DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

FEDERAL HOUSING ADMINISTRATION

MORTGAGE AND LOAN INSURANCE PROGRAMS

SUMMARY OF THE BUDGET ESTIMATES

Mortgage Insurance Commitment Limitations. The Budget requests an overall mortgage insurance commitment limitation of $210 billion on new fiscal year 2004 FHA loan commitments. The proposed total includes $185 billion under the Mutual Mortgage and Cooperative Management Housing Insurance (MMI/CMHI) Fund, which will exclusively support insurance of home mortgages; and $25 billion under the General and Special Risk Insurance (GI/SRI) Fund which supports home, multifamily rental, and an assortment of special purpose (hospitals, nursing homes, etc.) mortgage insurance.

Direct Loan Limitations. The Budget requests a direct loan limitation of $50 million under the MMI/CMHI account. A direct loan limitation of $50 million is also requested for the GI/SRI account.

Appropriations for Administrative Expense. The Budget requests a total of $767 million for administrative and administrative contract expenses in the FHA program accounts. Of this total, $564 million will be transferred to Salaries and Expenses (S&E), HUD; $24 million will be transferred to the appropriation for the Office of Inspector General (OIG); and $179 million for administrative contract expenses. Of the total $588 million to be made available by transfer to the Department's S&E and OIG accounts, $359 million would be funded in the MMI/CMHI account and $229 million would be in the GI/SRI account.

Appropriation for Mortgage Insurance Credit Subsidies. The Budget requests an appropriation of $15 million to support the credit subsidies associated with loan guarantees committed under the FHA's GI/SRI account. The credit subsidy is based on the net cost to the Government, exclusive of administrative expenses, of a direct loan or loan guarantee over its full term, discounted to present value at the Treasury's borrowing cost. In cases where premium and fee income is projected to be more than sufficient to support full costs (i.e., there is no net Federal cost), negative credit subsidy is generated as revenue to offset other spending or reduce the deficit.

PROGRAM DESCRIPTION

Through mortgage insurance, FHA helps lenders reduce their exposure to risk of default. This assistance allows lenders to make money available to more borrowers for home and home improvement loans, and apartment, hospital, and nursing home loans. FHA provides a vital link to financing for America's housing needs.

Mortgage insurance has made financing available in neighborhoods and geographic areas facing economic uncertainty, and to individuals and families not adequately served by the conventional mortgage market. FHA has been a product innovator, and has seen the private sector follow with similar products and terms once they learn from FHA's experience. FHA spreads and manages risk through geographically dispersed loan insurance activity and a portfolio that is diverse in borrowers and products.

Supporting FHA Administrative Costs

Annual Appropriations Acts include amounts under the MMI/CMHI and GI/SRI program accounts to be transferred to the Department's S&E account and to the OIG to support the general overhead costs associated with the administration of the various insurance funds. In addition to these amounts, the program accounts also include appropriations to pay for certain programmatic contract expenses relating to the conduct of FHA's endorsement, accounting and servicing, portfolio analysis, and other activities directly related to operations of the funds. For fiscal year 2004, the Department is proposing a total appropriation for the contract expenses of $179 million, of which $85 million is in the MMI/CMHI account and $94 million is in the GI/SRI account.

Costs associated with acquisition, management and disposition of specific assets, Headquarters-directed as well as field originated, are capitalized into the costs of those properties and notes, and affect the profit or loss realized on the disposition of the assets. These costs are not included in the FHA contract totals in the program accounts, but rather are reflected in the net cash flows reported in the FHA liquidating and financing accounts.

