HOUSING
FHA--MUTUAL MORTGAGE INSURANCE FUND
2015 Summary Statement and Initiatives
(Dollars in Thousands)

FHA--MUTUAL MORTGAGE & COOPERATIVE MGMT. HOUSING INSURANCE FUND	Enacted/ Request	Carryover	Supplemental/ Rescission	Total Resources	Obligations	Outlays
2013 Appropriation	$207,000[a/]	$15,968	-$10,827	$212,141	$110,146	$107,307
2014 Appropriation/Request	127,000	34,185[b]	...	161,185	161,185	102,000
2015 Request	170,000[c]	...	...	170,000	169,000	117,000
Program Improvements/Offsets	+43,000	-34,185	...	+8,815	+7,815	+15,000

a/ Includes a non-expenditure transfer of $67.8 million to the HUD Working Capital Fund. The transfer amount is excluded from obligations, outlays and carryover.
b/ Carryover excludes $49 thousand, which expired at the end of fiscal year 2013.
c/ This number includes an estimated Transformation Initiative (TI) transfer that may be up to 0.5 percent or $15 million of Budget Authority, whichever is less. In addition, the 2015 Budget proposes an administrative support fee estimated to produce $30 million in offsetting collections.

1. What is this request?

The Mutual Mortgage Insurance (MMI) Fund is the largest fund covering activities of the Federal Housing Administration (FHA). Since 1934, mortgage insurance provided by FHA has made financing available to individuals and families not adequately served by the conventional private mortgage market. Through MMI, the Department offers several types of single family forward mortgage insurance products and Home Equity Conversion Mortgages (HECMs) for seniors. Activity for the Cooperative Management Housing Insurance (CMHI) Fund – which insures mortgages for multifamily cooperatives – is reported together with MMI.

The fiscal year 2015 Budget request will enable FHA to continue its mission of providing access to mortgage credit for families with low and moderate wealth, and to play an important counter-cyclical role in the continued stabilization and recovery of the nation's housing market. By facilitating the availability of vital liquidity through a variety of HUD-approved lenders, including community banks and national credit unions, FHA has made a number of achievements including:

Helping over 3.9 million families buy a home since President Obama took office. In fiscal year 2013, more than 500,000, or over 78 percent, of FHA purchase loan endorsements were first-time buyers. These are families that likely would otherwise not be served by the conventional mortgage market.

- FHA accounted for 54 percent of purchase mortgage financing for Black or African-American and Hispanic borrowers.

- The total number of first time homebuyers that FHA has supported over the past three years now totals 3.3 million.
- Through its streamline refinance option, FHA helped 500,000 families reduce their monthly housing costs by an average of $200 per month, for an annual savings of $2,400 per family.
- FHA also helped more than 450,000 families avoid foreclosure this past year through its loss mitigation home retention servicing tools.

Managing in a challenging mortgage market - FHA's share of the mortgage market dropped to a low of 3.1 percent of loan originations (by count) in 2005 and then rose to a peak of 21.1 percent in 2010. Since then, FHA's share of new mortgage originations has come down to under 16 percent. FHA's core home-purchase loan activity in 2013 had declined to a level comparable to 1997 (702,417 vs. 704,286 homebuyers, respectively), and was less than the level of FHA activity from 1998 through 2002. FHA's current market share remains above 1990s levels only because of a substantial decrease in the size of the total housing and mortgage market, rather than exceptionally high FHA activity today.

As a result of making major programmatic changes, improving risk management, and restructuring pricing, the value of the MMI Fund has improved significantly since 2012. The improved economic value of the MMI Fund has led the FHA's independent actuary to expect the fund to accumulate capital at a much faster rate than was projected in 2012, which in turn would enable the MMI Fund to reach a 2 percent capital reserve ratio by fiscal year 2015 (2016 if reserve is measured by its ratio to the unamortized balance of insurance) rather than fiscal year 2017, as was projected in the 2012 actuarial review.

FHA is making it a priority focus to assist homeowners through early delinquency intervention, loss mitigation programs, and specific joint efforts with the Department of Treasury, including: the Home Affordable Modification Program and the FHA Short Refinance program for underwater borrowers with conventional loans. Over fiscal years 2012 and 2013, FHA has a 2-year goal of having 500,000 homeowners assisted through early delinquency interventions and 200,000 assisted through loss mitigation programs, with an additional goal of having at least 80 percent of loans receiving this assistance to be current on their mortgages for at least 6 months. FHA exceeded its goals by 20 percent and 70 percent, respectively, and 938,734 homeowners were assisted in total. Through the end of FY 2013, 91.62 percent of loans that received assistance remained current for at least 6 months.

Performance Indicator	**FY12/13 Goal**	**FY12/13 Outcome**
Homeowners assisted through early delinquency intervention (<90 days in default, individual cases)	500,000	599,555
Homeowners assisted through FHA loss mitigation programs (individual cases)	200,000	339,179

Mortgage and Loan Insurance Programs – MMI/CMHI Account

The fiscal year 2015 request for MMI includes four components:

- ***Commitment authority for up to $400 billion in new loan guarantees.*** The fiscal year 2015 Budget requests $400 billion in loan guarantee limitation, which is to remain available until September 30, 2016. The requested limitation has been unchanged since 2010. This limitation includes sufficient authority for insurance of single family mortgages, mortgages under the HECM program, and the FHA Short Refinance program. Total loan volume projected for all MMI programs for fiscal year 2015 is $150.6 billion. Of that total, $134.7 billion is estimated for standard forward mortgages, $15.9 billion for HECM, and $75 million for FHA Short Refinances. The 2-year availability for this commitment authority reduces the likelihood of program disruption under a continuing resolution.
- ***Negative Subsidy Receipts.*** The $150.6 billion in loan volume projected for the entire MMI portfolio in fiscal year 2015 is expected to generate $12.2 billion in negative subsidy receipts, which are transferred to the MMI Capital Reserve account, where they are available to cover any projected cost increases for the MMI portfolio.
- ***Appropriations for Administrative Contracts.*** The Department requests an appropriation of $170 million offset by estimated collections of $30 million from a new administrative fee charged to lenders. The appropriation requested reflects an increase of $43 million from the fiscal year 2014 appropriation. The additional resources will fund enhancements to administrative contract support, with a focus on increasing the number of loans reviewed annually for quality assurance. By increasing capacity to review recently endorsed loans, FHA will ensure lender compliance with FHA endorsement policies and reduce losses to the FHA insurance fund.
- ***Commitment authority for up to $20 million in direct loans to facilitate single family property disposition.*** The loan authority requested would provide short-term purchase money mortgages for non-profit and governmental agencies. It would enable these entities to make HUD-acquired single family properties available for resale to purchasers with household incomes at or below 115 percent of an area's median. Though the program has been infrequently utilized in recent years, it remains a valuable tool for HUD in managing its property portfolio. The loan program is designed to operate at break-even for the government, so no credit subsidy is involved.

	2013 Enacted	2014 Enacted	2015 Request	Increase/ (Decrease)
Loan Guarantee Commitment Limitation	$400,000,000,000	$400,000,000,000	$400,000,000,000	...
Direct Loan Limitation	$50,000,000	$20,000,000	$20,000,000	...

Salaries and Expenses (S&E) and Full-Time Equivalents (FTE) Request

The primary workload for FHA programs in the MMI Fund is carried out by HUD's Office of Housing, mainly the Office of Single Family Housing. Critical functions are also supported by financial management, procurement, Information Technology, and other administrative organizations. A total of 1,074.6 FTE are requested for the Single Family Housing programs. Total S&E funding is $137.088 million, or an increase of $6.086 million from the fiscal year 2014 estimate.

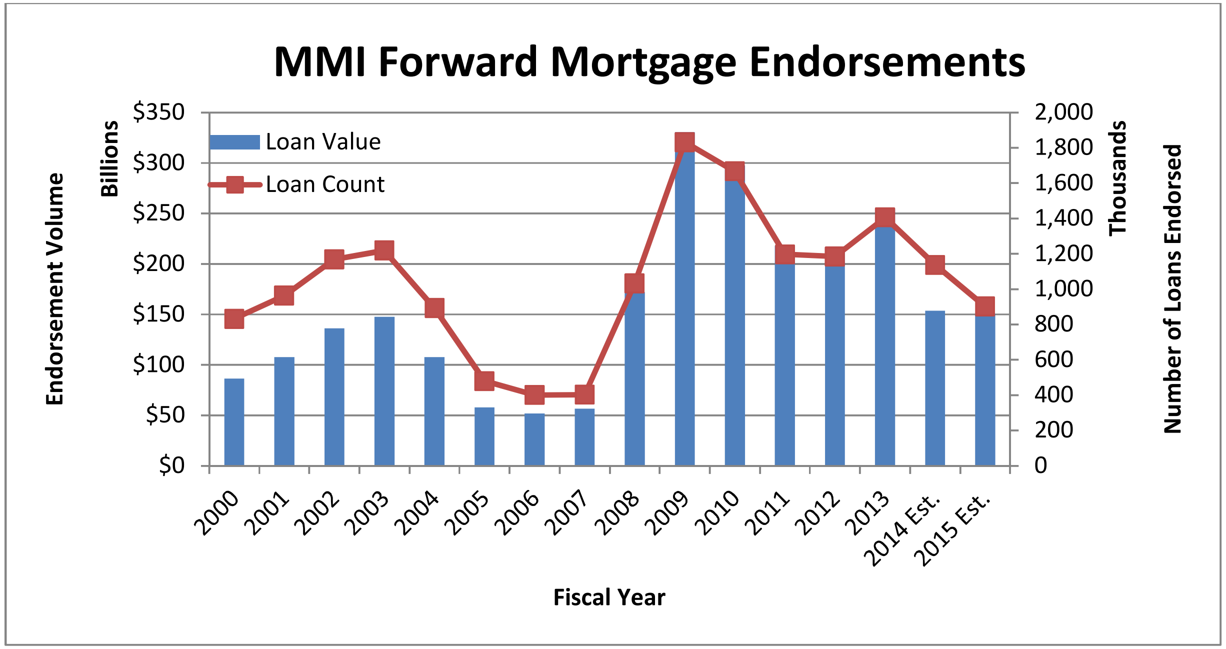
2. What is this program?

FHA has insured over 41 million home mortgages since 1934. In exchange for adherence to strict underwriting and application requirements established by HUD and the payment of insurance premiums, HUD-approved lenders are able to file claims with FHA when a borrower defaults. Mortgage insurance premiums and specific terms for claim payments vary by program. FHA insurance has played a key role in mitigating the effect of economic downturns on the real estate sector, as FHA plays a counter-cyclical role, providing access to mortgage credit during periods of constriction in credit markets. The FHA includes a strong, mandatory loss mitigation program. Through the recession, FHA has provided key support for the national mortgage market and is mitigating the foreclosure crisis and the overall economic downturn.

As of the 4th quarter of 2013, the MMI insurance portfolio included 7.6 million loans with an unpaid principal balance exceeding $1.1 trillion. FHA mortgage insurance enhances a borrower's credit and provides banks with better access to capital markets, most notably through Ginnie Mae securities. FHA has long been a valuable resource for enabling the purchase of a first home, especially among minority and low-income families. FHA loans are highly attractive to borrowers who are credit-worthy but have difficulty assembling a large down payment or securing conventional financing.

For budgetary purposes, the programs of the MMI Fund are broken into three risk categories, each of which is discussed below:

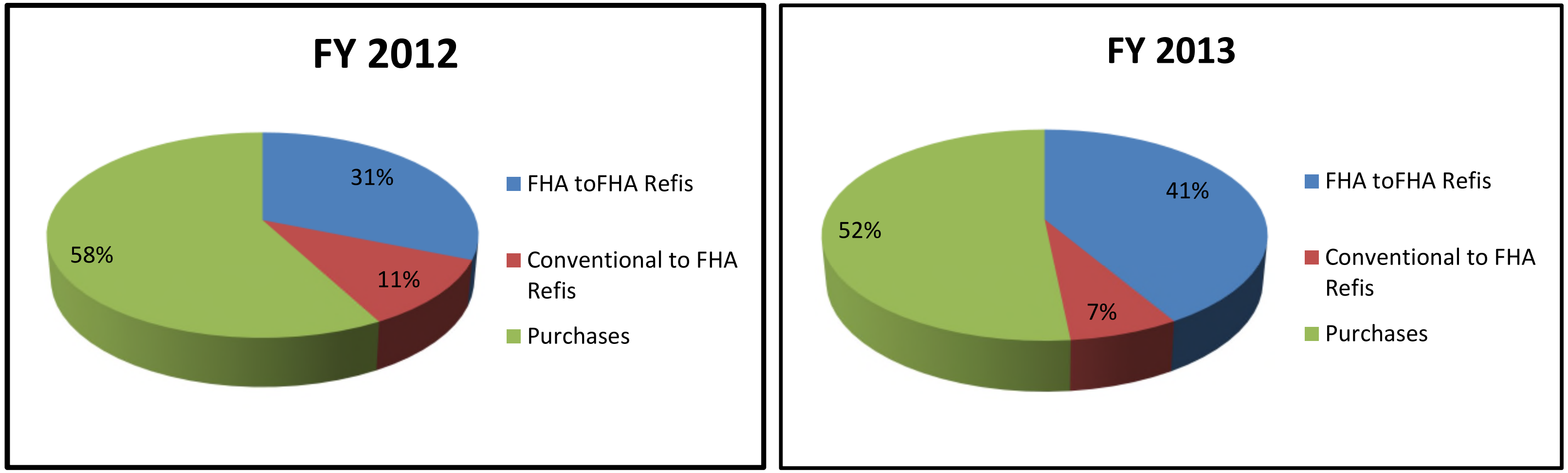
Forward Mortgages, FHA Short Refinances (Refi), and HECM.



