking Title I underwriters in FHA systems, updating active Title I lenders on HUD's website and updating FHA Connection (FHAC) so lenders may submit loan documents (data) electronically. This will enable automated review of the data elements for consistency and validity and automatically place them in the Title I origination system. Also, the integration of Title I systems (F71/72) into Title II systems (Computerized Homes Underwriting Management System [CHUMS]/A43C) needs to be reviewed and analyzed for cost savings in respect to maintenance costs and ease of program oversight and loan performance monitoring.

Automate Risk Management. Automating risk management is key to understanding and managing FHA's risk as well as modifying program guidelines to effectively adjust to market factors. Key risk management initiatives cited earlier include developing automated scoring models and underwriting criteria to enable FHA to realize this improvement. An additional risk management opportunity to leverage from Title II is the portfolio scoring concept. This includes

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monitoring the performance of FHA's Title I portfolio by reassessing its risk on a regular basis. The two components necessary for this monitoring include data on performance status (current/delinquent) and the borrower's scorecard emulator score (if one is developed for Title I).

Improve Program Oversight and Quality Control. Currently in the Title I Program, there is little data for FHA to review prior to claim submittal. This lack of data limits the ability to implement effective program oversight and quality control. Several considerations for improvement in program oversight and quality control consists of collecting additional data elements at loan origination and claim (improvement cost, borrower social security number, debt ratios, borrower address, income, why claim was approved after denial, etc.), implementing a quality control database (loan participant details and track record with other Title I loans), and developing targeted reports/decision support system to identify and track trends throughout the loan lifecycle (from application through loan termination). In addition, FHA could use internal databases to review borrower or lender history on these types of loans and verify borrower data with agencies such as the Social Security Administration (SSA) and the Internal Revenue Service (IRS).

3.2 Timeline

The estimated timeline for aligning the Title I business processes and systems with Title II is one year. A high-level justification and procedures list to accomplish this consideration are included in the actions section below. However, significant planning would need to take place to identify a complete list of changes necessary to implement this option.

The Align Title I with Title II Processes Project Schedule is depicted in Figure 3.1 below. The schedule shows the major actions necessary to complete this project and the estimated length of time for each action. To fully understand how this consideration will fit within the context of the other considerations identified in this report, refer to the BPI Project Plan in Appendix M.

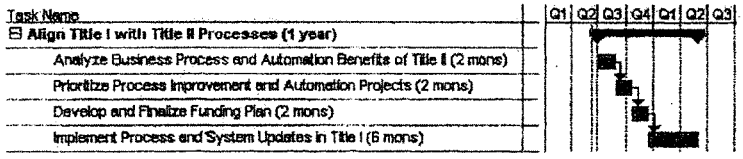

Figure 3 Align Title I with Title II Processes Project Schedule

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3.3 Actions

1. Decide on which business process and automation innovations to use from Title II. **(2 months)**
2. Prioritize process improvements and automation projects to implement. **(2 months)**
3. Based on Title II innovations needed, decide on how to obtain funding to incorporate Title I requirements. **(2 months)**
4. Develop plan to incorporate Title I requirements and implement plan. **(6 months)**

   This implementation should be conducted in a phased approach and the actual time for the system modifications are not included in this estimate.

3.4 Benefits

- Simplification of the program will enable more effective administration.

  The Title I Program is similar enough to Title II, whereas the resources used in Title II could be leveraged to support Title I. The recommendations presented in this study, which are designed to make Title I viable, reflect many of the effective practices used in Title II, and therefore, many of the systems and processes could be streamlined and modified to support both programs. Traditional cost efficiencies and economies of scale may then be realized as a result of simplifying and standardizing the program structure.

- Streamline processing and administrative procedures and leverage existing Title II innovations and assets.

  By eliminating the manual paper processes and using FHAC to facilitate data collection and validation, processing will be streamlined and program oversight will be improved. Also, this effort will enable Title I to comply with eGovernment and Government Paperwork Elimination Act (GPEA) initiatives.

  - Improve FHA's ability to better predict the potential of an individual default on a loan and to avoid the prospect of a potential loss to the Department.
  - Provide credit policy managers with early feedback on the risk associated with various programs and guidelines and provide evidence to justify changes.
  - Identify loans for monitoring reviews and help to prevent fraud.

