U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

ANNUAL REPORT TO CONGRESS
FISCAL YEAR 2012 FINANCIAL STATUS
FHA MUTUAL MORTGAGE INSURANCE FUND

NOVEMBER 16, 2012

Your Door to FHA HOMEOWNERSHIP

Annual Report to Congress Regarding the Financial Status of the FHA Mutual Mortgage Insurance Fund Fiscal Year 2012

U.S. Department of Housing and Urban Development
November 16, 2012

Secretary's Foreword

This year's report to Congress on the financial status of the FHA Mutual Mortgage Insurance (MMI) Fund, my fourth as Secretary, arrives at an important moment for our housing market. As 2012 draws to a close, Americans are starting to feel a sense of hope for the first time in half a decade – with the number of families falling into foreclosure at half what it was in 2009, housing construction activity stronger than at any time since 2008, the best year for home sales since the financial crisis began, and rising home values that have already restored positive home equity for 1.3 million families affected by our greatest economic challenge since the Great Depression. Our national housing market now has a momentum not seen in six years – and much of this progress has only been possible because of the FHA, which has provided access to homeownership for millions of American families. Without FHA's continuous presence in every State, and throughout every month of the ongoing crisis, housing market and economic conditions would have been much worse, and the road to recovery more difficult.

Yet, as the findings of the new independent actuarial study remind us, the job of re-stabilizing our national housing market is not finished. According to those findings, the capital reserve ratio of the MMI Fund, which contains FHA's single family mortgage insurance programs, has fallen below zero, to *negative* 1.44 percent. Loans insured prior to 2010 continue to be the prime source of stress on the Fund, with fully $70 billion in future claim payments attributable to the 2007-2009 books of business alone. As was the case last year, the independent actuary attests to value of the many reforms put in place over the past four years in its assessment of the high quality and profitability of loans insured since 2010.

There are three fundamental factors driving the decline in the capital reserve ratio this year. First, while FHA continues to have the most profitable new books of business in its history, the house price appreciation estimates used for this actuarial study are significantly lower than those used last year. This accounts for an estimated $10.5 billion in reduced value compared to the actuary's projection last year of what the Fund's economic value would be at the end of FY 2012. In addition, the house price assumptions used by the independent actuary do not include improvements to home prices observed since June, and the estimates of near-term movements in house prices are depressed by a high level of refinance activity in the particular index series used.

Second, the continued decline in interest rates, while good for the overall economy, is costly to FHA. There are two effects on FHA, both negative. First, premium revenues from the existing portfolio go down when more borrowers pay-off their mortgages to refinance into lower rates. The capital ratio calculation does not include any return of those borrowers into new FHA-insured loans. Second, the actuarial projections include higher claim expenses when interest rates stay low as borrowers with higher mortgage rates that are unable to refinance become more willing to default. These effects of continued low interest rates result in a reduction of $8 billion in estimated economic value for the Fund, versus what was anticipated in last year's report.

Third, based on recommendations made by the GAO, HUD's Inspector General and others, the actuary changed the way it reflects losses from defaulted loans and reverse mortgages in the economic value of the MMI Fund. This resulted in an estimated $10 billion in reduced economic value compared to last year's projections.

The results of the independent actuarial study are intended to inform policy. They do not directly affect the adequacy of capital balances in the MMI fund, nor do they directly imply the need for any assistance from the U.S. Treasury. The adequacy of the capital balance in the Fund and the need to draw on Treasury funds will be determined by the MMI Fund portfolio valuation that is part of the President's Budget for FY 2014. That Budget will be released in February.

At the same time, we take the report of the independent actuaries very seriously. That is why we are announcing a series of further changes designed to strengthen the MMI Fund. These measures will directly address the source of the financial strain—losses stemming from legacy books of business—and reverse a policy change made in 2001 that has led to significantly reduced premium income for each successive book of business. In addition, we will enact a modest increase to FHA's premiums, which will add significant revenue to the Fund and ensure that FHA does not take on additional market share, while at the same time being modest enough that it doesn't threaten our emerging housing recovery.