Mortgage Insurance and Guaranteed Loans. The largest FHA insurance program is the single family program authorized under Section 203(b) of the National Housing Act. During fiscal year 2013, 92.7 percent of the $255 billion in insurance endorsements for the MMI Fund were under the Section 203(b) program. Beginning in fiscal year 2009, FHA consolidated a majority of its single family mortgage insurance programs under this risk category, including those for condominiums, purchase of homes on Indian and Hawaiian lands, and rehabilitation loans (Section 203(k)). Single family programs provide mortgage insurance for the purchase and refinance of homes with one to four units. Maximum mortgage amounts insured by FHA are calculated annually by HUD and are tied to the median house price in each county. Maximum mortgages in high cost areas were legislatively increased in 2008 in order to expand the number of families who would be able to access affordable mortgage financing during the economic downturn. On January 1, 2014, HUD implemented new FHA loan limits as required by the Housing and Economic Recovery of Act of 2008 (HERA). Under HERA, the FHA loan limit ceiling drops from $729,500 to $625,500 and the home-price multiplier drops from 125 percent of the median home price to 115 percent.

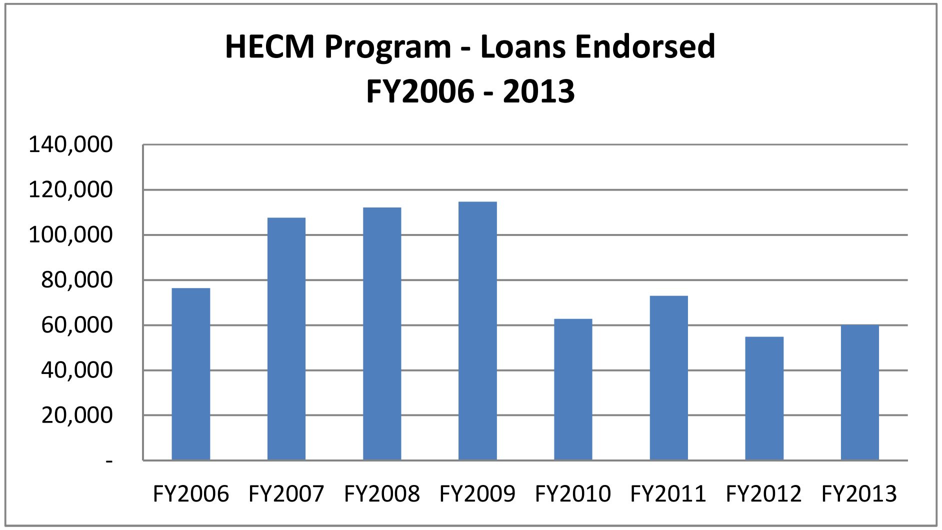
FHA endorsement activity peaked in fiscal year 2009, when monthly volume surpassed $25.8 billion, compared to just $4.7 billion per month in 2007. From this peak, FHA's annual endorsement volume dropped markedly in 2011 and 2012, but then increased in 2013 because of a large volume of refinance activity. Current estimates show that volume will decrease markedly in fiscal year 2014, with a further, but slight, decrease in 2015. FHA's current activity counts for its core home-purchase business are comparable to levels experienced in the mid-1990s, and lower than the experience of the 1998-2002 periods that preceded the recent boom-bust cycle.

203(b) Endorsement Volume by Loan Type



FHA Short Refinance. In fiscal year 2010, HUD and the Department of Treasury announced enhancements to FHA's refinance program that give a greater number of responsible borrowers the opportunity to remain in their homes. The enhancements were designed to maintain homeownership by borrowers who owe more on their mortgages than the value of their homes with opportunities to refinance into an affordable FHA loan. This program allows a borrower, whose mortgage is current, to qualify for an FHA refinance loan, provided that the lender or investor writes off the unpaid principal balance of the original first lien mortgage by at least 10 percent. FHA will accept applications for this program through the end of calendar year 2014.

HECM. FHA's HECM program allows senior homeowners age 62 and older access to FHA-insured reverse mortgages to convert the equity in their homes into monthly streams of income and/or a line of credit to be repaid when they no longer occupy the homes. In fiscal year 2013, HUD introduced new program requirements as a means to strengthen the MMI Fund and protect the viability of the HECM program. In addition to other requirements, homeowners will now be limited on the amount of equity that can be drawn within the first year of receiving a HECM loan and mortgage insurance premiums will be contingent upon the amount of funds withdrawn as a percentage of the principal limit factor. The amount a borrower is eligible for is based on the borrower's age, current interest rates, and the lesser of the appraised property value or the FHA mortgage limit for HECM. Currently, unlike forward mortgage borrowers, the HECM borrower has no income or credit qualifications to meet and makes no payments as long as the property securing the HECM loan continues to be the borrower's main residence; however, FHA is in the process of updating its policies to require a financial assessment. During fiscal year 2013, FHA endorsed more than 60,000 HECM loans with a total maximum claim amount of $14.7 billion.



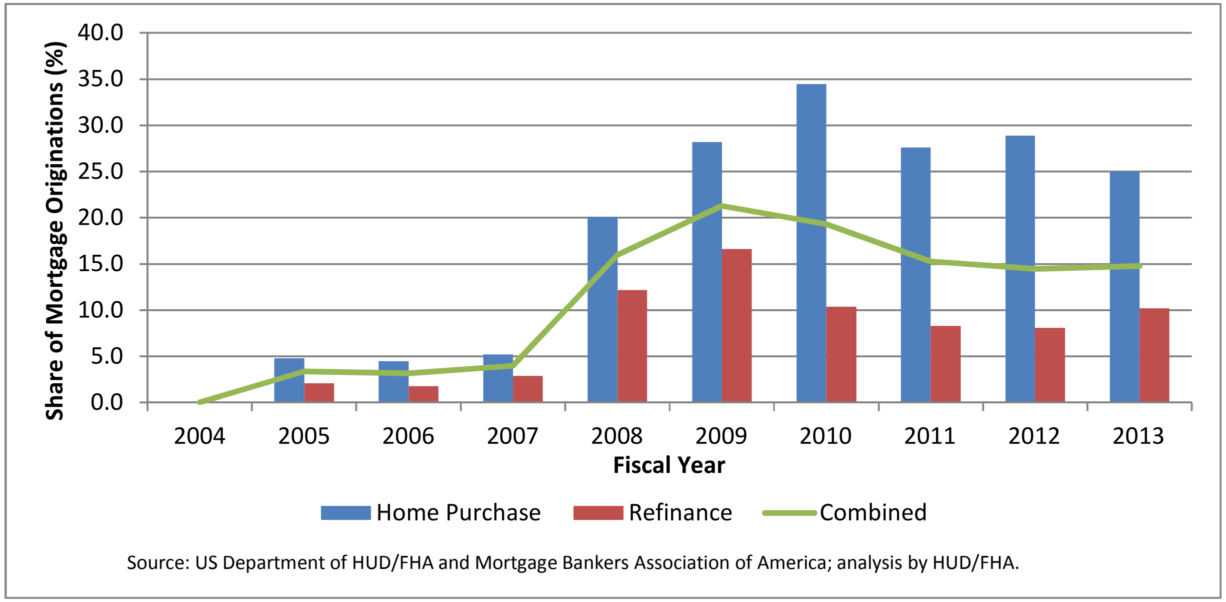
3. Why this program is necessary and what will we get for the funds?

FHA provides mortgage insurance on single family mortgage loans made by FHA-approved lenders throughout the United States and its territories. FHA's single family mortgage insurance program supports our nation's housing recovery by meeting the needs of borrowers facing difficult economic conditions, such as declining property values and contracting credit markets. FHA remains active and viable in all markets during times of economic disruption, playing an important counter-cyclical role until private capital returns to its normal levels. FHA will continue to meet the needs of many first time and minority homebuyers who–without the FHA guarantee–may otherwise find mortgage credit to be prohibitively costly.

The HECM program fills a special niche in the national mortgage market and offers critical opportunities for the nation's seniors to preserve their quality of life by tapping into their home equity. According to a 2009 study by MetLife's Mature Market Institute, today's issues of increased longevity, rising health care and other costs, fewer defined benefit pension programs, and diminished investment values have put extraordinary pressure on seniors in finding new sources of income and creative ways to stretch out accumulated savings during retirement. Options once available to tap home equity, such as selling the home and moving to less costly housing, are also more limited in today's market as homes can languish on the market for extended periods of time, and when they do sell, the price may be significantly below the homes' pre-crisis value. To supplement their budgets, older homeowners are increasingly considering the option of tapping their housing wealth. Consequently, reverse mortgages offer a viable option. Due to the tightening of conventional credit since the housing crisis, HECM has become nearly 100 percent of the reverse mortgage market. As the economy recovers, home prices rebound and credit becomes less constricted, conventional reverse mortgages will likely become available again. However, until then, FHA will continue to play a counter-cyclical role in this market, as it has with forward loans, providing access to credit. In addition to requesting commitment authority for HECM, the Budget will again propose to permanently lift the statutory aggregate cap of 275,000 HECM loan guarantees. Prior appropriations have lifted the cap on an annual basis. This change will help the program operate without disruption.

From the beginning of the HECM program in fiscal year 1990 through fiscal year 2013, over 965,999 loans have been endorsed under the program. Over 61 percent of these loans were endorsed during fiscal years 2007 through 2013. (HECM endorsements made prior to 2009 were under the General and Special Risk Insurance Fund.)

FHA Supports Mortgage Lending During Crisis
FHA As Share of Quarterly Mortgage Originations by Type (Percent)



Commitment Authority and Subsidy Projections

The fiscal year 2015 Budget request will provide the commitment authority and administrative funding for FHA to continue its important work.

Below is a table indicating loan commitment volumes, credit subsidy rates, and subsidy obligations for each MMI risk category in fiscal years 2014 and 2015. Credit subsidy rates represent the projected net cost (positive credit subsidy) or savings (negative credit subsidy) to the government of operating a loan guarantee program, and take into account projected claims, pre-payments, premium revenue, and recoveries on defaults for a cohort of loans over their lifetime. For more information on credit subsidy calculation please see the Notes section.

Estimates of single family commitment volume are calculated using both empirical inputs such as recent loan application volume and endorsement trends, as well as a variety of assumptions regarding expected condition in the housing and credit markets, interest rates, historic seasonal adjustment, and anticipated effect of program changes. These estimates are also very sensitive to other factors that cannot be readily anticipated or predicted, such as economic or fiscal policy changes. Even model variations in market trends or economic assumptions can result in significant changes in actual program demand and commitment volume.

MMI COMMITMENT VOLUME BY RISK CATEGORY (in millions)	FY 2013 Endorsements	FY 2014 Estimate	FY 2014 CSR	FY 2014 Subsidy Receipts	FY 2015 Estimate	FY 2015 CSR	FY 2015 Subsidy Receipts
MMI Purchase and Refinance	$240,126	$139,737	-7.25%	($10,131)	$134,707	-9.03%	($12,164)
MMI HECM	14,776	13,493	-0.41%	(55)	15,860	-0.23%	(36)
FHA Short Refinance	262	300	-0.00%	...	75	0.00%	...
FHA HAWK							10
Totals	$255,164	$153,530	-6.63%	($10,186)	$150,642	-8.09%	($12,190)

Administrative Contract Appropriations

The $170 million request for fiscal year 2015 will provide funding for contracts necessary in the administration of all FHA programs, including those operating under MMI and GI/SRI. (Beginning in fiscal year 2010, appropriations for FHA administrative contracts was consolidated under MMI to allow for more efficient management of funds.) This request will fund activities including, but not limited to: construction inspections on multifamily projects, the required annual FHA actuarial review and financial audit, management and oversight of asset disposition, risk analysis and accounting support, and assistance with claims and premium refund processing. The $43 million increase over the fiscal year 2014 appropriation is needed to fund further and needed improvements in risk management and mitigation. These new and expanded initiatives will allow FHA to incorporate lessons learned from the recent financial crisis to better protect its insurance fund and further promote operational efficiencies through the leveraging of Automated Valuations Methods (AVMs) to ensure optimal level pricing in REO management; leveraging of external Quality Control vendors to ensure appropriate depth and breadth of Quality Control reviews; development of risk analytics and modeling capabilities independent of actuarial review, and leveraging of industry vendors with best practices to develop and launch new, tier-based quality control and enforcement approach.

The benefits to be derived from these initiatives include the ability to: 1) leverage AVMs as part of business processes to reduce risks associated with inaccurate appraisals and ensure optimal recovery in loss mitigation; 2) leverage an external quality control vendor to add re-verification processes and absorb variations in sample sizes without taxing our already limited staff; 3) analyze portfolio risk, leverage external research and data on market trends, and enable more comprehensive and rapid policy change analysis in response to changing market dynamics; and 4) improve recovery rates for defective loans.

These initiatives are explained in detail below.

Quality Assurance/Compliance

FHA relies on private-sector lenders and servicers to underwrite and service endorsed loans. Occasionally, these lenders and servicers have operational failures that increase the likelihood of default and, thus, the likelihood of FHA having to pay a claim. When FHA detects a major operational failure, FHA generally asks the associated lender or servicer to indemnify FHA for any claims it has to pay on that particular mortgage loan or seeks other enforcement actions against that lender or servicer. FHA detects these failures through its quality-control and quality-assurance programs, wherein FHA reviews a subset of loan files, looking for errors made by its lenders and servicers. Over the past few years, FHA has significantly improved its enforcement policies and practices.