3.5 Risks/Possible Controversies

- Costs are too prohibitive to warrant implementation.
- Program volume and participation dwindles to a point where spending money to streamline program is not cost effective.

3.6 Mitigation

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In order to effectively mitigate the risks associated with implementing the automation options outlined in section three, FHA should implement the automation improvements in a phased implementation and continuously monitor the project at specific milestones to ensure the benefits are worth the expense.

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Title I Program View from Industry

Findings & Recommendations

July 1, 2005

Contents

Project Background

Borrower Profile

Overall Program Findings and Recommendations

PI Loan Findings and Recommendations

MH Loan Findings and Recommendations

Statutory, Regulatory, and Implementing Barriers

Recommended Priorities

Next Steps

Project Background

From September 2004 – May 2005 IES reviewed 2003 Title I Business Process Improvement Study recommendations, met with FHA policy and operations staff, trade associations, lenders, and dealers to discuss the Title I Program

Analyzed differences between Title I MH and PI loans and Title II MH and 203(k) Programs, Processes, and Data (September – December 2004)

Mapped Title I Processes for FHA and Lenders (April – May 2005)

Surveyed all relevant statutes, regulations, policies and procedures (May – June 2005)

Analyzed participant recommendations against existing program guidance (June 2005)

Documented and prioritized recommendations (June 2005)

Title I Borrower Profile

PI Loans

- Borrower hard to categorize
- Many live in rural areas
- Probably a recent purchaser of FHA Title II home
- Has little or no home equity
- Seeks a smaller loan
- Has a lower income
- May use unconventional financial services
- Includes owner-occupant landlords (small investors)

MH Loans

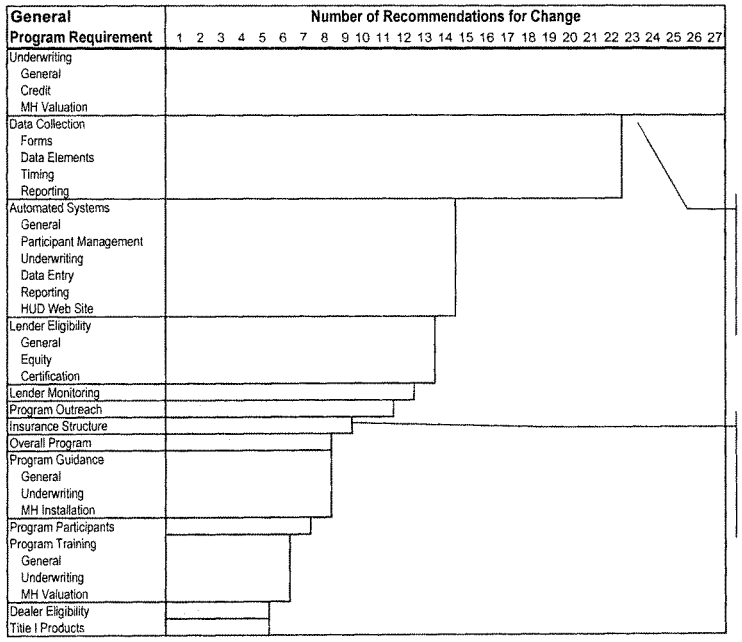
- 600+ FICO score
- "C" or "D" borrowers with average Beacon scores
- Has minimal cash flow
- Has little or no savings
- Is a typical working class family who wants to move up from renting to owning
- The pure "FHA Borrower" needing assistance to achieve homeownership

Overall Program Findings and Recommendations

- Insurance Structure
- Title I Products
- Program Outreach
- Program Guidance
- Program Training
- Program Participants
- Lender Eligibility Requirements
- Lender Monitoring

Overall Program Findings & Recommendations

Summary



Underwriting and Data Collection mentioned most frequently as needing improvement

Insurance Structure changes not seen as critical need

Overall Program Findings & Recommendations

Insurance Structure

FINDINGS:

- Frontline recommends changing from co-insurance to the Title II insurance structure
- MHI and Ginnie Mae recommend changing from lender-based to loan-based insurance
- Albany Financial Operations Center believes "up-front" structure is problematic since conditions include performance of servicing and claims
- Lenders do not view co-insurance as a problem but believe that they can not rely on claims being paid

RECOMMENDATIONS:

- Investigate simplifying the reserve account process to enable co-insurance on a per-loan basis
- Investigate ability to remove "conditions" from insurance claim payment

An important lesson learned was that co-insurance is not the problem—conditional insurance is

Overall Program Findings & Recommendations

Title I Products

FINDINGS:

- Loan limits are statutory, hopelessly outdated, and not tied to any inflation index
- PI loan amounts are not competitive with FHA HELOC or Streamline(K) products and other offerings of nontraditional lenders
- Multifamily PI loans serve unmet need in market place
- MH loan amounts limit borrowers to single-wide homes when majority of purchasers seek multi-section homes
- Loan terms should be extended to correspond with higher loan amounts
- Lenders offer MH loans at a premium of 200% or more of site-built homes, making them less attractive and decreasing their value

RECOMMENDATIONS:

- Begin process to change statutory loan product specifications immediately
- De-couple loan product specifications from statute
- Address issue of predatory interest rates on MH loans
- Clearly differentiate Title I products from other PI or MH offerings and articulate their unique benefits

Need to fast-track loan limit increases and tie them to an index to preclude need for future statutory change

Overall Program Findings & Recommendations

Program Outreach

FINDINGS:

- Title I volume is steadily decreasing
- Outdated requirements limit its competitiveness with other programs
- Industry understanding of Title I program benefits varies widely
- Lenders believe past changes to program requirements were arbitrary or focused on addressing isolated pr

Standardization and communication of unique benefits seen as key

RECOMMENDATIONS:

- Align Title I requirements with industry standards for PI and MH loans
  - Forms and data collection
  - Certifications
  - Loan amounts & terms
- Leverage HUD Web site and FOC Quarterly Newsletter
- Develop brochures for HOCs and industry on program benefits and modernization plans

Overall Program Findings & Recommendations

Program Guidance

FINDINGS:

- All participants believe complex and rigid program requirements reduce Title I's competitiveness and attractiveness to participants
- Lenders fear making mistakes through ignorance of current policies and procedures
- 100% consensus on need to update and clarify existing Handbook
- FHA and IES agree that most Title I Letters are also outdated
- All participants agree that the phrase "prudent underwriting" is not sufficient guidance

RECOMMENDATIONS:

- Update Title I Handbook as soon as possible
- Incorporate applicable TI Letters and cancel all others
- Adopt and adapt as necessary Title II underwriting guidance for MH and 203(k) loans
- Update Title I Pages on HUD Web site and leverage to provide interim updates and clarify immediate issues
- Seek support of industry trade associations to modify statutes as required

Handbook should be updated and re-issued ASAP

Overall Program Findings & Recommendations

Program Training

FINDINGS:

Consensus that new participants need training on program requirements

Some lenders suggest linking attendance at training to eligibility

Current participants require training on underwriting requirements

Current MH lenders need training on appraisal requirements

RECOMMENDATIONS:

Three types of training are immediate needs:

- New participant training
- Title I underwriting requirements
- Understanding MH appraisals

As Handbook is modified create updated training content

Pass updated training content to team working on overall training standards and development

Most lenders interviewed believe complexity of program and minimal guidance on underwriting requirements dictate need for mandatory new lender training

Overall Program Findings & Recommendations

Program Participants

FINDINGS:

- Program makes lenders responsible for dealer and broker performance
- Most recent program guidance sets up adversarial relationship between lenders and dealers
- Over time, program regulations have increasingly limited dealer role
- Lenders believe success of Title I program requires partnerships with dealers, brokers, and other participants
- Dealers and brokers seen as effective advertisers of Title I products

RECOMMENDATIONS:

- Establish dealer, broker, and investor "codes of conduct"
- Determine need for dealer equity requirements—may not be feasible for PI dealers
- Allow participation of brokers and investors
- Establish registry of approved Title I dealers (both PI and MH) based on lender recommendations
- Review requirements of lenders for monitoring brokers and dealers to identify less onerous alternatives