Coupled with the $11 billion in additional capital from expected new insurance guarantee volumes in FY 2013, we believe it is possible to return the MMI Fund capital ratio to a positive level within the year, and reduce the likelihood that FHA will need to call upon the Treasury for any special assistance this fiscal year.

While we are continuing to take aggressive measures to protect the MMI Fund using existing authorities, we need help from the Congress to take all of the steps required to fully protect Fund finances. That is why we're calling on Congress to act on a set of legislative proposals designed to place FHA in a stronger fiscal position over the next twelve months and into the future. These steps include:

- Additional authority to ensure that FHA borrowers are receiving the level of delinquency assistance they deserve from their servicer,
- Stronger and more flexible enforcement authorities so that FHA can identify non-compliance and poor performance and take action to avoid losses, and
- Additional authority to manage the reverse mortgage (HECM) program so that consumers are better protected and able to retain their homes.

Several of the proposals we are pursuing have already been passed by the House of Representatives, and we look forward to continuing to work with both chambers to enact final legislation to provide FHA with the tools it needs to build on the vital reforms already implemented by this Administration.

Finally, in accordance with FHA's continual analyses of its portfolio to identify and mitigate risks, and to provide enhancements that benefit both consumers and the Fund, FHA is also developing additional proposals which will further assist in strengthening the MMI Fund. Our aggressive but balanced approach will allow FHA to continue its historic role of providing access to homeownership for underserved communities, support the housing market recovery, and ensure that the federal government's footprint in the marketplace recedes as private capital returns.

Shaun Donovan
Secretary
U.S. Department of Housing and Urban Development

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Since the beginning of the recession, FHA has played a key role in helping to facilitate the housing market's recovery. Throughout its history, FHA has supported access to affordable, sustainable homeownership opportunities for people with limited wealth or who are otherwise underserved by the conventional market. It has also acted as a stabilizing force in the housing market during times of economic distress. At no time has this countercyclical influence been more pronounced than during the recent housing crisis. In the face of ongoing challenges, FHA has continued to provide access to mortgage finance opportunities during a period of severe constriction in conventional markets. As a result, FHA has played a central role in bringing the housing market from the brink of collapse to a place where it is positive and growing again.

FHA Endorsement Activity in Fiscal Year 2012

FHA insured nearly 1.2 million single-family forward mortgage loans during the year, with a total dollar value of approximately $213 billion. Since its inception, FHA has now insured more than 40 million single-family mortgages. Of the over 700,000 thousand home-purchase mortgages endorsed during the year, 78 percent were for first-time homebuyers, reaffirming FHA's role in providing access to new entrants to the home ownership market. Indeed, over the past four fiscal years, FHA has made homeownership possible for over 2.8 million first-time buyers.

And FHA has also continued to be a vital source of home financing for minority borrowers. While FHA insurance was used for approximately 27 percent of all home purchase mortgages in 2011, FHA accounted for 50 percent of home purchase mortgages for African American borrowers and 49 percent for Hispanic/Latino borrowers.

Although FHA continues to be an important source of access to credit for American families, its market share continues to decrease as the economy recovers and private capital begins to return to the market. New insurance endorsement activity in FY 2012 fell once again from that of the prior year, continuing its decline from the peak levels seen in FY 2009. In terms of dollars of single-family loans insured, 2012 is the lowest volume since the start of the crisis. Home Equity Conversion Mortgage (HECM) insurance endorsements in FY 2012 were also down by 25 percent from FY 2011 levels, to 54,591 loans. FY 2012 marks the third consecutive year in which HECM volume declined, as the combined effects of policy revisions to the product and changes within the industry have reduced participation in the program.

FHA-insured loans continued to exhibit strong performance in FY 2012, with each successive book since 2010 projected by the actuary to be more profitable than the year before, and for the books insured between 2010-2012, collectively, to dramatically outperform those books insured in 2009 and before. Insurance claims on earlier books – particularly those endorsed between 2007-2009 – are expected to cost FHA more than $70 billion. In addition, seller-funded downpayment loans continue to place significant stress on the MMI Fund. These loans account for only 4 percent of the outstanding portfolio but 13 percent of all seriously delinquent loans. Over the life of the loans, seller-funded downpayment loans are expected to cost the FHA MMI fund over $15 billion.