FHA's lenders and servicers work hard to avoid major operational failures, because indemnifying FHA for losses is very costly; however, some instances of failure will always remain. As such, lenders expect higher indemnification costs from making high-risk loans, so lenders curtail the amount they lend to high-risk populations. Unfortunately, it is precisely those high-risk populations that FHA seeks to help in fulfilling its mission to provide affordable housing to those most in need.

Over the past several months, FHA has been developing an alternative concept for conducting quality assurance and enforcement of loans it insures. In this new concept, FHA will create a framework that doesn't hinder or deter lending to FHA-targeted populations, facilitates timely feedback to lenders about underwriting quality, and increase efficiency of enforcement across all stakeholders. A common principle across all of these objectives is the need to look at a robust sample of loans early in the FHA process, thus minimizing the need to solely rely on adverse sampling criteria.

Currently, FHA has the capacity to review approximately 35,000 loans annually. This capacity is distributed largely to a risk-based sample of early defaulted loans. FHA believes it must increase its capacity to approximately 150,000 loans annually to ensure sufficient early sampling of endorsed loans, as well as still sampling early defaulted loans which are more likely to have defects.

Portfolio Analytics

As FHA works to improve and strengthen its capability for detecting and mitigating front and back end portfolio risks, access to timely and decision useful data is key. Essential to FHA's risk management strategy is its ability in fiscal year 2015 to procure comprehensive services and tools that allow the Office of the Chief Risk Officer to model risk at the portfolio levels and to perform data analysis to identify key credit risk drivers, segmentation profiles and emerging trends in credit and operational risk. In addition, the future state of FHA's risk and fraud detection business environment calls for continue work on the integration of FHA's risk and fraud tools with its credit score card. The benefits to be derived from these services include improved cash flow projections, better accuracy in budget inputs and subsidy modeling, reduced claims against the capital reserve and informed executive decisions and policies that are supported by healthier data.

Automated Valuation Model (AVM) and Broker's Price Opinion (BPO) to support Real Estate Owned (REO) Property Values

Traditionally, the Federal Housing Administration (FHA) initial list price for its real estate-owned (REO) property is based solely on an appraisal. Based on discussions with other stakeholders, FHA has learned that other market holders of REO properties establish the list price of their REO properties based on at least two valuation tools (Appraisal and/or Automated Valuation Model (AVM) , Broker's Price Opinion (BPO), etc.). FHA has conducted pilots in the Santa Ana Homeownership Center (HOC) and the Atlanta HOC to test the price variance by establishing the list price of their REO properties based on at least two valuation tools, and initial results indicate that in certain markets, appraisals are lagging the market, which has resulted in FHA not maximizing its recovery rates. The pilots have resulted in offers of approximately 104 percent of appraised value, compared to 93 percent nationally. Expanding these tools and approach would lower losses to MMIF by more than 10 percent.

4. How do we know this program works?

FHA single family insurance is known to work, not only because it provides a counter-cyclical backstop, but also because it: 1) increases liquidity for mortgage lending, including mortgage lending for low wealth families; 2) serves as a primary source of mortgage credit for minority and first time homebuyers; and 3) has key features that provide consumer protections that were lacking in much of the private lending leading up to the mortgage market collapse.

FHA continuously monitors and evaluates the results of its programs, and updates its policies as necessary to take into consideration product performance as well as market forces. To address current and difficult conditions in the housing market, aid homeowners, and mitigate risk to FHA's insurance fund, FHA develops new programs, modifies existing programs and improves controls. For example, FHA has recently modified its premium structure and tightened underwriting requirements for forward mortgages, steps necessary to raise negative subsidy receipts and restore FHA's capital reserve.

The continued weakness in the housing market and reduction in private lending have increased the demand for loss mitigation actions, and FHA has expanded its tools to meet that need. The Department has provided increased targeted loss mitigation training for lenders, and has increased monitoring of mortgagees and servicers to assure they are making sincere efforts to curb foreclosures. As part of its annual performance plan, the Department established an agency priority goal to assist homeowners who are at risk of losing their homes due to foreclosure. For FHA, that translates to specific targets and tracking of its early delinquency intervention efforts and loss mitigation program. HUD's loss mitigation efforts can be considered successful only if the program has effective solutions for homeowners in both the short and long term. Over fiscal years 2012 and 2013, FHA has a 2-year goal of having 500,000 homeowners assisted through early delinquency interventions and 200,000 assisted through loss mitigation programs, with an additional goal of having at least 80 percent of loans receiving this assistance to be current on their mortgages for at least 6 months. FHA exceeded its goals by 20 percent and 70 percent, respectively, and 938,734 homeowners were assisted in total. Through the end of FY 2013, 91.62 percent of loans that received assistance remained current for at least 6 months.

Strengthening FHA's Capital Reserves

HUD continued to strengthen the MMI Fund and improve the quality of endorsements by implementing a number of policy changes in 2013. These include:

- Premium increases – Building upon 2012 increases to mortgage insurance premium (MIP) rates, HUD again increased by 5 to 10 basis points the annual insurance premium for all forward mortgages except single family forward streamline refinance transactions that refinance existing FHA loans that were endorsed on or before May 31, 2009, and loans in Indian reservations and Hawaiian homeland.

- HUD also removed the exemption from the annual MIP for loans with terms of 15 years or less and loan-to-value ratios of less than or equal to 78 percent at origination. All loans are now subject to an annual mortgage premium. In addition, HUD revised the period for assessing the annual MIP for the maximum period permitted under statute, which, for most FHA-insured loans, will result in required MIP payments for the life of the loan.

- Lender enforcement – Mortgagee Letter 2013-12 was published on May 1, 2013, it implemented a final rule published in January 2012, which outlines new indemnification requirements for lenders participating in the Lender Insurance (LI) Program. Lenders are now required to indemnify HUD for losses associated with loans that were improperly originated, or for which fraud or misrepresentation were involved. This rule and Mortgagee Letter permits FHA to improve its oversight of LI lenders and better protect its insurance Funds from the adverse effects of non-compliant loans. FHA also continues to evaluate other opportunities to further strengthen its counterparty risk management.

- Loss mitigation – A Mortgagee Letter published on November 16, 2012, outlines FHA's update to its loss mitigation home retention options. One of the key elements of this update was moving FHA's Home Affordable Modification Program (HAMP) product up in FHA's loss mitigation waterfall so servicers could more quickly offer deeper payment relief to struggling FHA borrowers, resulting in an increase in the number of borrowers being able to retain their homes. FHA is also exploring additional mechanisms to facilitate refinance activity whereby distressed borrowers can benefit from today's low interest rates, and the execution of a robust and impactful housing counseling strategy that equips homeowners to make smart housing choices and obtain assistance when necessary.

- Borrower qualifications – HUD now requires manual underwriting for borrowers with credit scores below 620 and a debt- to-income ratio greater than 43 percent.

- REO and Pre-REO recovery - Through the Distressed Asset Stabilization Program (an expanded and targeted version of the Mortgage Acquisition and Disposition Initiative (601 Notes Sales)), FHA has implemented a successful strategy to increase REO recovery rates and limit losses to the MMI Fund. In Fiscal Year 2013, HUD sold approximately 36,700 non-performing loans in competitive sales with a combined unpaid principal balance of $6 billion. Of the loans sold, approximately 7,900 loans, with a combined unpaid principal balance of $1.25 billion, were sold with neighborhood stabilization requirements in Atlanta, Ohio, Orlando, Florida, California, North Carolina, and Chicago. FHA is also utilizing other innovative strategies, including ramping-up what was a pilot program into a broad-based effort whereby foreclosed properties are sold and a claim paid by FHA without the conveyance of these properties to FHA. These strategies build upon FHA's success in improving its REO disposition process, and, together with FHA's work to comprehensively address asset management and disposition, will have a measurable impact on improving loss severities arising from non-performing FHA-insured loans.

- HECM – Mortgagee Letter 2013-01 was published on January 30, 2013 and announced the consolidation of the Fixed Rate HECM Standard program's initial mortgage insurance premiums and maximum principal limit factors with those of the Fixed Rate HECM Saver, which resulted in a reduction of the maximum amount of funds available to a HECM borrower.

On July 30, 2013 Congress enacted P.L. 113-29, the Reverse Mortgage Stabilization Act of 2013, to authorize the Secretary of Housing and Urban Development to establish additional requirements to improve the fiscal safety and soundness of the HECM program. As a result, additional changes to the program became effective October 1, 2013, via mortgagee letter, thereby ensuring the long-term viability of the HECM program. These measures include:

  - Capping draws in the first year to the greater of 60 percent of the principal limit or mandatory obligations plus 10 percent of the principal limit;
  - Replacing the Standard and Saver principal limit factors (PLFs) with a single set of PLFs set at 85 percent of the baseline Standard PLFs;
  - Replacing the Standard and Saver upfront mortgage insurance premiums (MIPs) with a two-tiered MIP structure set at 50 bp for draws of 60 percent or less of the initial principal limit and 250 bp for draws greater than 60 percent;
  - Conforming calculation of MIPs for refinance transactions to the new MIP structure; and;
  - Requiring financial assessments and funding requirements for the payment of property charges based on the financial assessment.

- In total, FHA expects that the steps outlined above will protect and strengthen FHA's MMI Fund and assist in returning the Fund's capital ratio to a level of 2 percent. The 2013 actuarial review indicated the MMI portfolio is expected to reach a capital ratio of 2 percent during fiscal year 2015 (2016 if reserve is measured by its ratio to the unamortized balance of insurance).

Increasing Sustainable Access to Credit and Protecting the MMIF

HUD recently launched an innovative initiative called FHA HAWK (Homeowners Armed With Knowledge) to affirm FHA's important role in making homeownership available and sustainable for American families. FHA-HAWK is an umbrella for several FHA initiatives to bring the documented benefits of HUD-approved housing counseling to FHA borrowers. These benefits include improved loan performance, as counseled borrowers perform better than similar borrowers that do not receive housing counseling and increased access to home mortgages for first-time buyers underserved by the current mortgage market. There is strong and mounting evidence that properly structured and delivered housing counseling provides a significant benefit to borrowers, lenders, servicers and guarantors. In response, many states, local governments and large private lenders mandate or encourage housing counseling.

FHA-HAWK represents innovation and evidence-based policy in a number of ways:

a. It is consumer-driven, incorporating behavioral science principles to bring education and positive benefits to the consumer on a just-in-time basis.

b. HAWK counseling will occur at the points in time when it is most useful: before the home purchase contract is signed, before the loan closes, during the first year of homeownership, and before delinquent loans are modified.

c. In exchange for the consumer's commitment to work with a HUD-approved housing counseling agency, FHA will offer incentives through reductions in the upfront MIP and the annual MIP, and incorporate the counseling process into loan modifications.

d. The program incorporates extensive research on the impact of housing counseling on consumer outcomes and loan performance, as well as the experience of more than 100 state and local programs that link housing counseling to the home mortgage process. HUD will also leverage initiatives and experience from other agencies, including FHFA, Fannie Mae, Treasury, CFPB, and the Veterans Administration.

The 2015 budget includes two initiatives: Pre- and Post-Purchase HAWK

Pre-Purchase HAWK

HAWK for New Homebuyers will pilot an incentive-driven model of pre-purchase counseling for FHA first-time homebuyers. The MMI Fund is expected to benefit from this initiative from a reduction in serious delinquent loans of first-time homebuyers. Studies performed by Freddie Mac (2013), Mayer (2012) and Agarwal (2010) have shown reductions in serious delinquencies by nearly 30% for homebuyers who complete housing counseling with a HUD-approved agency. FHA expects to achieve similar results in the pilot, which will transition to permanent policy to provide incentives for first-time homebuyers to complete a course of pre-purchase and post-closing housing counseling with HUD-approved housing counseling agencies. Participation in the pilot would be capped at 100,000 closed and endorsed loans per year for up to four years and is subject to an allowance of $10 million in reduced negative subsidy receipts included in the 2015 Budget estimates. The pilot will allow for an initial start-up period and time for program evaluation to test operational capacity, methods of attracting homebuyer participation, and loan performance results. Although participation in housing counseling is voluntary, the proposed incentive structure is expected to motivate a significant number of first-time homebuyers coming into the FHA portfolio to participate in housing counseling. HUD is prescribing the timing and content associated with the housing counseling and education, which will be aligned with existing HUD standards and National Industry Standards for Homeownership Education and Counseling. The program will include several interventions: housing counseling prior to the contract of sale; prior to loan closing; and during the first year post-closing. The borrower will earn the discount on the first year's annual MIP with 12 months of on-time payment in addition to participation in post-closing housing counseling. There will be a permanent MIP step-down for HAWK borrowers who retain FHA loans more than 3 years after closing. HAWK will run parallel to an extensive randomized study of the long-term impacts of pre-purchase housing counseling on mortgage and household outcomes that is just underway, and an internal evaluation of the HAWK for New Homebuyers program is part of the pilot design.

Post-Purchase HAWK

The second HAWK initiative, *Modification Success Program*, seeks to connect defaulted borrowers to housing counseling prior to permanent loan modification, providing a consumer-friendly approach to help reduce defaults on modified loans. This approach will integrate housing counseling into default servicing and the FHA loss mitigation process. Building on a counseling outreach requirement imposed by the Treasury for HAMP Servicers, FHA would impose similar requirements on servicers as part of their loss mitigation activities. The program would require servicers to conduct outreach to borrowers, but borrowers' decision to obtain housing counseling would remain voluntary; it would not be a condition of obtaining the modification. The goal is to increase the number of borrowers who obtain delinquency counseling in connection with receiving a modification, which should reduce defaults on the modifications and thereby reduce claims to the MMIF. This initiative builds on the results of a Fannie Mae pilot in which servicers offered counseling to borrowers when they were beginning a trial modification plan. Counseled borrowers were more likely to be current on modifications after 12 months in a permanent modification, showing a 32.4 percent improvement over non-counseled borrowers. Recidivism to serious delinquency (90 or more days late on a payment) for counseled borrowers decreased from 19.2 percent to 12.3 percent (a 36 percent improvement) after adjustment for selection bias. An innovative aspect of this program is that servicers are required to build an infrastructure for connecting borrowers to counselors, which can be used to target different borrower groups in the future as the FHA portfolio changes and analysis identifies borrowers who would benefit from outreach to connect them to counseling. The Modification Success Program gives FHA greater flexibility going forward in helping troubled borrowers while protecting the MMIF.