MUTUAL MORTGAGE AND COOPERATIVE MANAGEMENT HOUSING INSURANCE ACCOUNT

PROGRAM HIGHLIGHTS

	ACTUAL 2002	ESTIMATE 2003	ESTIMATE 2004	INCREASE + DECREASE - 2004 vs 2003
		(Dollars in Millions)		
APPROPRIATION REQUEST				
Insurance Commitment Limitation	$165,000 a/	$165,000	$185,000	$20,000
Use	-157,031	-163,008	-177,500	-14,492
Subtotal	7,969	1,992	7,500	5,508
Direct Loan Limitation	250	50	50	...
Administrative Transfers (S&E & OIG)	337	348	359	11
Non-overhead admin. costs	176 b/	86 c/	85 d/	-1
Discretionary outlays (Net)				
Program Account Discretionary Outlays	557	479	444	-35
Mandatory Outlays (Net):				
Mandatory Outlays (Net), Program account	1,017	2,390	...	-2,390
Mandatory offsetting collections, Capital Reserve account	-2,717	-2,709	-1,846	863
Mandatory Outlays (Net), Liquidating account	-907	141	71	-70
Subtotal	-2,607	-178	-1,775	-1,597
Mortgage Insurance Commitments: (Units)				
Homes Current	1,299,868	1,419,769	1,474,051	54,282
Insurance Written (units):				
Homes Current	1,221,340	1,163,480	1,156,919	-6,561
Insurance Written (dollars):				
Homes Current	136,382	133,582	139,289	5,707
Insurance in-force (dollars):				
Homes	467,549	520,406	588,228	67,822
Payment of insurance claims	5,616	3,662	3,824	162
Negative Subsidy (Discretionary)	-2,880	-3,226	-3,378	-152

a/ Includes supplemental of $5 billion for commitment authority.
b/ Includes $16 million in appropriation conditional on commitment level exceeding $65.5 billion by April 1, 2002.
c/ Includes no less than $21.4 million to be transferred to the Working Capital Fund for development and maintenance of information technology systems.
d/ Includes no less than $20.7 million to be transferred to the Working Capital Fund for development and maintenance of information technology systems.

SUMMARY OF BUDGET ESTIMATES

Credit Limitation. The Budget requests $185 billion as limitation on new insurance commitments for fiscal year 2004. This limitation includes standby commitments to avoid the need for supplemental appropriations if the demand for insurance should exceed the projected level; but standby commitments are not reflected in the estimates for net outlays and receipts. A limitation of $50 million is requested for direct loans.

An estimated $134 billion of insurance will be written in 2003, and $132 billion in 2004,excluding the additional $7.5 billion in endorsements expected to be generated by the new MMI product that offers loans for borrowers that are ineligible for standard financing. This program will be geared towards borrowers who, due to poor credit, would be served at a higher cost by the conventional market or not at all.

Appropriation Request. An appropriation of $444 million is requested for administrative expenses for fiscal year 2004. Of this sum, $355 million is to be transferred to the Departmental Salaries and Expenses account, $4 million to the Office of Inspector General accounts, and $85 million for contract expenses, including a transfer of not less than $20.7 million to the Working Capital Fund for system development.

The MMI Fund is expected to generate $3.2 billion of negative subsidy on insurance written in fiscal year 2003 at a subsidy rate of –2.53 percent. In 2004, nearly $3.3 billion in negative subsidy is expected to result from the current types of business at a subsidy rate of –2.47 percent, and an additional $103 million at a subsidy rate of -1.37 percent for the new sub-prime loan program.

EXPLANATION OF INCREASES AND DECREASES

Mortgage Origination. FHA anticipates that it will endorse less insurance in the current base business in MMI single family mortgages in fiscal year 2004 ($132 billion and 1.095 million homes) than in fiscal year 2003 ($134 billion and 1.163 million homes), due to a projected general slowdown in mortgage lending activity. The new MMI mortgage loan program is expected to generate an additional $7.5 billion in endorsements for 62 thousand additional homes, over the base business. An additional $20 billion in commitment authority is requested in 2004 above the $165 billion in 2003.

Mortgage Assignment, Property Acquisitions, and Property Sales. Starting with a demonstration project in 2002, FHA is acquiring notes under Section 601 of the 1999 Appropriations Act, with accelerated claims processing. These notes are transferred to joint venture partners, with the partner providing an upfront payment to FHA at the time of the transfer. Under this arrangement, FHA would retain an equity interest until the partner disposes of the notes, and would receive additional payments for that interest. The first sale occurred in October 2002.