Contrary to the books of business insured prior to the start of this Administration, those endorsed since 2010 continue to exhibit very strong performance. By every measure – credit quality, premium revenue, early period delinquency, claims, etc. – the quality of loans insured from 2010 onward is the best in FHA's history.

The Financial Status of the MMI Fund

This fiscal year, the Mutual Mortgage Insurance Fund (MMI Fund or Fund) capital reserve ratio fell below zero to *negative* 1.44 percent. While this one-time valuation of the economic net worth of FHA's portfolio is obviously of concern, it does not mean that FHA will have to draw from the Treasury. Any required draw would be determined not by the economic assumptions of this review but those used in the President's budget to be released in February. In addition, analysis of the economic value of the fund does not take into consideration revenues generated after FY2012, estimated by the actuaries to be $11 billion through the end of FY2013. Final accounting is not performed until the end of FY 2013.

There are three factors driving the change in the estimated economic value of the MMI Fund compared to last year:

- First, the Moody's July 2012 house price appreciation forecast, which was used in this year's actuarial study, predicted significantly lower levels of appreciation in the near term than the forecast used in last year's actuarial study. This results in a cumulative difference in projected house price appreciation of 8 percentage points over the first five years. Thus, this downward revision in house price forecasts from last year to this year accounted for an estimated $10.5 billion in reduced economic value compared to the actuary's 2011 projection of what the Fund's economic value would be as of the end of FY 2012. Further, near-term house-price movements in the index used by the actuaries were depressed by high levels of refinance activity in 2012, and therefore, they do not reflect improvements seen this year to home prices in other measures of housing market strength. Additionally, because the forecast utilized was from July and covers the period through June 2012, it does not include substantial improvements to home prices seen since that time.
- Second, the continued decline in interest rates since last year, while good for the overall economy, causes a substantial loss of revenue. The reasons for this are two-fold. First, because of the higher interest rates being paid by borrowers on loans made before 2009, the actuary projects that these borrowers will default at marginally higher rates than would otherwise be expected. Second, the actuary projects that FHA loans would be paid off earlier than expected through refinances, and in accordance with statutory requirements, the methodology the actuary uses assumes that none of these loans will refinance back into FHA. The effect of these two assumptions by the actuaries resulting from a prolonged period of low interest rates is a reduction of $8 billion in estimated economic value for the Fund from what was anticipated in last year's report.
- Third, based on recommendations made by the GAO, HUD's Inspector General and others, FHA directed the actuary to employ a refined methodology this year to adjust the way losses from defaulted loans and reverse mortgages are reflected in the economic value of the MMI Fund, resulting in an estimated $10 billion in reduced economic value compared to last year's projections.

Actions Taken to Strengthen the Fund

In response to this actuarial review, HUD is announcing a series of changes designed to build on previous steps that have improved the health of the Fund. Throughout this Administration, when FHA's health has faced challenges, we have taken action to protect the Fund. Indeed, the steps we have taken to date are estimated to have improved the health of the Fund by more than $20 billion. Therefore, FHA is continuing to take additional actions designed to add billions more to the Fund over the coming years.

The measures FHA will take emphasize maximizing recoveries on FHA's legacy loans which are responsible for significant stress on the Fund. Focusing our efforts first and foremost on improved outcomes for legacy books of business is important because not only is that where the current stress on the portfolio is coming from, but finding better solutions to deal with those loans will also provide assistance to distressed borrowers as the economic recovery continues.