Strengthening FHA Business Practices – FHA Transformation IT Investments

FHA Transformation is developing and implementing a modern financial services IT environment to better manage and reduce risk across all of FHA's Mortgage Insurance Programs. To date, FHA Transformation has delivered a new lender certification system, and has made sound progress on the Single Family Housing's systems and its new risk management tool. HUD has also made critical enterprise software and infrastructure investments for FHA that will reduce maintenance costs once the FHA Transformation initiative is complete.

FHA Transformation will allow HUD to start the careful process of migrating relevant portions of Housing's legacy applications into a modern automated financial service environment, and will help administer many aspects of the multifamily and health care insurance programs. FHA Transformation monitoring and enforcement projects will allow the Office of Lender Activities to automate many current manual processes.

FHA Transformation will also bring a new level of intelligent rules-based activities such as automated risk analysis and lender targeting according to a risk scoring framework. This will help HUD manage its credit risk prudently at the portfolio and loan levels, and will enable HUD to respond rapidly to changing market conditions. The new Federal Financial Services Platform will be leveraged across several Housing programs by migrating away from the 30-year old Computerized Home Underwriting Management System (CHUMS). These FHA Transformation initiatives will enable FHA to better recognize risk and fraud trends in borrower attributes, collateral attributes, and appraisal valuation accuracy during the transaction process, and to help identify cases that may be detrimental to the MMI fund.

The next steps for FHA Transformation will enable risk detection and fraud prevention by capturing critical data points at the front-end of the loan life cycle; and will leverage the right set of risk and fraud tools, rules-based technology, and transactional controls to minimize exposure to FHA's Insurance Funds. These IT investments will facilitate enhanced business analytics and informed decision-making by providing decision-makers with higher quality data that is more up-to-date. This will enable FHA's leadership to analyze portfolio trends and patterns across the lending community, and will help with the identification of fraudulent lenders and reduce risk in the FHA portfolio.

Risk Management

The major objective of the Office of Risk Management and Regulatory Affairs (ORMRA) is to: conduct analysis and recommend actions to reduce exposure to FHA insurance funds while meeting its housing mission; ensure that FHA operates in compliance with statutory capital requirements; and promote a well-controlled operational infrastructure. The risk management staff's scope of credit and operational risk management work encompasses Program Area (Single Family, Multifamily and Healthcare) activities conducted at headquarters and the Field Offices.

ORMRA performs the following functions to manage risk:

- performs analyses and recommends actions to support FHA's ability to reduce risk exposure to its insurance funds;
- identifies the policies and processes that are key drivers of risk via a structured risk identification framework;
- recommends risk mitigation strategies for FHA and specific program areas and provide independent oversight and assessment of risk remediation activities;

- designs and maintains a comprehensive risk governance infrastructure, including implementing policies, processes, and committees to reduce risk exposure to the insurance funds;
- maintains risk management processes to perform independent internal risk and control assessments aligned with federal standards, including front end risk assessments of new and high impact programs and activities; and
- ensures that risks are measured, monitored and managed according to an integrated framework across programs.

5. Legislative/Regulatory Proposals

Proposals included in the 2015 Request

- Administrative Support Fee – Up to $30 million in fees to be charged to lenders pursuant to section 202 of the National Housing Act, as amended by section 244 of the General Provisions. Collection of the receipts from such fees will be credited as offsetting collections to the MMI Program account. Up to $15 million of the total fees may be transferred to the Housing Salaries & Expenses account.
- Permanent Removal of HECM cap – (section 209 of the General Provisions) This provision removes the aggregate mortgage cap in Section 255(g) of the National Housing Act (Act), which limits the total number of Home Equity Conversion Mortgages (HECM) loans that can be insured by the FHA. The Department proposes to repeal the first sentence in the Act to remove the cap permanently.
- Clarification on Non-Borrower Spouse Upon Death of HECM Borrower – (section 228 of the General Provisions) This section revises the National Housing Act to clarify that the HECM becomes due and payable on the death of the mortgagor spouse. This clarifies that a non-mortgagor spouse cannot benefit from the HECM despite the death of the mortgagor spouse.

6. Notes to Justification

Credit Subsidy Calculations and the Annual Re-estimate

Credit subsidy rates represent the projected net cost or savings to the government of operating a loan guarantee program, and take into account projected claims, pre-payments, premium revenue, and recoveries on defaults for a cohort of loans over their lifetime. In accordance with the Credit Reform Act of 1990, administrative costs (excluding property disposition) are not included in credit subsidy calculations. FHA credit subsidy rates reflect historic performance data for similar loans made over the past 40 years, with adjustments made for significant policy shifts as well as changing economic and market conditions. The Department devotes significant efforts to updating and continuously refining the credit subsidy estimates. Each year the extensive statistical base, from which projections of future loan performance are calculated, is updated with an additional year of actual data. The Department and OMB continue to examine the data, assumptions, and calculations that are used to estimate loan program cash flows and subsidy rates in order to eliminate errors and improve the accuracy and reliability of projections.

Each year, FHA completes a required re-estimate of liabilities and subsidy costs associated with the existing insurance portfolio. Revised liability estimates take into account another year of actual loan portfolio performance and the latest economic assumptions. Vacancy rates, Treasury interest rates, and house price appreciation are among the key variables that shape MMI projected cash flows. Multivariate statistical models generate the claim and prepayment rates that drive the fund's financial worth. To determine the amount of the re-estimate, the revised liabilities (net of projected loan default recoveries) are compared to the current assets on hand. When assets exceed projected liabilities, a downward re-estimate occurs with the difference being transferred from the Financing Account to the MMI Capital Reserve account. When projected liabilities exceed assets, an upward re-estimate occurs and the fund must transfer cash from its Capital Reserve account to bring the assets and liabilities in balance. For example, if the portfolio of loans made in a given year has a net liability of $250 million and cash on hand of $300 million, then the cohort would require a downward re-estimate in which $50 million would be moved from the fund's Financing account (which handles all loan guarantee cash flows) to the MMI Capital Reserve account. If the financial position was reversed – if a cohort had assets of $250 million and a net liability of $300 million – then a $50 million upward re-estimate would be transferred from the Capital Reserve Account to the MMI Program Account (an "on-budget" account) and then forwarded to the Financing Account to ensure it contained sufficient resources to cover the anticipated lifetime liabilities of the portfolio.

Re-estimates are calculated each year for each cohort of loans (from 1992 onward). As of 2013, 20 MMI cohorts had a lifetime upward re-estimate, meaning the original subsidy calculation is now believed to have underestimated the costs. Two cohorts had net lifetime downward re-estimates, meaning costs to the government for that group of loans are now projected to be less than the original subsidy calculation.

HOUSING
FHA – MUTUAL MORTGAGE INSURANCE FUND
Summary of Resources by Program
(Dollars in Thousands)

Budget Activity	2013 Budget Authority	2012 Carryover Into 2013	2013 Total Resources	2013 Obligations	2014 Budget Authority/ Request	2013 Carryover Into 2014	2014 Total Resources	2015 Request
Administrative Contract Expense	$128,413	$15,968	$144,381	$110,146	$127,000	$34,185	$161,185	$170,000
Working Capital Fund transfer	67,760	...	67,760	...	...	...	...	...
Transformation Initiative (transfer)	...	...	...	...	...	...	...	[850]
Total	196,173	15,968	212,141	110,146	127,000	34,185	161,185	170,000

HOUSING
FHA – MUTUAL MORTGAGE INSURANCE FUND
Appropriations Language

The fiscal year 2015 President's Budget includes proposed changes in the appropriation language listed and explained below. New language is italicized and underlined, and language proposed for deletion is bracketed.

MUTUAL MORTGAGE INSURANCE PROGRAM ACCOUNT

New commitments to guarantee single family loans insured under the Mutual Mortgage Insurance Fund shall not exceed $400,000,000,000, to remain available until September 30, **[**2015**]** *2016*: *Provided*, That during fiscal year **[**2014**]** *2015*, obligations to make direct loans to carry out the purposes of section 204(g) of the National Housing Act, as amended, shall not exceed $20,000,000: *Provided further*, That the foregoing amount in the previous proviso shall be for loans to nonprofit and governmental entities in connection with sales of single family real properties owned by the Secretary and formerly insured under the Mutual Mortgage Insurance Fund. For administrative contract expenses of the Federal Housing Administration, **[**$127,000,000,**]** *$170,000,000*, to remain available until September 30, **[**2015**]** *2016, of which up to $15,000,000 may be used for necessary salaries and expenses of the Federal Housing Administration, which is in addition to amounts otherwise provided under this title for such purposes: Provided further, That any amounts to be used in fiscal year 2015 for such salaries and expenses pursuant to the previous proviso shall be transferred to the "Housing" account under the heading "Program Office Salaries and Expenses" under this title and shall remain available until September 30, 2015, and any such transferred amounts may be transferred back to this account on or before September 30, 2015, and shall remain available until September 30, 2016*: *Provided further*, That to the extent guaranteed loan commitments exceed $200,000,000,000 on or before April 1, 2014, an additional $1,400 for administrative contract expenses shall be available for each $1,000,000 in additional guaranteed loan commitments (including a pro rata amount for any amount below $1,000,000), but in no case shall funds made available by this proviso exceed $30,000,000*; Provided further, That receipts from administrative support fees collected pursuant to section 202 of the National Housing Act, as amended by section 244 of this title, shall be credited as offsetting collections to this account*. *(Department of Housing and Urban Development Appropriations Act, 2014.)*

HOUSING
GENERAL AND SPECIAL RISK INSURANCE FUND
2015 Summary Statement and Initiatives
(Dollars in Thousands)

FHA--GENERAL AND SPECIAL RISK INSURANCE FUND	Enacted/ Request	Carryover	Supplemental/ Rescission	Total Resources	Obligations	Outlays
2013 Appropriation	...	$16,403	...	$16,403	...	$408
2014 Appropriation/Request	...	16,403	...	16,403	...	5,000
2015 Request	...	16,403	...	16,403	...	...
Program Improvements/Offsets	...	...	...	...	...	-5,000

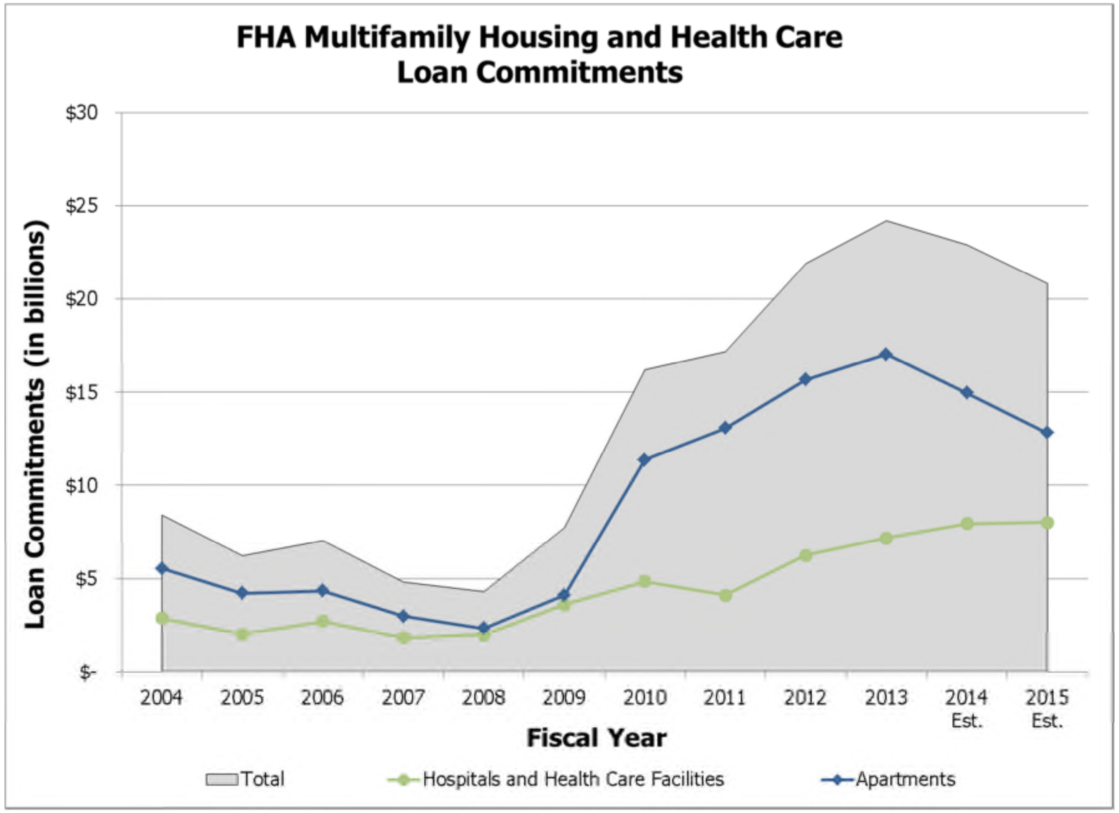
1. What is this request?