The claims for MMI are estimated for each cohort by year of endorsement using the claim rates from the 2002 Actuarial Review, as adjusted for program changes. These changes include high use of the loss mitigation techniques in 2003 and 2004, and use of note claims under Section 601 of the 1999 Appropriations Act. Sales of properties are projected based on the estimated inventory at the end of fiscal year 2003 and estimated acquisitions in fiscal year 2004.

Financial Activity. FHA established, in fiscal year 2002, a new “MMI Capital Reserve” account, to hold the MMI reserves required by statute. In 2002, balances of MMI reserves were transferred from the MMI Liquidating account to the new Capital Reserve account. Henceforth, negative subsidy and downward reestimates are booked to this account from the Financing account. Upward reestimates are booked from the new account to the Financing account, via the Program account. Net outlays in 2004 are estimated at -$3.3 billion for all accounts, including the off-budget financing accounts.

The fiscal year 2004 Budget shows negative subsidy disbursed to the Capital Reserve Account through the financial planning period, where it is invested in special Treasury securities and earns interest.

PROGRAM DESCRIPTION AND ACTIVITY

MMI/CMHI Funds. The Mutual Mortgage Insurance Fund consists of the basic single family home mortgage program (Section 203(b)), the largest of all the FHA programs.

The Section 203(b) program, enacted in the National Housing Act of 1934, provides mortgage insurance for one- to four-family residences. This program has contributed to expanding the opportunities for homeownership in the United States and will continue to meet the needs of first-time homebuyers, working families, and minority families, as well as underserved communities, especially central city and rural areas. Under the 203(b) program, any person able to meet the cash investment, mortgage payments and credit requirements may obtain an FHA-insured loan from a private lending institution to purchase a home. Since its inception through September 30, 2002, the MMI Fund has insured approximately $1.3 trillion in mortgages for about 20 million families.

The Cooperative Management Housing Insurance Fund 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. The insurance program can be used for new construction, rehabilitation, acquisition, improvement or repair of a project and resale of individual memberships in the cooperative. This program was enacted in 1950 and only minor program activity has occurred in recent years.

PROPOSED CHANGES FOR 2004 FROM THE 2003 BUDGET ASSUMPTIONS

Single Family assumes for MMI:

- Legislation for the new sub-prime loan product is being proposed as part of the Department's administrative provisions. This line of insurance is targeted to persons who, due to poor credit, would either be served by the conventional market at a higher cost or not at all. It is anticipated that some of these borrowers that are able to meet more restrictive loan to value requirements and slightly higher mortgage insurance premiums will be offered FHA loan guarantees under this new initiative, allowing them to maintain their home or to purchase a new home at a lower cost than is now possible.

- The MMI Capital Reserve account has had transferred to it in fiscal year 2002 the MMI Liquidating account balance as of October 1, 2001, including Treasury securities previously held in the 86X4070 Liquidating account, and the downward reestimates. For 2003, negative subsidy for 2003 and future years, downward re-estimates, and the interest earned on Treasury securities will be booked to the Capital Reserve account. End-of-year balances also will be swept from the 86X4070 Liquidating account into the Capital Reserve account. Any funds for upward reestimates (to be transferred to the Financing account via the Program account) and drawdown of authority to cover any shortfalls in the 86X4070 Liquidating account will be obligated against the Capital Reserve account.

- Claim estimates use the claim rates in the 2002 Actuarial Review, as adjusted for anticipated programmatic changes.

- Implementation of the accelerated claims processing to allow FHA to take mortgage notes, as authorized in section 601 of the 1999 Appropriations Act, began at the end of 2002.

ADMINISTRATIVE EXPENSES

FTE/OBJECT CLASS	ACTUAL 2002	ESTIMATE 2003	ESTIMATE 2004
FTE			
Headquarters	328	359	357
Field	698	730	725
Total FTE	1,026	1,089	1,082
S&E Cost (Dollars in Thousands)			
Personal Services	$86,416	$94,444	$96,372
Travel	1,509	1,286	1,337
Rent, Communications & Utilities	3	3	3
Printing	220	306	310
Other Services	1,476	1,211	1,155
Supplies	109	97	98
Furniture & Equipment	18	...	...
Total S&E Cost	$89,751	$97,347	$99,275