First, with $70 billion in FHA losses attributable to loans insured from 2007-2009, FHA will take additional steps to minimize losses incurred as borrowers go into foreclosure. Foreclosures are expensive, for families, communities and the MMI Fund. By reducing the likelihood that a loan ends in foreclosure and, in turn, becomes an FHA real estate owned (REO) property, costs to the Fund are decreased. The measures FHA will take include the following:

- Building on the success of FHA's Distressed Asset Stabilization Program, we will continue to sell expanded pools of defaulted mortgages headed for foreclosure, providing the opportunity for the purchaser and borrower to avoid a costly foreclosure while reducing costs to the Fund. The FHA is committing to sell at least 10,000 distressed loans per quarter over the next year.
- We are also targeting deeper levels of payment relief for struggling borrowers by revising our loss mitigation program. The changes being made will more quickly and effectively assist distressed borrowers in finding solutions to keep their homes and meet their obligations.
- Additionally, we are expanding the use of short-sales to provide more families the opportunity to avoid foreclosure. As we have said repeatedly over the last four years, foreclosures are expensive, for families, communities and the Fund. By reducing the likelihood that a family will be foreclosed upon, we reduce costs for the Fund.
- Finally, building upon changes we have already made to streamline our asset management policies and procedures, we are expanding initiatives that increase efficiency and decrease losses associated with the sale of foreclosed properties.

Second, on new loans, we will reverse a policy change made in a prior Administration that eliminated the requirement for borrowers to pay premiums after their loan reached 78 percent of its original value. As a result, FHA has been left without premiums to cover losses on loans held beyond the period for which we are collecting premiums.

We will also enact a modest increase to the annual insurance premium paid by borrowers on an FHA loan. This premium increase – $13 per month for the average FHA borrower – which FHA will enact in 2013, will add significant revenue to the Fund and ensure that FHA does not take on additional market share, while at the same time being modest enough that it doesn't impact borrower access to credit or threaten our emerging housing recovery.

Finally, in accordance with FHA's continual analyses of its portfolio to identify and mitigate risks, and to provide enhancements that benefit both consumers and the Fund, FHA is also developing additional proposals which will further assist in strengthening the MMI Fund. More details will be provided when these policies are announced in the coming months.

Coupled with the $11 billion in additional revenue FHA is expected to earn from new business in FY 2013, the steps we will take are designed to return FHA's capital reserves to a positive position within the year and reduce the likelihood that FHA would need to use its authority to draw funds from the Treasury next September. This balanced approach to strengthening FHA and providing much needed stability during the recovery of the housing market sets the stage for a stronger FHA and an improved economy, while continuing to take steps to reduce government's footprint in the marketplace.

Stepping into the breach during the worst recession since the Great Depression obviously increased FHA's risk, and we have not been immune to the effects of the housing and economic crisis. However, the reforms we have made – the most sweeping in the nearly eighty-year history of FHA – as well as those we will continue to make moving forward, have altered the long term trajectory of the MMI Fund. So while stresses and difficulties remain in the near term, we are committed to ensuring that FHA is strong, stable, and viable for many years to come.

II. Introduction

This report provides information regarding the status and activity of the Mutual Mortgage Insurance Fund (MMI Fund or Fund) of the Federal Housing Administration (FHA). That Fund is a system of accounts used to manage the single-family mortgage insurance programs of FHA, which itself is a wholly-owned government agency housed in the U. S. Department of Housing and Urban Development (HUD). FHA provides guarantees on mortgage loans issued by private lenders, enabling those lenders to provide credit to borrowers who might otherwise be unable to access the capital markets to purchase or refinance a property. The various FHA portfolios include mortgages on single-family residential properties, apartments, hospitals, assisted-living facilities, and nursing homes. As an agency, the FHA oversees an insurance portfolio of over $1.3 trillion, of which the MMI Fund programs account for approximately $1.1 trillion. MMI Fund programs represent a commitment by the Federal government to support economic activity and correct market failures in the housing sector.