Loan guarantee programs operating under the Federal Housing Administration's (FHA) General Insurance and Special Risk Insurance (GI/SRI) Fund encourage critical mortgage financing opportunities that strengthen communities across the country. GI/SRI houses a wide range of mortgage insurance products to address specialized financing needs, including insurance for loans to develop, rehabilitate, and refinance multifamily rental housing, nursing home facilities, and hospitals. GI/SRI programs also include loan guarantees for Title I manufactured housing and for property improvement loans.

FHA's multifamily and healthcare programs are a critical component of the Department's efforts to meet the Nation's need for decent, safe and affordable housing. At a time, in particular, when there is unprecedented stress in the financial markets, FHA Multifamily programs provide the necessary liquidity so that communities can continue to provide quality affordable housing and assisted living/nursing home opportunities. In fiscal year 2014, FHA is now projected to issue loan insurance commitments providing financing for over 1,450 apartment projects and for 800 healthcare facilities. There will likely be an increase in the Multifamily Risk Share program and affordability initiatives. With the anticipated increase in interest rates, FHA expects to see volume decline in the refinance programs over the course of 2014 and fiscal year 2015, then stabilize over the next several years as private mortgage markets are strengthened.

FHA mortgage commitment issuances for multifamily housing and healthcare rose from $4.3 billion in fiscal year 2008 to $15.9 billion in 2010 to approximately $25 billion in 2013. Volume in fiscal year 2013 was constrained by the $25 billion commitment limitation, which did not fully accommodate demand for FHA insurance products. At the end of fiscal year 2013, GI/SRI's multifamily/healthcare portfolio had an unpaid principal balance (UPB) of $93.4 billion on 13,365 loans, an increase of $8.5 billion over that at the end of September 2012. FHA's multifamily programs have helped private lenders fill the gap resulting from the shrinkage of conventional financing resources. Historically low interest rates provided the opportunity for FHA to strengthen and preserve its existing Multifamily and Healthcare portfolio through refinancing. As the private industry prepares to increase its share of the housing market and interest rates rise, FHA is requesting access to more loan guarantees to provide the necessary liquidity during that transition. The fiscal year 2015 request for GI/SRI includes four components:

- **Commitment authority for up to $30 billion in new loan guarantees, the same level as the FY 2014 request.** New insurance commitments reached the $25 billion limitation in fiscal year 2013, and are expected to be a little over $23 billion in fiscal year 2014. Preliminary estimates show a decline to $21 billion in fiscal year 2015, attributable to a marked reduction in apartment refinance activity. The amount requested above the fiscal year 2015 projection will minimize the potential for reaching the limitation and having to suspend program activity prior to the end of the year due to unpredictable market conditions. Of the total commitments projected for fiscal year 2015, it is estimated that $13 billion will be issued for FHA's multifamily housing programs. Another $8 billion is estimated for hospitals, nursing homes, and assisted living facility mortgages. Title I Property Improvements and Manufactured Housing commitments are expected to make up less than 1 percent of new activity in the fund.



- **Offsetting receipt estimates from negative credit subsidy.**

  Negative subsidy receipt estimates for fiscal year 2015 for GISRI are estimated at $876 million in the President's fiscal year 2015 budget, with the subsidy rate for new business averaging -4.23%. No new appropriations for positive credit subsidy are requested for fiscal year 2015, the same as in fiscal years 2013 and 2014. In fiscal year 2013, FHA indefinitely suspended new activity for three GI/SRI programs that were not self-supporting, and realigned certain supplemental loans to the risk categories of the primary FHA mortgage, for which they enhanced or maintained performance.

- Funding for administrative contracts associated with GI/SRI programs was realigned to the Mutual Mortgage Insurance (MMI) Fund beginning in fiscal year 2010 to enable more efficient management of FHA resources.

- **Commitment authority for up to $20 million in direct loans to facilitate single family property disposition.**

  The loan authority requested is for short-term purchase money mortgages for non-profit and governmental agencies to make HUD-acquired single family properties available for resale to purchasers with household incomes at or below 115 percent of an area's median. This program has been infrequently utilized in recent years, but remains a valuable tool for HUD in managing its property portfolio.

	2013 Enacted	**2014 Enacted**	**2015 Request**	**Increase/ (Decrease)**
Loan Guarantee Commitment Limitation	$25,000,000,000	$30,000,000,000	$30,000,000,000	...
Direct Loan Limitation	$20,000,000	$20,000,000	$20,000,000	...

<u>Salaries and Expenses (S&E) and Full-Time Equivalents (FTE) Request</u>

The primary workload for FHA programs in the GI/SRI Fund is carried out by HUD's Office of Housing, mainly the Office of Multifamily Housing and the Office of Healthcare programs. Critical functions are also supported by financial management, procurement, Information Technology, and other administrative organizations.

A total of 912.5 FTE are requested for the Multifamily and Healthcare Programs, which is a decrease of 62.0 FTE from the fiscal year 2014 estimate. Total S&E funding is $128.9 million, or a decrease of $1.9 million from the fiscal year 2014 estimate. These decreases are primarily the result of efficiencies gained from the implementation of the Multifamily Transformation initiative.

GI SRI (Dollars in Thousands)				
	Personnel Services	**Non-Personnel Services**	**Total**	**FTE**
Finance and Budget	9,981	65.0	10,046	78.2
Healthcare Asset Management and Recapitalization	10,504	254.0	10,758	75.1
Healthcare Policy Development	1,133	28.0	1,161	8.1
Healthcare Production and Processing	8,671	211.0	8,882	62.0
Multifamily Asset Management and Recapitalization	19,614	1,154.0	20,768	138.3
Multifamily Policy Development	4,580	57.0	4,637	36.1
Multifamily Production and Processing	67,079	2,369.0	69,448	494.7
Risk Management	3,004	217.0	3,221	20.0
Total	**124,566**	**4,355**	**128,921**	**912.5**

2. What is this program?

FHA has insured mortgages on over 41 million single family and multifamily properties since its inception in 1934 (under both MMI and GI/SRI Funds). As of the end of fiscal year 2013, the GI/SRI insurance portfolio included loans with an unpaid principal balance of $147.9 billion (including $54.5 billion in single family and HECM loans issued before 2009). These active loans cover more than two million apartments, healthcare facility beds, and single family homes across the nation. FHA mortgage insurance enhances a borrower's credit and provides banks with better access to capital markets, most notably through Ginnie Mae securities. In exchange for adherence to strict underwriting and application requirements established by HUD and the payment of annual insurance premiums, HUD-certified lenders are able to file claims with FHA when a borrower defaults. Mortgage insurance premiums and specific terms for claim payments vary by program.

FHA mortgage insurance works in part by helping private lenders access liquidity otherwise not available to borrowers developing or maintaining rental housing for low- and moderate-income families. The credit enhancement provided by an FHA loan guarantee (typically 100 percent) enables borrowers to obtain long-term, fully amortizing financing (up to 40 years in the case of new construction/substantial rehabilitation) which can result in substantial cost savings that can be passed on to residents. FHA mortgage insurance provides long-term amortization not found with conventional lending sources. The fact that FHA loans are fully amortizing protects properties from interest rate and liquidity risk in that project owners don't have to refinance with unattractive terms. The long-term amortization period and guarantee of payment in the event of claim stabilizes interest rates and allows monthly mortgage payments to be less than payments required under non-insured financing. These savings in turn can also reduce the overall costs of developing and maintaining housing, stabilizing housing markets and benefiting low- and moderate-income residents. In a similar relationship, FHA financing of healthcare facilities contributes to lower healthcare costs for taxpayers and consumers.

Multifamily and healthcare loans – which now constitute 99 percent of new insurance commitments in GI/SRI – are much larger and substantially more complex than their FHA single family counterparts. Prior to receiving a mortgage guarantee for any multifamily or healthcare loan, lenders and borrowers must complete a rigorous application process in which HUD staff review borrower credit worthiness, project cash flow projections, property appraisals, architectural design, environmental impact, requested loan size, quality of the property management, and other information that establishes a loan as an acceptable credit risk to HUD. Large multifamily housing projects and all healthcare facility loans receive secondary review and approval by a national loan committee of senior HUD officials. Once insurance has been approved, progress on any new construction or renovations is closely monitored by HUD inspectors. HUD asset managers monitor project financial statements on an ongoing basis and periodic physical inspections are conducted by HUD's Real Estate Assessment Center. (Note that GI/SRI does not include funding for administrative contracts and program staffing, which are covered by appropriations under MMI and Housing Personnel and Benefits, respectively.) Loss mitigation measures – including a partial payment of claim policy approved in 2010 – are undertaken before a default and full claim on the loan occurs. When a borrower does default and a claim is filed, HUD will take possession of the mortgage note or property and seek to recover losses.

Active programs included under GI/SRI are authorized under Sections 220, 221(d)(3) with tax credits, 221(d)(4), 223(a)(7), 223(f), 223(d), 231, 241(a), 232, 207,and 242 of the National Housing Act and Sections 542(c) and 542(b) of the Housing and Community Development Act. In addition, GI/SRI includes single family property improvement and manufactured housing programs authorized by Title 1 of the National Housing Act. Sections of the act citations are commonly used to identify the programs, both within HUD and the housing industry. In the President's Budget, programs are identified and discussed according to their risk category. Risk categories are groupings of loans with similar terms and/or credit risks. A credit subsidy rate and loan volume projection is prepared annually for each risk category. For fiscal year 2015, there will be 11 risk categories within GI/SRI – 6 covering multifamily housing programs, 3 for healthcare facilities, and 2 for Title 1 programs. Each risk category is briefly described below.

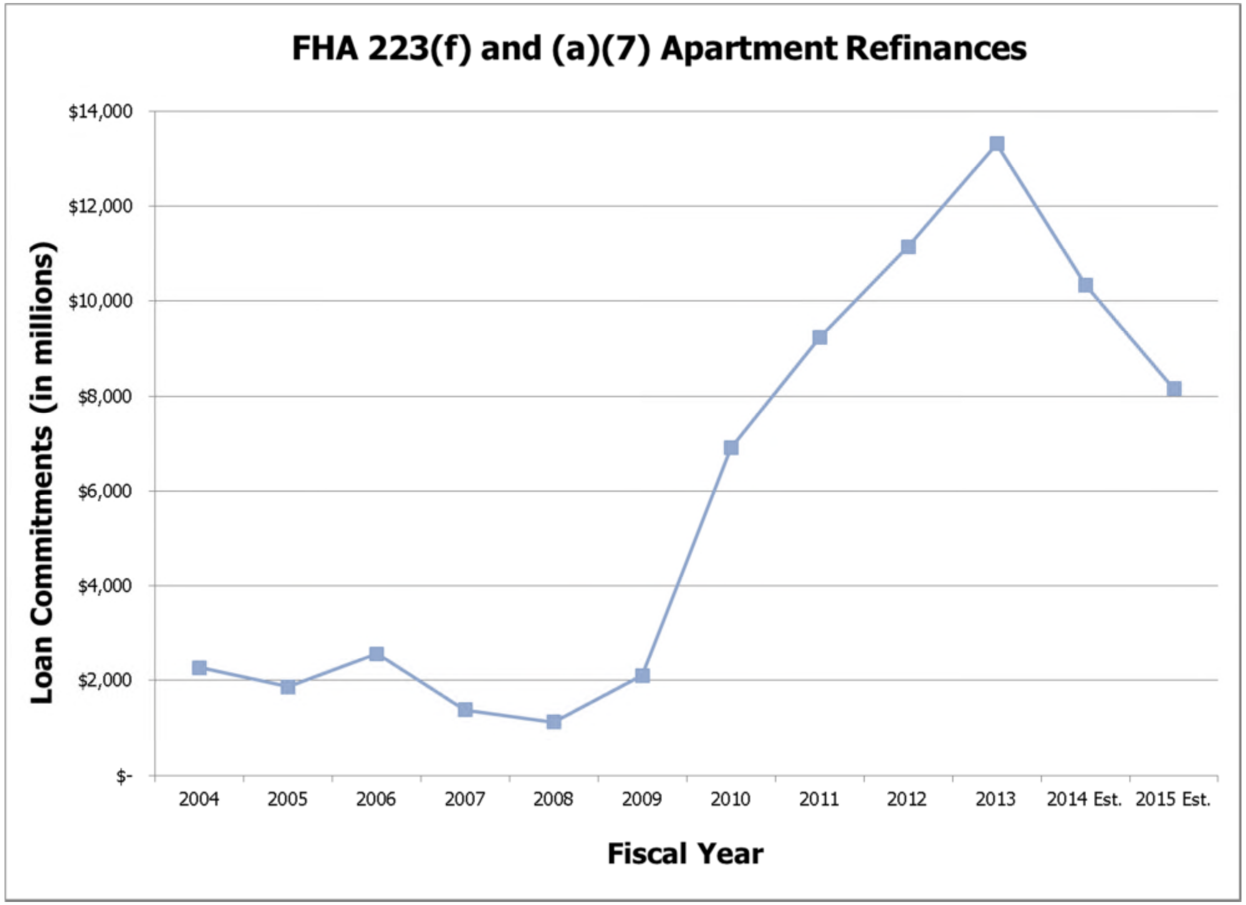
Beginning in fiscal year 2013 and continuing in fiscal year 2015, new insurance is not being issued for Section 223(d) operating loss loans to multifamily housing projects with a HUD-insured primary mortgage, Section 238(c) single family loans in military impact areas (suspended in March 2012), and Section 221(d)(3) loans to non-profit housing developers except when tax credits are being utilized. Section 241(a) supplemental loans to FHA-financed multifamily housing projects and Section 223(d) Operating Loss loans to heath care facilities with a primary Section 232 mortgage are reported in the budget risk category of the primary FHA mortgage.