Most see need for further collaboration and participation, not more limits

Overall Program Findings & Recommendations

Lender Eligibility Requirements

FINDINGS:

- Majority of lenders concur with increasing equity requirements for non-regulated institutions but suggest eliminating requirements for regulated banks
- Lenders would like to tie equity requirements to performance
- Ginnie Mae requires increased capital requirements for MH lenders before re-accepting MH loans in pools

It may make the most sense to develop eligibility requirements that will encourage Ginnie Mae to pool MH loans

RECOMMENDATIONS:

- Determine if Title I lenders should have varying capital requirements depending on type of loan (PI or MH)
- Work with Ginnie Mae to identify appropriate Title I capital requirements
- Do not impose additional requirements on regulated FIs
- Consider certifying MH lenders
- Update Title I lender list on HUD's Web site

Overall Program Findings & Recommendations

Lender Monitoring

FINDINGS:

- For the past 2 years, QAD has performed no reviews on Title I loans
- Current lenders desire some type of monitoring to keep program standards high
- Most lenders recommended periodic reporting of Title I portfolio performance
- One lender suggested posting Title I lender performance on FHA's Web site

RECOMMENDATIONS:

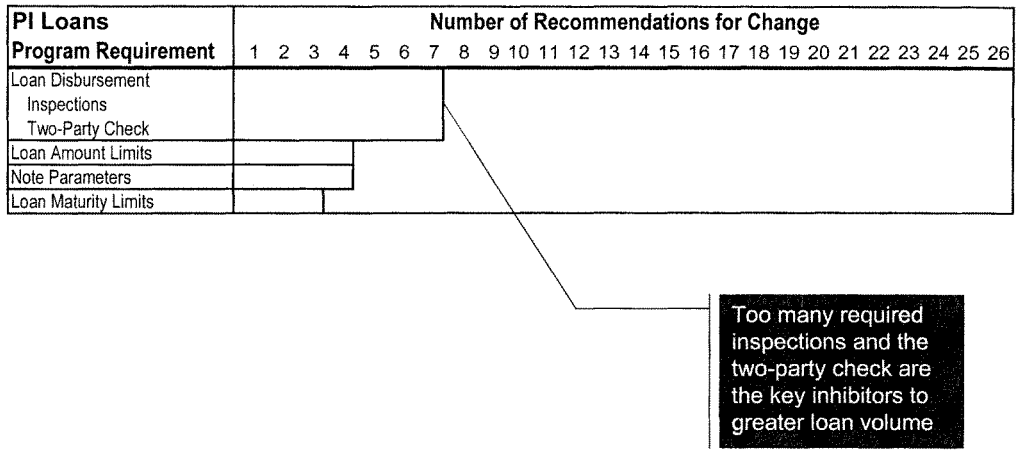
- For each modification FHA-SF makes to Title I Program requirements it should implement performance measures to assess impact of change both on risk and lender participation
- Periodic, data-based, online reporting by lenders would enhance FHA's understanding of the program while enabling it to monitor participants

Determination of what FHA wants to monitor for risk purposes requires identifying what defines success for Title I

PI Loan Findings and Recommendations

- Loan Products
- Note Parameters
- Disbursement Requirements
- Underwriting Requirements

PI Loan Findings & Recommendations
Summary



PI Loan Findings & Recommendations

Loan Products

FINDINGS:

- 100% consensus that loan limits need to be raised and tied to CPI index
- While Frontline recommended minimum loan amounts, lenders believe small loans meet needs for emergency repairs
- While Frontline recommended eliminating multifamily loans, this product meets needs of small owner-occupant landlord
- Most lenders recommended increasing loan terms to 20 – 30 years depending on loan size and whether it is secured or unsecured

RECOMMENDATIONS:

- Begin work immediately to change statutory limits and tie to CPI index and solicit aid of industry groups
- Work with industry to determine appropriate set point
- Review competitive products to identify unmet needs when setting loan terms
- Do not set a minimum loan amount
- Maintain multifamily loans

While the Title I program demands many other improvements, making them without increasing loan amount limits is meaningless

PI Loan Findings & Recommendations

Note Parameters

FINDINGS:

- Most lenders recommend allowing third lien position for qualifying borrowers to be competitive with industry
- Many lenders would like to finance additional closing costs
- Some lenders seek ability to assess late charges for simple interest loans
- Some lenders believe pre-payment penalty within first 2 years would provide program stability

RECOMMENDATIONS:

- Clarify situations for which FHA allows third lien positions
- Clarify ability of lenders to assess late charges
- Research potential impacts of pre-payment penalties

More information is needed to understand implications of any of these recommendations

PI Loan Findings & Recommendations

Disbursement Requirements

FINDINGS:

Completion certificate and site certifications add complexity, are difficult to obtain, and seem out of proportion to loan amount

Two-party check requirement does not guarantee borrower satisfaction, mitigate lender's responsibility that work was completed properly, and often unfairly delays dealer payment

RECOMMENDATIONS:

Eliminate need for completion certificate for loan amounts less than $7,500 and unsecured loans

Eliminate two-party check

Re-engineer certifications for secured loans with amounts higher than $7,500

Onerous inspection & certification requirements seen as keeping Title I loans from being competitive with other products

PI Loan Findings & Recommendations

Underwriting Requirements

FINDINGS:

- 100% consensus on need to modify credit criteria
- Verification of borrower's past 2 years of employment and payment of past-due accounts is not required by conventional lenders
- Difficult—if not impossible—to obtain credit reporting agency information about past 90-days' inquiries
- Verification of whether mortgage payments are current is difficult and often must be done twice--at loan qualification and prior to disbursement
- Not clear about acceptable "compensating factors" for granting loans with debt ratios higher than 45%

RECOMMENDATIONS:

- Balance underwriting requirements with loan amounts and whether they are secured or unsecured
- Eliminate requirement to obtain information about credit inquiries
- Align verifications of employment and credit history with industry standards for property improvement loans
- Confirm requirement for debt ratio of 45%
- Determine need for granting loans to borrowers not meeting established debt ratio and then describe compensating factors for exceptions
- To extent possible, model additional guidance on Title II 203(k) program

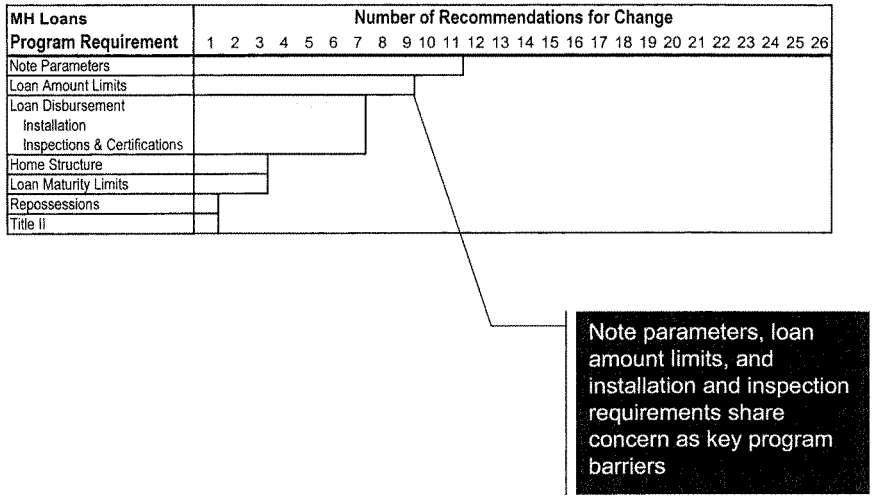
Confusion reigns on how FHA wants underwriting performed—even among experienced lenders

MH Loan Findings and Recommendations

- Home Specifications
- Home Valuation
- Loan Products
- Note Parameters
- Disbursement Requirements
- Underwriting Requirements
- Dealer Eligibility

Overall Program Findings & Recommendations

Summary



MH Loan Findings & Recommendations

Home Specifications

FINDINGS:

- Level of construction should align with Title II program
- Terminology makes "modular" homes seem better than manufactured housing and adds $15,000 to prices
- Today's MHs cannot be distinguished as such in a mixed subdivision
- Park owners add a level of monitoring to home quality