The FHA story is one of effective federal government involvement in assuring credit flows into housing markets throughout the country at very critical periods in our nation's history. Since its inception in 1934, FHA has provided access to homeownership for credit worthy lower wealth or otherwise underserved borrowers, enabling more than 40 million families who may otherwise have been prevented from doing so to realize the American dream of homeownership. The MMI Fund was designed to be self-sustaining, but as is true of all government loan and loan guarantee programs, FHA's insurance is backed by the full faith and credit of the United States Government and the MMI Fund possesses permanent and indefinite budget authority by which it may draw on assistance from the U.S. Treasury as needed to address unanticipated stresses. Self-sufficiency faced a critical test in the 1980s as severe rolling regional recessions nearly depleted the MMI Fund reserve account. Because of this extremely difficult period, although it still had cash reserves, in both 1990 and in 1991, FHA was estimated to have a negative economic value. So while FHA has never required additional financial support, it has experienced periods during which the estimated economic value of its insurance portfolio was negative. Today, although there have been improvements in housing markets that suggest the United States is emerging from its national housing recession, the impact of a fragile housing market and a weak economy continue to severely impact the MMI Fund capital reserve account. This administration has been aggressive in protecting the MMI Fund and taking action to strengthen it. Section V outlines additional measures we will implement this year to further strengthen the Fund while continuing to support the ongoing economic recovery.

The following chapter of the Annual Report describes characteristics of the loans that FHA endorsed in fiscal year 2012, as well as those loans insured in previous years that were outstanding at the end of the fiscal year. The conclusion from this chapter is twofold: first, as it always has been, FHA continues to be a critical source of financing for underserved communities and first-time homebuyers; second, recent books of business are much better from a risk standpoint than past books of business and the FHA mortgages outstanding will be increasingly weighted toward these better books of business as time progresses, resulting in significant improvements in the overall health of FHA's insured single-family loan portfolio over time.

III. Composition and Performance of FHA Mortgages

A. NEW ENDORSEMENT AND PORTFOLIO CHARACTERISTICS

New insurance endorsement activity in FY 2012 fell once again from that of the prior year, continuing its decline from the peak levels seen in FY 2009 (see Exhibit II-1). In terms of dollars of single-family loans insured, 2012 is the lowest volume since the start of the crisis and volume has fallen each year since 2009. FHA home purchase activity was down in FY 2012 by approximately 6 percent. The FHA share of total home sales remained at approximately 15 percent, which is the same level as 2011. Overall endorsement levels did not decrease significantly in FY 2012 because of the 52 percent increase in streamline refinance mortgages. In the last quarter of the fiscal year, there were 104,840 streamline refinances alone, due in part to today's historically low interest rates, but even more so to the premium decrease enacted for these loans in June.

Exhibit III -1
FHA Single-Family Mortgage Insurance Endorsements[a]

Fiscal Year	Counts by Loan Purpose: Home Purchase	FHA Streamline Refinance	Other FHA Refinance	Conventional-to-FHA Refinance	All Loans	Dollar Volume (bil)
2000	839,869	34,443	6,780	32,007	913,099	$94.22
2001	806,818	188,422	17,230	46,207	1,058,677	117.69
2002	862,898	318,245	28,525	64,474	1,274,142	148.10
2003	658,640	560,891	37,504	62,694	1,319,729	159.24
2004	586,110	291,483	26,146	56,696	960,435	115.98
2005	353,844	113,062	11,840	33,581	512,327	62.36
2006	313,998	36,374	14,722	60,397	425,491	55.30
2007	278,394	22,087	16,504	107,739	424,724	59.84
2008	631,655	66,772	28,508	360,457	1,087,392	181.17
2009	995,551	329,437	38,069	468,942	1,831,999	330.48
2010	1,109,581	212,893	39,591	305,544	1,667,609	297.60
2011	777,427	180,269	44,557	195,562	1,197,815	217.81
2012	733,864	274,066	47,578	129,233	1,184,741	213.30
2011Q1	196,801	93,198	16,252	65,317	371,568	72.12
2011Q2	168,775	45,766	12,939	58,571	286,051	52.82
2011Q3	201,156	22,837	8,055	41,253	273,301	47.31
2011Q4	210,695	18,468	7,311	30,421	266,895	45.56
2012Q1	176,167	36,656	11,229	31,850	255,902	44.63
2012Q2	166,169	62,180	13,373	36,617	278,339	49.98
2012Q3	193,557	70,390	14,035	38,080	316,062	57.82
2012Q4	197,971	104,840	8,941	22,686	334,438	60.87

[a]This table includes all single-family endorsements. There are a small number of loans today that are not obligations of the MMI Fund. For providing a complete picture of the FHA single-family activity, those are included here. Prior to FY 2009, two measurable programs were not obligations of the MMI Fund. Those are the 203(k) purchase-and-rehabilitation program, and the 234(c) condominium insurance program. Again, they are included here to provide a complete picture of FHA activity.
Source: U.S. Department of HUD/FHA.