Multifamily Housing Risk Categories

Section 221(d)(4) Mortgage Insurance for Rental and Cooperative Housing. The Section 221(d)(4) program is FHA's largest new construction/substantial rehabilitation for multifamily housing. In 2013, new Section 221(d)(4) loans averaged $14.4 million and included an average of 147 units. The program insures loans made primarily to profit-motivated sponsors, with financing allowed for up to 90 percent of the project replacement cost (as limited by debt service coverage and per-unit cost requirements). The program covers long-term mortgages of up to 40 years and, like all FHA new construction loan programs, provides for both construction and permanent financing. In 2010, HUD implemented tighter underwriting requirements for 221(d)(4) – with the largest adjustments coming for market-rate projects – to ensure deals in the rapidly increasing portfolio remain financially sound.

Section 223(f) Mortgage Insurance for Refinancing or Purchase of Existing Multifamily Rental Housing. Section 223(f) is currently the highest volume program operating under GI/SRI. It allows for long-term mortgages of up to 35 years for refinance or purchase of existing multifamily rental housing. Refinances of current FHA-insured multifamily loans are also offered under Section 223(a)(7), but are grouped together with Section 223(f) for budgetary purposes. Properties must have been completed or substantially rehabilitated for at least 3 years prior to the date of the application for mortgage insurance. This "3-year rule" may currently be waived for affordable housing projects that are now unable to obtain permanent financing.

The maximum mortgage limitation for a market-rate refinance transaction is up to 83.3 percent of the HUD appraised value. Commitments under these programs totaled $13.3 billion in fiscal year 2013, an increase of 19 percent over fiscal year 2012. This high level of activity has been due to the historically low interest rates for FHA insurance combined with Ginnie Mae securities. As rates rise, we expect the demand to drop by more than 35 percent over a two year period.



Section 241(a) Mortgage Insurance for Supplemental Loans for Multifamily Housing Projects. Section 241(a) provides mortgage insurance for supplemental loans for multifamily housing projects already insured or held by HUD. Beginning in fiscal year 2013, each 241(a) loan is assigned to the risk category of the associated primary FHA mortgage. In fiscal year 2013, FHA made 3 loan commitments under this program totaling $16.9 million. This program is intended to keep projects competitive, extend their economic life, and finance the replacement of obsolete equipment. Section 241(a) mortgages finance repairs, additions, and other improvements. These loans take second position to the primary mortgage.

Section 542(b) Risk Sharing with Qualified Participating Entities (QPEs). This is one of two multifamily programs under which FHA insures only a portion of the losses by sharing the risk with Fannie Mae, Freddie Mac, and other qualified Federal, State, and local public financial and housing institutions. If a loan insured under Section 542(b) defaults, the QPE will pay all costs associated with loan disposition and will seek reimbursement from HUD for 50 percent of the losses. A variation of Section 542(b), called "Green Refinance Plus," – introduced in 2011 – permits QPEs to offer loans to both preserve older affordable properties and install energy-saving features by allowing expansion of the QPE's Debt Service coverage and Loan-To-Value lending limits for qualified properties. With terms of 10, 15, or 30 years (all with 30-year amortization), "Green Risk Sharing" loans require an MIP higher than under the standard Section 542(b) program. Fannie Mae has closed four transactions under the program totaling 696 units. This variation of Section 542(b) is also known as "Green Risk Sharing" or "Risk Sharing Plus".

As in the fiscal year 2014 budget, the fiscal year 2015 Budget proposes amendments to the Section 542(b) authorizing statute that will facilitate lending to small multifamily properties, which are an important provider of affordable, but unsubsidized, housing for low- and moderate-income families. According to the 2010 American Community Survey, nearly one-third of all renters live in 5- to 49-unit buildings. The 2001 Residential Finance Survey also demonstrates that these small multifamily properties have lower median rents than larger properties: $400 per month for 5- to 49- unit properties, as compared to the $549 monthly rent for properties with 50 or more units. While 62 percent of unsubsidized 5- to 49- unit properties charge rent below $500 per month, just 38.5 percent of larger unsubsidized properties charge rent below $500 per month. At a time when federal budgets are shrinking and the need for affordable housing is growing, the amendments will allow us to preserve this vital asset without significant cost to the federal government, by drawing in state, local and community resources to these rental properties.

HUD will enter into Risk Share agreements with qualified lenders, such as well-capitalized Housing Finance Agencies or Community Development Financial Institutions, with demonstrated experience making loans for affordable housing. HUD could then work with these approved lenders to endorse loans to refinance and recapitalize small multifamily rental properties. The proposed legislation would allow qualified lenders to then securitize these loans with Ginnie Mae. The proposed language also simplifies the affordability requirements and provides more flexibility to use the Risk Share program to target small multifamily properties.

Section 542(c) Risk Sharing with Housing Finance Agencies (HFAs). Section 542(c) provides mortgage insurance of multifamily housing projects whose loans are underwritten, processed, serviced, and disposed of by state and local HFAs. FHA insurance enhances HFA bonds to investment grade and provides capital for affordable housing construction. HFAs may elect to share from 10 to 90 percent of the loss on a loan with HUD. Section 542(c) insured projects often include low-income housing tax-credits, in which case they are reported under GI/SRI's risk category for Tax Credit Projects.

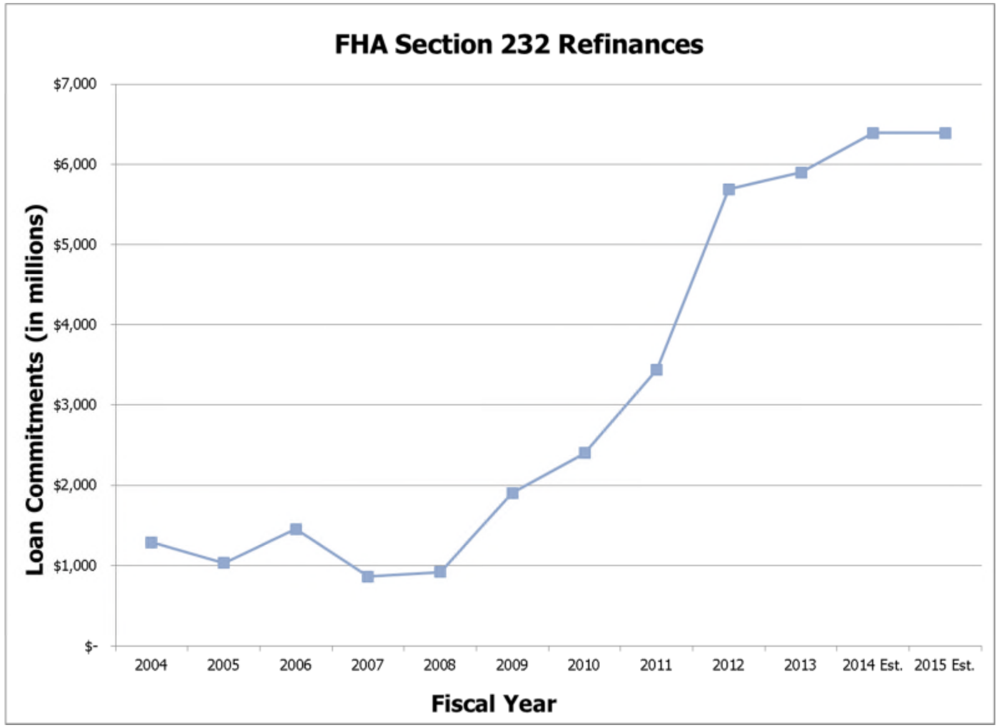
Other Rental Programs. This risk category includes several relatively low-volume programs that have been grouped together for budgetary purposes, including: Section 220 loans in urban areas, Section 231 loans for elderly housing, and Section 207 loans for mobile home park development. Section 220 is a new construction program, distinct from 221(d)(4) in that it insures loans for multifamily housing projects in urban renewal areas, code enforcement areas, and other areas where local governments have undertaken designated revitalization activities. The program offers special underwriting allowances for greater mixed-use development. Section 231 is also a new construction/substantial rehabilitation program, but for projects specifically designed for senior citizens. For Section 231 projects with 90 percent or greater rental assistance, the maximum loan amount is 90 percent of the estimated replacement cost. For market-rate projects, the maximum loan is 83.3 percent of the replacement cost.

Tax Credit Projects. Projects assisted with Low-Income Housing Tax Credits (LIHTC) may be insured under a number of FHA multifamily programs, but are grouped together in a single budget risk category. These loans have a lower risk of default than similar projects without tax credits and require borrowers to pay lower FHA mortgage insurance premiums. Use of Section 221(d)(4) with LIHTC will likely be consistent with original estimates for 2014 given recent increased interest in FHA lending by state HFA's and other mission driven lenders for new construction and substantial rehab transactions. We anticipate that use of Section 223(f) with LIHTC will begin to increase in 2014 and 2015 as a result of the Tax Credit Pilot introduced in spring 2012.

Healthcare Risk Categories

Section 232 New Construction/Substantial Rehabilitation of Skilled Nursing, Assisted Living, and Board and Care Facilities. Section 232 programs are split into two budget risk categories, the first of which includes new construction and substantial renovation projects. The program enables access to capital that may not otherwise be available for many quality providers in underserved areas, thereby providing access to needed healthcare and residences for seniors. These loans are offered for terms of up to 40 years, and provide both construction and permanent financing. This risk category also includes Section 241(a) supplemental loans made to projects with a primary FHA Section 232 mortgage.

Section 232/223(f) Refinancing and Purchase of Existing Skilled Nursing, Assisted Living, and Board and Care Facilities. The Section 232/223(f) refinancing program has grown to be one of the highest volume insurance programs in GI/SRI, due in great part to mortgagors of existing facilities taking advantage of refinancing at low interest rates. This program offers loan terms of up to 35 years. For a refinance, maximum mortgage amounts are up to 85 percent of appraised value (90 percent if the borrower is a non-profit organization). For acquisitions, mortgages are insured up to 85 percent of the acquisition price plus transaction costs (90 percent of acquisition price if the borrower is a non-profit organization). Equity cash-out transactions are prohibited under this program. Section 223(a)(7) refinances of existing Section 232 loans are also reported under this risk category. New loan commitments for Sections 232/223(f) and (a)(7) surpassed $11.1 billion in fiscal year 2012 and $13.3 billion in fiscal year 2013.



Section 242 Hospitals. The Section 242 program provides mortgage insurance for loans made for the construction, renovation, and/or equipping of acute care hospitals. An FHA guarantee allows hospitals to lock in low interest rates and reduce borrowing costs for major renovation, expansion, replacement, and refinancing projects that help improve healthcare access and quality. Loans are up to 25 years in length, plus a construction period. The risk category also includes the following types of loans when made to hospitals: Section 241(a) supplemental loans; Section 223(a)(7) loans for refinancing current FHA-insured projects; and Section 223(e) loans for hospitals in older, economically declining urban areas. On February 5th, 2013, HUD published a final rule that enables HUD to offer Section 242/223(f) refinance loans. Under the standard Section 242 program, refinances are offered only for existing FHA loans, with all other loans required to be at least 20 percent new construction. New loan commitments for all Hospital programs were $889 million in fiscal year 2013, and are projected to surpass $1 billion in fiscal years 2014 and 2015. Favorable interest rates have sparked interest in refinancing the mortgage debt of hospitals in the FHA Section 242 portfolio using Section 223(a)(7) authority.

Section 223(d) Mortgage Insurance for 2-year Operating Loss Loans. Section 223(d) insures short term loans that cover operating losses during the first 2 years after a project's completion (or any other 2-year period within the first 10 years after completion) for projects with a HUD-insured first mortgage. Since 2012, HUD has offered this type of mortgage insurance only to healthcare facilities with a primary mortgage under Section 232. Mortgage insurance on this type of loan has previously been offered (though infrequently utilized) for multifamily housing, but it is no longer viewed as a cost-effective means for preventing future losses on the associated primary FHA mortgages. The program remains a valuable option for Section 232 projects, which are more likely to benefit from the early infusion of working capital and thus avoid default on the primary mortgage. Beginning in fiscal year 2013, each 223(d) loan is assigned to the risk category of the associated primary FHA mortgage.

Single Family Risk Categories

Title 1 Property Improvement. The Title I Property Improvement program insures loans for repairs and other improvements to residential and non- residential structures, as well as new construction of non-residential buildings. Property Improvement disbursements were $107 million in fiscal year 2013 and projected to be $98 million each for fiscal years 2014 and 2015. In 2011, FHA launched a "PowerSaver" pilot program that has generated new loan volume for this risk category. Operating under Title 1 authority and regulatory framework, PowerSaver provides single-family homeowners loans of up to $25,000 for proven energy improvements. Program lenders will receive incentive grants from the HUD Energy Innovation Fund to help lower the cost of loans to consumers. The program was recently extended for 2 additional years, through May 2015.

Title 1, Manufactured Housing. Under Title I, HUD provides mortgage insurance for individuals to purchase manufactured homes. In fiscal year 2013, $39 million in manufactured housing loans were endorsed, with $26 million projected for fiscal years 2014 and 2015.