RECOMMENDATIONS:

- Evaluate need for difference between Title I and Title II MH specifications
- Update perception of MH and understand role in achieving affordable housing goals
- Understand unintended consequences of terminology on perception
- Nurture relationships between MH participants for the benefit of purchasers

MH seen by many as a critical component for meeting FHA's affordable housing goals—but perceptions must change

MH Loan Findings & Recommendations

Home Valuation

FINDINGS:

MH lenders vary widely on type of appraisal that should be used…

- Traditional (real property)
- NADA
- Marshall & Swift
- Combination

…but all agree they need training on how to evaluate MH appraisals for accuracy

Site built homes can be appropriate comps

RECOMMENDATIONS:

Work with Valuation Division to determine if new Fannie Mae MH forms can be used for Title I appraisals

Select valuation model then provide focused training on it as it relates to FHA requirements

Investigate allowing comps of site-built homes, especially in mixed subdivisions

Lenders have limited understanding of how to evaluate the quality of an MH appraisal

MH Loan Findings & Recommendations

Loan Products

FINDINGS:

100% consensus that loan limits need to be raised and tied to CPI index

Loan terms should be increased based on whether it is land-home or chattel

Chattel loans should be tied to long term leases in MH communities

As with PI loans, making other required changes without increasing loan amount limits would be meaningless

RECOMMENDATIONS:

Begin work immediately to change statutory limits and tie to CPI index and solicit aid of industry groups

Work with industry to determine appropriate set point

Review competitive products to identify unmet needs when setting loan terms

Understand relationship between chattel loan performance and space lease in MH communities

MH Loan Findings & Recommendations

Note Parameters

FINDINGS:

- Most lenders recommend allowing third lien position for qualifying borrowers to be competitive with industry
- Many lenders would like to finance additional closing costs
- Significant premium is being charged for MH
- It is common that a used MH has a lower interest rate than a new one

Interest rate differential is seen as "predatory lending" by MH manufacturers and dealers

RECOMMENDATIONS:

- Begin work immediately to change statutory limits and tie to CPI index, soliciting help from industry groups
- Work with industry to determine appropriate set point
- Carefully review whether interest rate premiums represent predatory lending—chattel loans are analogous to condo loans and should be priced accordingly
- Establish interest rate guidance and encourage decreasing rates over time

MH Loan Findings & Recommendations

Loan Disbursement Requirements

FINDINGS:

All participants find certification requirements difficult to meet

Sanitation engineer certification is a major inhibitor to resales of existing homes

Most county officials refuse to sign zoning or sanitation certificates

RECOMMENDATIONS:

Accept dealer's permit in lieu of requiring all systems to be operational prior to loan disbursement

Accept pre-construction permits for sanitation and zoning

Allow borrowers to attest to lack of local zoning restrictions

Accept certificate of completion or occupancy and eliminate 2-party checks

Here too, inspections and certifications are major competitive barriers

MH Loan Findings & Recommendations

Underwriting Requirements

FINDINGS:

- 100% consensus on need to modify credit criteria
- Some lenders recommend PMI and escrowing of taxes and insurance
- Dealer recommends requiring a "true" 10% down payment as a risk mitigation measure
- Allow MH lenders to finance origination fees

RECOMMENDATIONS:

- Align underwriting requirements with Title II MH program
- Look into need for PMI and escrow
- Evaluate impact of increasing down payment requirement

Any changes to MH underwriting requirements should be geared toward increasing confidence of industry in MH product

MH Loan Findings & Recommendations

Dealer Eligibility

FINDINGS:

Most participants believe lenders should better monitor dealers

Some believe dealers should have net worth requirements

Others believe dealers should have been operating the same business for at least 4 years

Lenders are already supposed to maintain these lists; compiling one at an FHA level should not be too difficult

RECOMMENDATIONS:

Maintain a list of certified MH dealers who meet the following professional standards:

- Deliver and erect home according to manufacturer's warranty in timely & efficient manner
- Execute warranty services
- Recondition repossessed homes
- Assist banks with returning repossessed homes to housing market