GENERAL AND SPECIAL RISK INSURANCE ACCOUNT

PROGRAM HIGHLIGHTS

	ACTUAL 2002	ESTIMATE 2003	ESTIMATE 2004	INCREASE + DECREASE - 2004 vs 2003
		(Dollars in Millions)		
APPROPRIATION REQUEST				
Insurance Commitment Limitation	$21,000	$24,000	$25,000	$1,000
Supplemental	2,000	...	...	...
Subtotal	23,000	24,000	25,000	1,000
Direct Loans Limitation	50	50	50	...
Budget Authority				
Administrative Expenses	216	224	229	5
Contract Expenses	150 a/	94 b/	94 c/	...
Positive Credit Subsidy	15	15	15	...
Subtotal	381	333	338	5
Program level				
Use of insurance commitment limitation	22,081	23,989	24,960	971
Administrative Expenses				
Appropriation, S&E Transfer ...	216	224	229	5
Appropriation, Contract Costs .	150 a/	94 b/	94 c/	...
Subtotal	366	318	323	5
Credit Subsidy Reservations:				
Appropriations	15	15	15	...
Insurance Commitments (dollars) :				
Multifamily	5,700	6,334	6,643	309
Hospitals	149	550	700	150
Homes	13,931	14,625	15,012	387
Title I	150	180	180	...
Nursing Homes (includes Refis)	2,151	2,300	2,425	125
Subtotal	22,081	23,989	24,960	971
Insurance Written (units):				
Multifamily	115,876	127,050	133,400	6,350
Hospitals	...	...	...	...
Homes	119,088	124,086	126,330	2,244
Title I	8,778	9,041	9,041	...
Nursing Homes (includes Refis)	32,195	42,500	44,750	2,250
Subtotal	275,937	302,677	313,521	10,844
Insurance Written (dollars):				
Multifamily	4,560	6,011	6,544	533
Hospitals	199	619	623	4
Homes	13,931	14,625	15,012	387
Title I	149	180	180	...
Nursing Homes (includes Refis)	1,761	2,209	2,394	185
Subtotal	20,600	23,644	24,753	1,109

a/ Includes $4.5 million in appropriation conditional on commitment level exceeding $8.4 billion by April 1, 2002.
b/ Includes no less than $14.2 million to be transferred to the Working Capital Fund for the development and maintenance of information technology systems.
c/ Includes no less than $16.9 million to be transferred to the Working Capital Fund for the development and maintenance of information technology systems.

SUMMARY OF BUDGET ESTIMATES

Credit Limitation. A limitation on new insurance commitments for fiscal year 2004 of $25 billion is requested. It is estimated that $9 billion in insurance will be issued for multifamily and healthcare related programs in fiscal year 2004 for 178,150 units. Another $700 million is estimated in hospital mortgage insurance. Single family and Title I commitments are projected at $15.2 billion in fiscal year 2004 for an estimated 135,371 units.

A direct loan limitation of $50 million is requested. Of this amount, $30 million is intended for bridge loan financing to facilitate the sale of multifamily projects, and $20 million is for 5-year purchase money mortgages for non-profit and governmental agencies to make HUD-acquired single family properties available for resale to purchasers at or below 115 percent of area median incomes.

Appropriations. The 2004 request includes appropriations of $15 million for positive credit subsidy necessary for commitments related to various multifamily programs and for the Title I property improvements loan program in the GI/SRI program account. Appropriations of $323 million in administrative expenses are requested for 2004, of which $209 million is transferred to the Departmental Salaries and Expenses Account, $20 million is transferred to the Office of Inspector General account, and $94 million for contract expenses, including a transfer of not less than $16.9 million to the Working Capital Fund for system development.