3. Why is this program necessary and what will we get for the funds?

FHA's multifamily and healthcare programs are a critical component of the Department's efforts to meet the Nation's need for decent, safe and affordable housing. At a time, in particular, when there is unprecedented stress in the financial markets, FHA Multifamily programs provide the necessary liquidity so that communities can continue to provide quality affordable housing and assisted living/nursing home opportunities. Driven by low interest rates, more constrained lending in the conventional mortgage market, and improvements in HUD business operations, demand for FHA loan insurance for multifamily and healthcare programs has increased dramatically in the last 3 years. In fiscal year 2015, FHA is projected to issue loan insurance commitments providing financing for over 1,150 apartment projects with more than 182,000 units and for 850 healthcare facilities with more than 101,000 beds. We expect to see FHA volume decline over the next several years as interest rates rise and as private mortgage markets are strengthened.

The fiscal 2015 request supports mortgage insurance programs that are essential in achieving the Department's mission of strong, sustainable, inclusive communities and quality affordable homes for all. More specifically:

- At a time when credit availability is low, FHA mortgage insurance encourages private lenders to make loans for important projects that might otherwise not be possible. New workforce housing in high demand markets, innovative "green" technology renovations, nursing homes serving aging senior citizens, and critical access hospitals are among the types of projects that FHA makes possible. In fiscal year 2013, HUD endorsed a total of 2,672 multifamily and healthcare loans in GI/SRI in 50 states, the District of Columbia, Virgin Islands and Puerto Rico, covering 390,423 units of housing and healthcare facility beds.

- In addition to new development, FHA supports refinance lending that preserves financially healthy housing and healthcare projects that are endangered due to their current debt obligations. FHA's major refinancing programs for housing and nursing home facilities offer long-term amortization periods and are a critical option for many conventionally financed projects facing large balloon payments. FHA refinancing may also enable properties to undertake needed renovation and rehabilitation. New loan insurance commitments in 2013 include 2,315 refinances of existing properties that include more than 244,000 apartment homes and more than 90,700 nursing home/assisted living beds.
- FHA mortgage insurance has a strong secondary effect of creating and preserving jobs. HUD estimates that Multifamily housing loans endorsed in fiscal year 2011 are supporting 54,525 private sector jobs in construction, property management, service and administrative fields. In addition, FHA's internal forecast estimates that the 6 loans made to hospitals in fiscal year 2013 are creating an economic benefit of $1.9 billion and 3,786 jobs during the construction period alone.

Approval of the requested GI/SRI commitment limitation of $30 billion for fiscal year 2015 will allow FHA to respond to the continuing high level of need for FHA programs and contribute to the nation's economic recovery. Loan volume projections for fiscal year 2015 will be the product of several factors, including:

- Pace of recovery and re-engagement by the conventional market;
- Interest rates, which will significantly impact all product lines;
- Changes in HUD policy to improve risk position; and
- HUD capacity to process high volumes of applications.

The following table indicates projected loan commitment volumes in fiscal years 2013, 2014 and 2015 and credit subsidy rates and negative subsidy in fiscal year 2015. Credit subsidy rates represent the projected net present value cost or savings to the government of operating a loan guarantee program, and take into account projected claims, pre-payments, premium revenue, and recoveries on defaults for a cohort of loans over their lifetime.

For more information on credit subsidy calculation please see the Notes section of this justification.

Mortgage and Loan Insurance Programs-GI/SRI Account

GI/SRI PROGRAMS (IN $MILLIONS)	Commitment Actuals FY2013 [1]	Commitment Estimates FY2014	Commitment Estimates FY2015	Subsidy Rate FY2015	Negative Subsidy FY2015
Multifamily					
221(d)(4) Apartments New Construction/Sub. Rehab	$1,833	$2,044	$2,044	-3.65%	($75)
Tax Credit Projects	$1,460	$2,034	$2,096	-3.19%	($67)
223(f)/223(a)(7) Apartments Refinance/Purchase	$13,312	$10,337	$8,155	-4.69%	($382)
HFA Risksharing	$205	$280	$230	-2.67%	($6)
GSE Risksharing	$140	$138	$184	-0.89%	($2)
Other Rental (Sections 220,231,207)	$93	$121	$122	-3.39%	($4)
Multifamily Housing Subtotal	**$17,043**	**$14,954**	**$12,831**		**($536)**
Section 242 - Hospitals (includes Refinances & Supplemental Loans)	**$889**	**$1,050**	**$1,100**	-4.45%	($49)
Section 232 - Nursing Homes/Assisted Living					
Full Insurance for Health Care Facilities	$381	$521	$521	-4.23%	($22)
Health Care Refinance Facility Refinance	$5,897	$6,390	$6,390	-4.33%	($277)
Section 232 Subtotal	**$6,278**	**$6,911**	**$6,911**		**($299)**
Healthcare Housing Subtotal	**$7,167**	**$7,961**	**$8,011**		**($348)**
Title I					
Title I Property Improvements	$107	$98	$98	-2.13%	($1)
Title I Manufactured Housing	$39	$26	$26	-0.76%	($1)
Title I Subtotal	**$146**	**$124**	**$124**		**($2)**
GI/SRI TOTAL	**$24,356**	**$23,039**	**$20,966**		**($886)**
Offsetting Receipts Paid to Treasury [2]	**$914**	**$927**			**$876**

1. Total is net of commitment authority restored due to owner withdrawal prior to closing or other cancellation. Total is slightly less than $25 billion due to late year recaptures of authority.
2. Negative subsidy is obligated when the commitment for insurance is issued and disbursed subsequently at the time of initial endorsement.

Examples of Developments Using FHA Insurance

FHA's multifamily programs have encouraged the development of housing with important, positive benefits beyond just the permanent shelter of families. Many projects feature supporting energy conservation and sustainability efforts, and all new construction and rehabilitation projects stimulate job creation and preservation. Some examples:

- Turtle Creek Apartments is a 110 unit senior property located in Beverly, Massachusetts. All tenants will continue to receive Section 8 rental assistance, under a new 20 year HAP contract issued in conjunction with the new loan. The project's not-for-profit sponsor secured a $10,492,500, 223(f) loan through FHA's Low Income Housing Tax Credit Program. The preservation of this project was essential to serve the growing elderly population in the Beverly area, especially because it provides and arranges for needed resident services, and because it is located in a desirable residential neighborhood with excellent access to elderly medical and community facilities, multiple transportation options, and all necessary retail outlets.

- Villa Santa Fe consists of two separate projects in Santa Barbara CA. It is the first Rental Assistance Demonstration (RAD) closing in the Los Angeles area. The Housing Authority of the City of Santa Barbara (HACSB) combined sites to form Villa Santa Fe. HACSB receives project-based vouchers from HUD for all units. They will be rehabilitating the project with Low Income Housing Tax Credit syndication proceeds and an $18,000,000 FHA Insured Section 223(f) loan. Over $5.6 Million in renovations will occur and will be completed in October 2014.

- La Belle Vie located in Lumberton, Texas is a newly constructed, 80-unit, affordable senior community, comprised of 56 one-bedroom and 24 two-bedroom Low Income Housing Tax Credit (LIHTC) units. All the units are restricted to households earning 30%, 50%, and 60% of Area Median Income (AMI). The Borrower received a Texas Department of Housing & Community Affairs Housing Tax Credit Commitment in August 2011. The development has an affordability requirement with a 15-year compliance period as well as an additional 15-year period extended use period. The developer elected to extend the period for 10-years, which equates to a total affordability period of 40 years.

- Viera Manor, located in Viera, Florida, is OHP's 50th construction loan to welcome residents. The two-story structure features 86 Assisted Living units, and is adjacent to the VA Medical Center, an outpatient clinic which serves about 30,000 veteran visits annually.

- The town of Viera is a master planned community just outside Melbourne, on Florida's central east coast. Viera features a vibrant town center with retail shopping, restaurants, specialty food/coffee stores, and healthcare and dental services. The town also features Space Coast Stadium, a minor league baseball park that is home to the Washington Nationals spring training facility. Residents at Viera Manor have clear views of the ballpark from the second story of the facility.

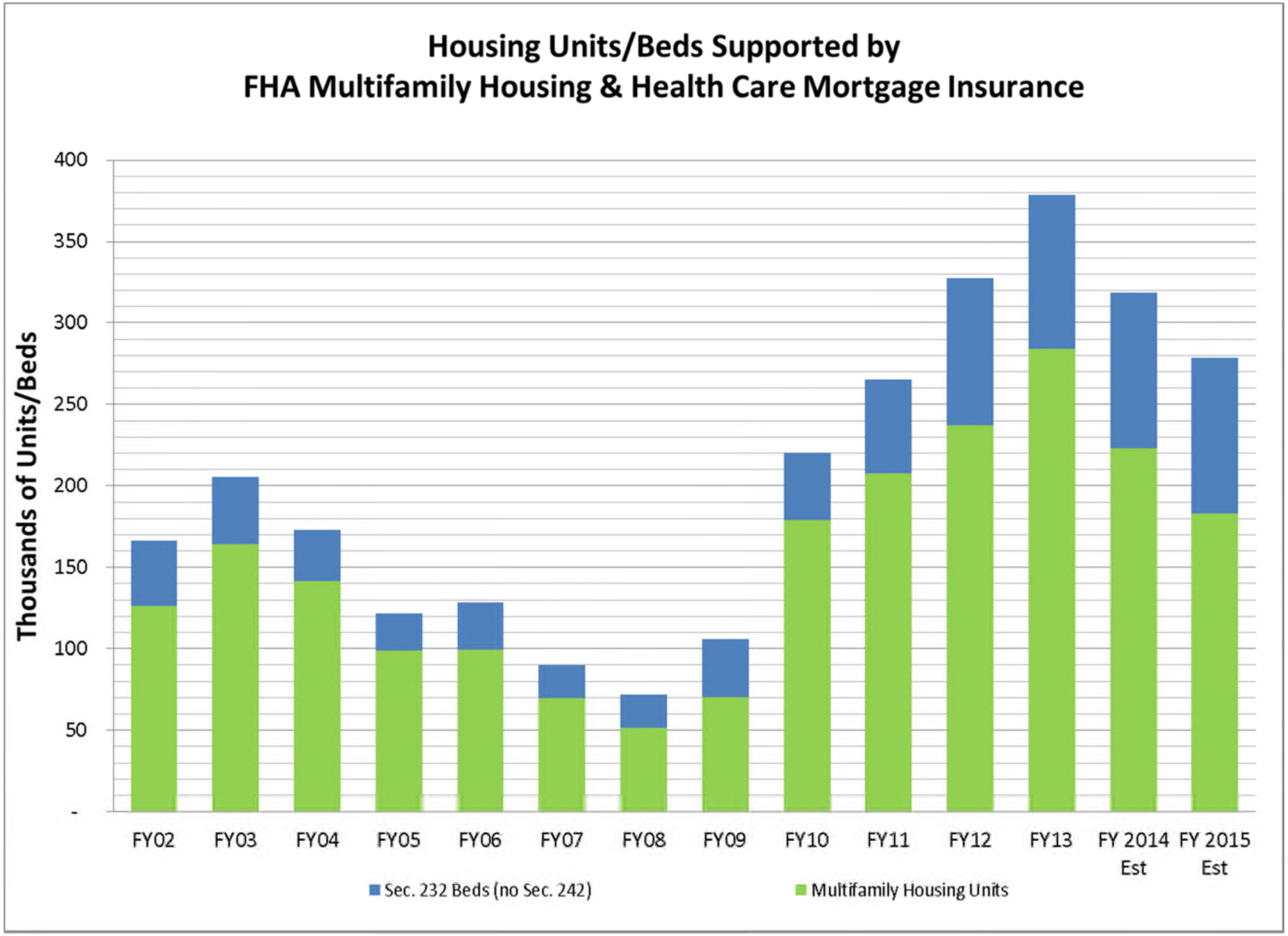
  The facility includes a full commercial kitchen, restaurant style dining area, private dining areas made available by appointment, activities rooms, and large front porch area for gatherings, indoor sitting areas, and a workout room. In addition to the dining, lounge, and activities facilities, the subject has physical therapy spaces and spa type bathing rooms for wellness and rehab usage. Other common areas include a library, gift shop, beauty shop, ice cream parlor and multi-purpose room for the residents' use. The living units feature individual temperature controls, kitchenettes and step-in/sit-down showers within full bathrooms.

- The Federal Housing Administration, through its Section 242 Hospital Mortgage Insurance Program, committed to insure a $32.0 million mortgage loan for St. John's Lutheran Hospital on August 28, 2012. St. John's Lutheran Hospital, a critical access hospital designated by the Centers for Medicare and Medicaid Services, is a not-for-profit organization operating a 25-bed acute care facility in Libby, MT. The $32.0 million loan allows St. John's Lutheran Hospital to construct a new, modernized replacement facility. The town of Libby, MT is the location of two Environmental Protection Agency Superfund Sites and as a result has a significant resident population diagnosed with asbestos related disease. The replacement facility will provide a modernized facility for the community's healthcare needs.

  By insuring the mortgage loan, FHA is enabling the hospital to obtain lower cost financing that will save an estimated $21.0 million in debt service over the life of the loan. HUD estimates that the Saint John's Lutheran construction project will support approximately 509 FTEs in the community and provide economic stimulus of $102.5 million during the construction period. Following construction, the completed project will support 43 FTEs and provide an annual economic benefit of $9.0 million.

4. How do we know this program works?

The greatest testament to FHA's effectiveness is the tangible result of its programs. Quality housing and healthcare facilities are made possible and/or more affordable throughout the country due to an FHA mortgage guarantee. For example, FHA recently approved mortgage insurance for a loan supporting the preservation of 100 units of affordable family housing at Family Tree and Lincoln Way in Lynnwood, Washington. The loan ensures the continued availability of housing for residents whose income is at or below at 30 percent, 40 percent and 60 percent of area median income. This is just one example from the over 1.3 million multifamily housing units that GI/SRI insurance has supported over the last 10 years.