1. Market Share

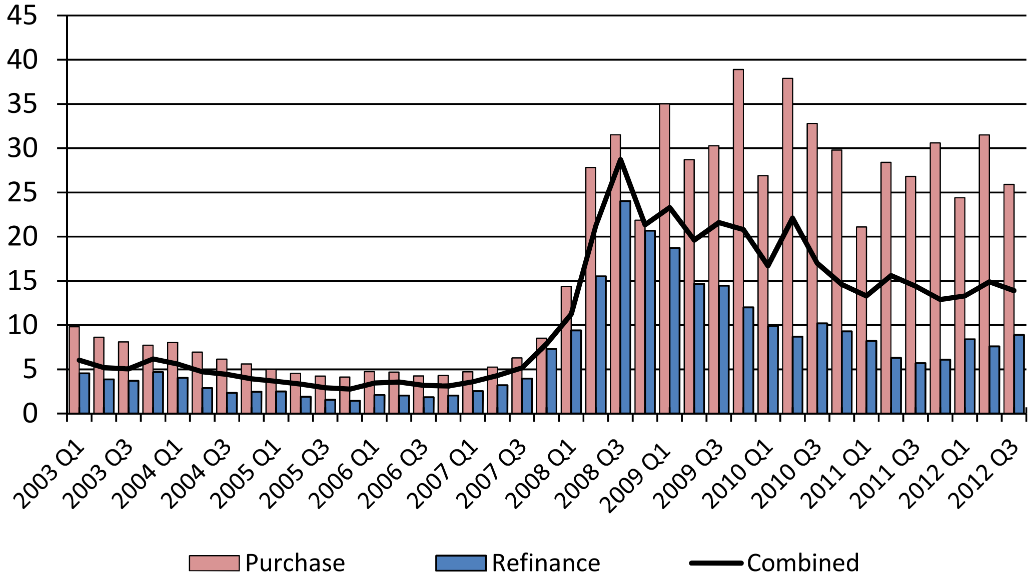
FHA has played a vital role in ensuring access to credit for borrowers and liquidity in the market. The increase in FHA's home purchase market share starting in 2008 is due to three principal factors: the tightening of private credit, FHA keeping its underwriting standards fairly constant, and the temporary increases in FHA's loan limits enacted by Congress. In 2006, FHA was authorized to insure loans of up to $200,160 in all markets and up to $363,790 in high cost markets. In 2008, the Emergency Economic Stabilization Act (EESA) and later the Housing and Economic Recovery Act (HERA) granted FHA temporary authorization to insure mortgage loans of up to $271,050 in all markets and up to $729,750 in high cost areas. The result was that during fiscal year 2006 as the crisis was about to begin, FHA insured 314,000 home purchase loans, but by fiscal year 2009 it had increased its volume of home purchase loans to 996,000 during a year in which the overall home purchase market was considerably smaller.

FHA also provided support for the refinance segment of the housing market during the crisis. Beginning in 2007, FHA stepped in to enable growing numbers of homeowners facing large interest rate resets from expiring teaser rates on conventional ARMs to avoid large payment shocks. These conventional-to-FHA "product refinances" helped hundreds of thousands of borrowers who met FHA's standard underwriting criteria to convert conventional mortgages facing (or which already had received) monthly payment increases into far more sustainable FHA loans. In addition to providing help to homeowners with unsustainable conventional loans, FHA also enabled borrowers with existing FHA loans to refinance through its streamlined FHA-to-FHA refinance programs. The assumption underlying a streamline refinance is that FHA, which already holds the default risk on the loan, would not be taking on new risk if it insured a rate or term refinance of the loan (with no cash out other than to cover closing costs), even if the loan were underwater, or if the borrower's credit history had deteriorated.