	ACTUAL 2002	CURRENT ESTIMATE 2003	ESTIMATE 2004	INCREASE + DECREASE - 2003 vs 2004
		(Dollars in Millions)		
APPROPRIATION REQUEST				
INSURANCE COMMITMENT				
Limitation Enacted/Requested.........	$21,000	$24,000	$25,000	+1,000
Supplemental.........................	2,000	...	...	...
Subtotal	23,000	24,000	25,000	+1,000
Direct Loans.........................	50	50	50	...
BUDGET AUTHORITY				
Discretionary:				
Administrative Expenses (S&E)........	216	224	229	+5
Non-overhead administrative expenses.	150	94	94	...
Positive Subsidy Appropriations......	15	15	15	...
Total Discretionary Approp.........	381	333	338	+5
Offsetting Receipts..................	-363	-326	-256	+70
Mandatory:				
Liquidating account (net)...........	1,343	697	797	+100
Mortgage sales......................	[-86]	[-265]	[-250]	[+15]
Program Account Upward Reestimate...	995	1,167	NA	-1,167
Receipt Account.....................	- 88	-26	- 7	+19
Receipt Account Downward Reestimate..	-1,542	-1,102	NA	+1,102

	ACTUAL 2002	CURRENT ESTIMATE 2003	ESTIMATE 2004	INCREASE+ DECREASE - 2003 vs 2004
		(Dollars in Millions)		
BUDGET OUTLAYS				
Discretionary:				
Administrative expenses (S&E).......	$ 216	$ 224	$ 229	$ +5
Non-overhead administrative expenses	113	121	94	-27
Credit Subsidy.....................	16	11	15	+4
Offsetting receipts................	-363	-326	-256	+70
Mandatory:				
Liquidating account (net)...........	546	917	577	-340
Program Account Upward Reestimate...	995	1,167	NA	-1,167
Receipt Account....................	-88	-26	-7	+19
Receipt Account Downward Reestimate.	-1,542	-1,102	NA	+1,102

EXPLANATION OF INCREASES AND DECREASES

The fiscal year 2004 request also includes estimated commitments of $25 billion in loan programs where the present value of projected revenues from new insurance exceeds the present value of estimated costs, resulting in the generation of negative credit subsidy. This negative credit subsidy of $256 million from new insurance will be a discretionary offset against the total budget authority of the Department.

PROGRAM DESCRIPTION AND ACTIVITY

GI/SRI Insurance Programs. The Department will continue to offer a range of alternative loan guarantee programs to address specialized mortgage financing needs. These products include mortgage insurance for rehabilitating, developing, and refinancing of apartment buildings, nursing home facilities, nonprofit hospitals and Title I loans. The Department's insurance programs will continue to meet the Nation’s need for decent, safe and affordable housing.

Hospital Programs. The Department will continue the Section 242 Program, which provides mortgage insurance for loans made for the construction; renovation and/or equipping of acute care hospitals. Since the program began in 1968, FHA has insured 317 hospital mortgages totaling more than $9.5 billion. The Hospital Mortgage Insurance Program also includes: Section 241 supplemental loans; Section 223(a)(7) loans for refinancing existing insured projects; and Section 223(e) loans for hospitals in older, economically declining urban areas. The Hospital Mortgage Insurance Program is administered by HUD Headquarters, with support from staff at the U.S. Department of Health and Human Services.

Multifamily Credit Subsidy Rates. The Department continuously devotes significant efforts in updating and refining credit subsidy estimates. The credit subsidy estimates were developed after extensive consultation with Office of Management and Budget (OMB) by FHA and reflect substantial additional analysis by the Department. Each year the extensive statistical base, from which projections of future loan performance is calculated, is updated for an additional year of actual data. The Department and OMB continue to examine the data, assumptions, and calculations, which are used to estimate loan program cash flows and subsidy rates in order to eliminate errors, and to seek improvements in the accuracy and reliability of the analysis.

The multifamily credit subsidy rates used in previous years reflected historic performance data for similar loans made over the past 40 years. Concerns were raised over the accuracy of these assumptions based on historical data in light of recent improvements in underwriting, program monitoring, and asset management, as well as unprecedented changes in tax law in the 1980’s adversely affecting the performance of loans in the FHA portfolio at that time.