Impact of Statutes, Regulation, and Policy on Recommendations

	Statute	Regulation	Policy Letter	Handbook
Program Recommendations				
Insurance Structure				
Program Participants				
Lender Eligibility Requirements				
Lender Monitoring				
Data Collection (by FHA)				
Automation				
Dealer Eligibility Requirements				
Title I Products				
Recordkeeping (by Lender)				
Program Outreach				
Program Guidance				
Program Training				
PI Loan Recommendations				
Loan Products				
Note Parameters				
Disbursement Requirements				
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Underwriting Requirements				
Home Specifications				
Home Valuation				
Note Parameters				
Dealer Eligibility				
Disbursement Requirements				

Handbook does not address any issues not covered in other guidance (i.e., no examples or tables)

Regulations impact every recommendation category except:
- MH Home Spec (Statutory)
- Program Guidance & Training

Statutory Changes required for:
- Insurance structure
- Loan amounts & terms
- Note parameters
- Participant eligibility reqts

Specific Statutory Requirements
(12 USC 1703)

Insurance Structure: 90% co-insurance

Lender Eligibility:

- Lender must be government-regulated
- Lender must meet other qualifications established by the Secretary

Loan Amounts and Terms-PI:

- Existing SF structure: $25,000 for 20 years & 32 days
- Existing MH: $17,500 for 15 years & 32 days
- Multifamily unit: $60,000 or $12,000/unit for 20 years & 32 days
- Historic preservation: $15,000/unit for 15 years & 32 days

MH Specification: Built in accordance with National MH Construction & Safety Standards Act of 1974

Loan Amounts and Terms-Manufactured Housing

- Chattel loan for new or existing home: $48,600 for 20 years & 32 days for single wide and 23 years & 32 days for 2 or more modules
- Land-home loan for new or existing home: $64,800 for 20 years & 32 days for single wide and 25 years & 32 days for 2 or more modules
- Lot only: $16,200 for 20 years and 32 days

Note Requirements-MH: Chattel or Land-Home loan to be secured by first lien on MH or MH and lot plus all appurtenances

Recommendations Governed only by Policy

Underwriting Requirements

- Determine reasonableness of the cost for materials and labor
- Verify borrower's SSN

Dealer Eligibility: Specifies who must prepare Dealer's financial statements

Have greater flexibility with PI loans…MH loans are governed by detailed regulations

Conditions for Loan Disbursement-PI

- Inspection reports required on all PI loans:
  - Greater than or equal to $7,500
  - Less than $7,500 if borrower does not submit completion cert
- Requires lender to telephone interview borrower to ensure work was done satisfactorily and both borrower and dealer have signed completion cert
- Two-party check requirement

Recommended Implementation Strategy

Immediate:

- Begin process to achieve statutory changes for loan limits and terms—partner with industry
- Begin process to achieve required regulatory changes (much more extensive)
- Update information on Title I Web pages and post information about planned change

Important to continue reaching out to Title I lenders to retain and gain participant confidence that FHA is listening

Recommended Implementation Strategy

Short-Term:

- Complete update to Handbook and enter it into clearance
- Update and create additional participant training
- Identify additional data collection needs for managing program and submit FHAC modification request
- Decide which regulatory changes to pursue and continue change process (see next page)

None of these activities depends on statutory or regulatory changes in the near term

Recommended Implementation Strategy—Regulatory Changes

PI Loans

- Increase loan limits & terms
- Decide whether to allow third lien positions for worthy exceptions
- Align required certifications with industry
- Align underwriting requirements with industry and Title II 203(k) loans

Bottom Line: Understand and foster Title I's unique benefits, but standardize the processes that allow borrowers to obtain those benefits

MH Loans

- Increase loan limits & terms
- Align certifications with industry and Title II MH requirements
- Align underwriting guidance with industry and Title II MH requirements
- Modify MH dealer eligibility requirements to add detail and include registry
- Review foreclosure procedures to determine if lenders can be encouraged to return repossessed MHs to production

Next Steps

- Develop more detailed implementation plan
- Initiate statutory change process
- Use Web site to reach out to Title I lenders with planned changes and to solicit feedback
- Finalize Handbook and move it into the clearance process as soon as possible
- Identify data needs and develop data collection strategy