Housing Units/Beds Supported by
FHA Multifamily Housing & Health Care Mortgage Insurance
Thousands of Units/Beds
400
350
300
250
200
150
100
50
-
FY02
FY03
FY04
FY05
FY06
FY07
FY08
FY09
FY10
FY11
FY12
FY13
FY 2014 Est
FY 2015 Est
Sec. 232 Beds (no Sec. 242)
Multifamily Housing Units

In addition to the direct impact of production and preservation of needed multifamily housing units and healthcare facilities, FHA projects can be significant contributors to the economic health of a community. For fiscal year 2013, there have been 24 firm commitments issued to: 16 section 232/New Construction projects, 5 section 232/241(a) projects and 3 section 223(f)/Substantial Rehabilitation project. The Office of Healthcare Programs (OHP) has estimated the economic impact of these projects based on an Economic Development Model (EDM) developed by OHP and HUD's Office of Policy, Development and Research. The results for the EDM illustrate the significant favorable economic impact that these programs are having on local communities; including a substantial impact on employment (24 projects endorsed in 2013 are estimated to create direct employment during construction for 2,493 full-time positions in 14 States).

With each mortgage it insures, FHA carefully considers the benefits to the community along with financial risks to the government. Cognizant of the increased risk associated with FHA's expanding role in the multifamily housing market, the Department has launched several new initiatives aimed at appropriately managing the risk involved with multifamily and healthcare loans. In fiscal year 2010, FHA made a number of updates to underwriting requirements for multifamily housing loans. These updated requirements are part of a broader strategy that features a national loan committee process for all large projects, new initiatives (under development) to improve lender oversight, and a revised partial payment of claim policy that will generate savings by reducing the number of full claims. FHA also adopted a more balanced approach to loan-to-value and debt service coverage requirements and increased scrutiny of borrowers' other real estate obligations that could jeopardize their financial positions and make it more difficult for them to assist projects with financial or operational challenges. FHA is taking steps such as these to ensure its policies and practices do not contribute to any unanticipated losses.

As a companion to risk management efforts, FHA increased mortgage insurance premiums (MIP) beginning October 1, 2013 for market-rate projects. MIPs for all market-rate new construction and substantial rehabilitation loans – including Section 221(d)(4), Section 220, Section 231, and Section 242 –increased by 20 basis points. MIPs for refinances made under 223(a)(7) increased by 5 basis points, with a 15-basis point increase for all other multifamily housing and healthcare loans. The increases do not apply to loans to projects with HUD rental assistance contracts, LIHTC deals, and those under FHA risk sharing programs. These modest increases ensure that the MIPs are priced appropriately to compensate for FHA's risk, consistent with current and potentially volatile market conditions. The MIP increases are also in line with programmatic requirements to align pricing with the administration's risk tolerance and address potential risk attributed to the shift in portfolio, from a primarily subsidized stock with small loans to a primarily market-rate portfolio with larger average loan sizes and the attendant risk of single point failures.

GI/SRI by the Numbers – FY 2013

Insurance in Force	**$148.9 Billion**
New Commitments	$24.4 Billion
Average Multifamily Housing Loan	$9.8 Million
Average Section 232 Loan	$10.4 Million
Average Hospital Loan	$81.5 Million
Negative Subsidy Offsetting Receipts	$913 Million
Premiums Collected	$842 Million
Claims Paid – Single-Family/HECM	$2.4 Billion
Claims Paid - Multifamily/Healthcare	$230 Million
Recoveries on Claims	$933 Million

In addition to strengthening performance in the portfolio, FHA has also taken steps to improve program administration through business process improvements. For the Section 232 program, a Lean Process has been adopted for both new construction and refinance applications. Lean Processing employs standardized work product and processes to obtain a consistent, timely result. The following are some of the specific changes implemented with Lean Processing: standardized checklists, statements of work for third party work, certifications, and templates for the lenders to use in their assembly of the application package; development of standardized punch lists for HUD staff to use in their underwriting of submitted applications; initiation of HUD legal review immediately when the Firm Application is submitted in order to cut down the time between Firm Commitment issuance and closing; and removal of portions of the application process/requirements for submittal that were duplicative or not necessary.

For the multifamily housing insurance programs, FHA has launched the "Breaking Ground" initiative that focuses on optimizing processes, strengthening risk management, developing specialized skills of the staff and strengthening the way the organization manages this workload. The Office of Multifamily Housing is employing standardization of processes to achieve consistent and timely results. It has created a standardized loan underwriting review template, adopted an early warning system, created application staging areas, and standardized work products. It has established timeframes for which staff must strive to meet regarding the review and approval/rejection of applications. In addition, it has created a dashboard which tracks and reports the number of concept meetings, applications in processing, the number of decisions made and the length of time that applications are in processing as well as how many decisions are overdue for each multifamily processing office. The dashboard is reviewed monthly by Headquarters with each office to discuss the successes and issues/challenges that the office may be facing as it meets the targeted timeframes. FHA has moved applications to various processing centers, using the existing Hub structure, in an effort to clear the backlog and balance workloads across offices. In fiscal year 2012, the total backlog in offices that completed Breaking Ground decreased by almost 75 percent. Specifically, the number of applications in processing for over 90 days dropped from 191 to 50 in just 7 months.

FHA Transformation

FHA Transformation is developing and implementing a modern financial services IT environment to better manage and reduce risk across all of FHA's Mortgage Insurance Programs. To date, FHA Transformation is in the process of delivering a new lender certification system, and has made sound progress on the Single Family Housing's systems and its new risk management tool. HUD has also made critical enterprise software and infrastructure investments for FHA that will reduce maintenance costs once the FHA Transformation initiative is completed.

FHA Transformation will allow HUD to start the careful process of migrating relevant portions of Housing's legacy applications into a modern automated financial service environment, and will help administer many aspects of the multifamily and health care insurance programs. FHA Transformation monitoring and enforcement projects will allow the Office of Lender Activities to automate many current manual processes.

FHA Transformation will also bring a new level of intelligent rules-based activities such as automated risk analysis and lender targeting according to a risk scoring framework. This will help HUD manage its credit risk prudently at the portfolio and loan level, and will enable HUD to respond rapidly to changing market conditions. The new Federal Financial Services Platform will be leveraged across several Housing programs by migrating away from the 30-year old Computerized Home Underwriting Management System (CHUMS). These FHA Transformation initiatives will enable FHA to better recognize risk and fraud trends in borrower attributes, collateral attributes, and appraisal valuation accuracy during the transaction process, and to help identify cases that may be detrimental to the MMI Fund.

The next steps for FHA Transformation will enable risk detection and fraud prevention by capturing critical data points at the front-end of the loan life cycle; and will leverage the right set of risk and fraud tools, rules-based technology, and transactional controls to minimize exposure to FHA's Insurance Funds. These IT investments will facilitate enhanced business analytics and informed decision-making by providing decision-makers with data that is higher quality and more up-to-date. This will enable FHA's leadership to analyze portfolio trends and patterns across the lending community, and will help with the identification of fraudulent lenders and reduce risk in the FHA portfolio.

FHA Transformation TI/IT initiative has created a high-level business requirements and conducted tool selection for portfolio evaluation risk & fraud capabilities (portfolio modeling and emerging trends analysis); developed both short and long term FHA master data management roadmaps and strategies; completed permanent development and user acceptance test environments for the Lender Electronic Application Portal (LEAP) current lender approval application deployment and future work within approval, recertification, monitoring, and enforcement; completed permanent integration test and production environments for LEAP for current lender approval application deployment and future work within lender approval, recertification, monitoring, and enforcement; successfully entered LEAP into production, including the automation of lender application and approval process, lender submission of application, Office of Lender Activities workflow, status tracking, automatic notifications, application assignment to FHA staff for review, and interface with third party Dun & Bradstreet for lender profile information and verification; and procured licenses for Portfolio Evaluation Tool to begin execution of pilot deployment tasks.

5. Legislative/Regulatory Proposals

1. ***MAHRA Extension of Sunset Date (Sec. 240):*** This provision extends the sunset date of the Multifamily Assisted Housing Reform and Affordability Act (MAHRA) of 1997 to October 1, 2018 (expires in 2015).

2. ***Eligibility for FHA-insured Properties (Section 241):*** Clarifies that low-and-moderate income persons under 62 years of age are eligible for occupancy of dwelling units in a project financed with a mortgage insured under 221(d)(4), similar to those with a mortgage insured under 221(d)(3).

3. ***Loan Assignment Authority (Sec. 242):*** Eliminates Section 221(g)(4) of the National Housing Act regarding loan assignment authority. The provision is no longer necessary because there are no longer any outstanding loans remaining in the portfolio that would qualify under this provision.

6. Notes to Justification

GI/SRI Single Family Portfolio

In addition to new insurance commitments for the multifamily, healthcare and Title 1 programs, the GI/SRI fund also houses activity on mortgage insurance and HUD-held notes for a number of large single family programs. Prior to fiscal year 2009, the GI/SRI Fund housed new insurance for a number of significant single family insurance programs, such as the Home Equity Conversion Mortgage (HECM) reverse mortgage guarantees and condominium unit financing. With the enactment of the Housing and Economic Recovery Act of 2008 (HERA), financial responsibility for almost all single family programs was transferred to the Mutual Mortgage Insurance (MMI) Fund. However, obligations made prior to 2009 (and the associated cash flows) remain in GI/SRI.

Credit Subsidy Calculations and the Annual Re-estimate

Credit subsidy rates represent the projected net cost or savings to the government of operating a loan guarantee program, and take into account the present value of projected claims, pre-payments, premium revenue, and recoveries on defaults for a cohort of loans over their lifetime. In accordance with the Credit Reform Act of 1990, administrative costs (excluding property disposition) are not included in credit subsidy calculations. FHA credit subsidy rates reflect historic performance data for similar loans made over the past 40 years, with adjustments made for significant policy shifts as well as changing economic and market conditions. The Department devotes significant efforts to updating and continuously refining the credit subsidy estimates. Each year the extensive statistical base from which projections of future loan performance are calculated is updated with an additional year of actual data. The Department and OMB continue to examine the data, assumptions, and calculations that are used to estimate loan program cash flows and subsidy rates in order to eliminate errors and improve the accuracy and reliability of projections.

Each year, FHA completes a required re-estimate of liabilities and subsidy costs associated with the existing insurance portfolio. Revised liability estimates take into account another year of actual performance and the latest economic assumptions. Vacancy rates, Treasury interest rates, individual property's past financial performance, and house price appreciation are among the key variables that shape GI/SRI's projected cash flows. Multivariate statistical models generate the claim and prepayment rates that drive calculations of the Fund's financial worth. To determine the re-estimate, the revised liabilities (net of projected loan default recoveries) are compared to the current assets on hand. When assets exceed projected liabilities, a downward re-estimate occurs with the difference being transferred to the Treasury general fund as mandatory receipts. When projected liabilities exceed assets, an upward re-estimate occurs and the fund receives a mandatory appropriation to bring assets and liabilities into balance. For example, if the portfolio of loans made in a given year has a net liability of $250 million and cash on hand of $300 million, then the cohort would require a downward re-estimate in which $50 million would be paid from the Fund's Financing account (which handles all loan guarantee cash flows) to the Treasury. If the financial position was reversed – if a cohort had assets of $250 million and a net liability of $300 million – then a $50 million mandatory appropriation would be recorded in the GI/SRI Program Account to cover the cost of the upward re-estimate. Those funds would then be forwarded to the Financing Account to ensure it contained sufficient resources to cover the anticipated lifetime liabilities of the portfolio.

Re-estimates are calculated each year for each cohort of loans. Fourteen GI/SRI cohorts have net lifetime downward re-estimates, meaning costs to the government for that group of loans are now projected to be less than the original subsidy calculation. Nine cohorts have a lifetime upward re-estimate, meaning the original subsidy calculation is now believed to have underestimated costs.

Mortgage and Loan Insurance Programs-GI/SRI Account

While GI/SRI's newer books of business consist primarily of multifamily and healthcare loans, it is important to keep in mind that GI/SRI re-estimates for all cohorts prior to 2009 also include assets and liabilities for a large portfolio of single family loans (programs subsequently transferred to MMI).

HOUSING
GENERAL AND SPECIAL RISK INSURANCE FUND
SUMMARY OF RESOURCES BY PROGRAM
(Dollars in Thousands)

Budget Activity	2013 Budget Authority	2012 Carryover Into 2013	2013 Total Resources	2013 Obligations	2014 Budget Authority/ Request	2013 Carryover Into 2014	2014 Total Resources	2015 Request
Positive Subsidy								
Appropriation	...	$16,403	$16,403	...	...	$16,403	$16,403	...
Total	...	16,403	16,403	...	...	16,403	16,403	...

HOUSING
GENERAL AND SPECIAL RISK INSURANCE FUND
Appropriations Language

The fiscal year 2015 President's Budget includes proposed changes in the appropriation language listed and explained below. New language is italicized and underlined, and language proposed for deletion is bracketed.

New commitments to guarantee loans insured under the General and Special Risk Insurance Funds, as authorized by sections 238 and 519 of the National Housing Act (12 U.S.C. 1715z-3 and 1735c), shall not exceed $30,000,000,000 in total loan principal, any part of which is to be guaranteed, to remain available until September 30, [2015] <u>*2016*</u>: *Provided,* That during fiscal year [2014]<u>*2015*</u>, gross obligations for the principal amount of direct loans, as authorized by sections 204(g), 207(l), 238, and 519(a) of the National Housing Act, shall not exceed $20,000,000, which shall be for loans to nonprofit and governmental entities in connection with the sale of single family real properties owned by the Secretary and formerly insured under such Act. *(Department of Housing and Urban Development Appropriations Act, 2014.)*