In the fiscal year 2003 Budget, the Department and OMB agreed to change the methodology used to calculate new construction conditional claim and prepayment rates for credit subsidy rate estimates through the application of new econometric analyses applied to loan level data. For the fiscal year 2004 Budget, updated loan performance data combined with the improvement of the recovery lag calculations in the cash flow model itself yield a break-even premium at 50 basis points for the section 221(d)(4) program that serves as the primary apartment development program of FHA. This is a seven basis point reduction in the premium in effect for the current fiscal year. In addition, FHA will reduce the premium for Section 207 manufactured home parks and section 220 development loans to 50 basis points, which is an eleven basis point reduction. This is also a break-even premium rate for this risk category requiring no appropriated credit subsidy. Positive credit subsidy continues to be required for the section 221(d)(3), 223(d) and 241(a) loan programs so no reduction in the applicable 80 basis point insurance premium is proposed.

Title I Program Subsidy Rates. The fiscal year 2004 estimates for the Title I Programs reflect the loan characteristics of the property improvement and the manufactured housing program, which are incorporated into the cash flows used to calculate the subsidy rate for loan programs, in accordance with the Federal Credit Reform Act of 1990.

Title II Program Single Family Subsidy Rates. The GI/SRI single family credit subsidy estimates also reflect review of loan performance. This includes updated loan performance data and assumptions of the major GI/SRI single family programs that are currently active. Those mortgage insurance programs are 234(c) Condominium Housing and 203(k) Purchase/Rehabilitation. Premium policy changes for the 203(k) program in the 2004 Budget include cancellation of annual premium when loan to value reaches 65 percent, rather than 78 percent. On an average 203(k) loan, it is estimated that annual premium will be required for the first 17 years of a 30-year term. With this slight alteration of the premium structure, this program is expected to break even and require no positive credit subsidy appropriations. Other small programs that do not have sufficient volume to model and estimate individually are included in the Section 234(c) risk category for budgetary purposes.

The following table displays the estimated allocation of commitment authority and subsidy by program for fiscal year 2004.

GI/SRI PROGRAMS	Commitment Authority FY 2004	Subsidy Rate FY 2004	Positive Subsidy BA FY 2004
Multifamily & Healthcare			
Apartments NC/SR (includes Mixed Use)	$3,000,000,000	-0.62%	
221 (d3) NP coop owned apts.	$100,000,000	5.35%	$5,350,000
Tax Credit Projects	$850,000,000	-1.59%	
Apartments Refinance	$1,800,000,000	-2.13%	
241a Supplemental loans for Apts.	$25,000,000	8.60%	$2,150,000
223 Operating Loss Loans	$3,000,000	17.84%	$535,200
HFA Risksharing	$420,000,000	-1.67%	
GSE Risksharing	$120,000,000	-1.08%	
FHA Full Insurance for Health Care Facilities	$725,000,000	-0.22%	
Health Care Refinance	$1,700,000,000	-1.28%	
Other Rental	$325,000,000	-0.08%	
Hospitals (includes refi. & Suppl. Loan)	$700,000,000	-3.33%	
Multifamily & Healthcare Subtotal	$9,768,000,000		$8,035,200
Single Family Programs			
Title I			
Property Improvements	$105,000,000	1.86%	$1,953,000
Manufactured Housing	$75,000,000	-0.14%	
Title I Subtotal	$180,000,000		$1,953,000
Title II			
234 Condominium Housing & Other	$14,100,000,000	-1.03%	
203(k) Rehabilitation Mortgage	$912,000,000	-0.02%	
Title II Subtotal	15,012,000,000		
Single Family Subtotal	$15,192,000,000		$1,953,000
Stand-by Authority	$40,000,000		
GI/SRI TOTAL	$25,000,000,000		$9,988,200

Office of Multifamily Housing Assistance Restructuring (OMHAR). The Multifamily Assisted Housing Reform and Affordability Act of 1997 was included in the 1998 Appropriations Act. The initial legislative authority establishing OMHAR ended September 30, 2001. Prior to expiration, Public Law 107-116 extended OMHAR as an entity within the Office of Housing for an additional 3 years through fiscal year 2004 and extended the attendant mortgage restructuring authorities for another 5 years through fiscal year 2006. The restructuring process is expected to preserve over 174,000 units of affordable housing stock through long-term use agreements.

The restructurings are performed through oversight of a national network of 13 public Participating Administrative Entities (PAEs), and 8 private partners. OMHAR staff is currently located in a central District of Columbia office and three satellite field offices, located in Chicago, New York and San Francisco, which oversees the program through nationally consistent guidelines, which provide for local flexibility to the extent possible.

As of December 1, 2002, OMHAR reported completing over 1,600 restructurings, averaging 35-40 per month, and resulting in an annual reduction of Section 8 outlays of $115,096,455. The average rent reduction is $93 per unit per month. The reductions in future Section 8 outlays and expected recoveries of second mortgage payments exceed the one-time costs of restructuring for FHA claims and PAE costs. In addition to ensuring long-term financial viability and achieving Section 8 savings, physical and managerial assessments are conducted for each property to assure the long-term viability of the portfolio. Expenses are analyzed to ensure efficient operations. Immediate capital needs are addressed through repair escrows. Long-term physical needs are provided for through increased deposits to reserve for replacement accounts. Initial deposits to these accounts were increased on average from $1,343 to $2,329 per unit, and annual deposits increased on average from $297 to $439 per unit per year.

The M2M program realigns the owners' and HUD's interest by providing a return on the owner's equity through a capital recovery payment, an incentive performance fee, and 25 percent of net cash flow. The financial structure of the properties is designed to ensure efficient operations and maintenance of the properties. HUD is closely monitoring the performance of restructured properties through a portfolio management contract and through a "watch list" for at-risk properties which had rents reduced without a debt restructuring.

A significant amount of work still remains to be completed. Over 600 deals are currently in various stages of restructuring. There are another 2,600 Section 8 contracts expiring through fiscal year 2006, at least a third of which are estimated to be above market and eligible for M2M.

Mortgage Note Sales. FHA successfully executed GI/SRI Multifamily Mortgage Note Sales in fiscal year 2002 which will continue into 2005. In 2002, FHA sold 114 unsubsidized mortgage notes with an unpaid principal balance (UPB) of $502 million. These notes were valued to HUD at $177 million. The net sales proceeds amounted to $287 million. Negative subsidies realized from the sales amounted to $110 million.

FHA plans to continue selling Multifamily unsubsidized mortgage notes in fiscal year 2003 through 2005. Currently, large portions of the remaining multifamily notes are subsidized. Therefore, FHA is also planning to sell the subsidized inventory starting in fiscal year 2003. Ongoing note sale activity in the future will be driven by the amount of salable notes entering the inventory.

Multifamily Enforcement. The Department's multifamily housing enforcement strategy reflects the integrated and coordinated efforts of the Real Estate Assessment Center (REAC) within the Office of Public and Indian Housing and the Departmental Enforcement Center (DEC), an element of the Office of the General Counsel. REAC is completing a comprehensive and uniform portfolio wide assessment of the physical and financial condition of all the properties. Results are being forwarded to Housing's Multifamily Hubs for additional actions. The Multifamily Hubs are responsible for servicing the loans and overseeing subsidy contracts. In those cases where there appear to be severe performance problems, cases are referred to the DEC. The DEC evaluates each case it receives and, where the DEC decides that severe problems exist, the DEC provides an action plan to be implemented by the Hubs to address the problem(s). Qualitative improvement in the assessment and enforcement effort is being realized through the centralization and specialization of these staff. The ultimate goal, however, is improved living conditions for residents, improved neighborhoods, communities, and improved financial performance for FHA because performance standards for participants are raised.

ADMINISTRATIVE EXPENSES

FTE/OBJECT CLASS	ACTUAL 2002	ESTIMATE 2003	ESTIMATE 2004
FTE			
Headquarters	264	309	308
Field	875	848	847
Total FTE	1,139	1,157	1,155
S&E Cost (Dollars in Thousands)			
Personal Services	$94,810	$99,495	$102,001
Travel	1,330	1,107	1,157
Rent, Communications & Utilities	1	1	1
Printing	177	262	265
Other Services	907	673	640
Supplies	89	83	82
Furniture & Equipment	1	...	...
Total S&E Cost	$97,315	$101,621	$104,146