Despite FHA's importance in providing liquidity and stability to the market throughout the housing crisis, its current role is outsized and should and will decrease. Indeed, FHA's market share has declined yearly since it peaked in 2009. Credit and pricing policies that FHA, has made and will continue to refine, will further facilitate the return of private capital sources in the market while simultaneously strengthening FHA's own capital position – without limiting access to credit for qualified borrowers. Although market share is considerably higher than 2003, when FHA's market share was more representative of historical averages, overall loan volume is now at comparable levels to that seen in 2003.

Exhibit III-2 is shown below to illustrate FHA's response to the crisis in terms of market shares by loan type (purchase or refinance).

Exhibit III-2
FHA As a Percent Of Mortgage Originations By Type

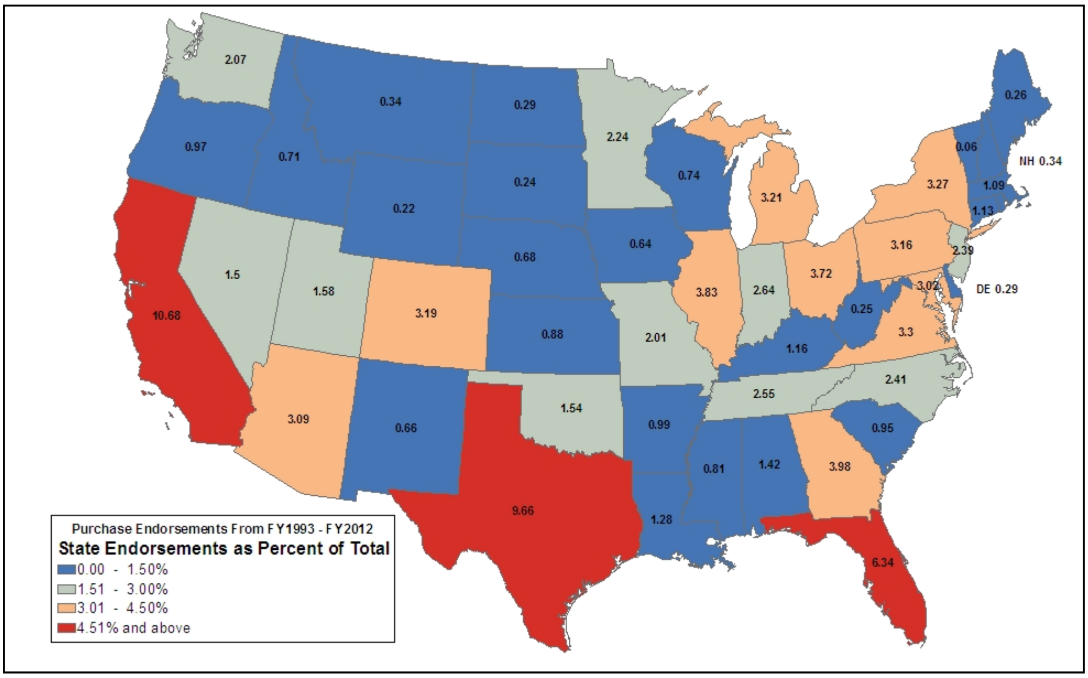


Sources: MBA and HUD.

2. Geographic Concentration

Exhibit III-3 depicts the percentage of FHA home purchase endorsements by state for fiscal years 1993 through 2012. Twenty-seven percent of all FHA home purchase endorsements since 1993 have been in California, Texas, and Florida.

Exhibit III-3
State Share of FHA Home Purchase Endorsements



Source: U.S. Department of HUD/FHA.

Exhibit III-4 highlights FHA home purchase mortgage activity over time in the top ten states for endorsements for 1993 through 2012 and the FHA share of the market in each state. The second panel of Exhibit III-4 illustrates how FHA business patterns across states changed between 2001 and 2006, and then again between 2006 and 2012. For example, California, on average, accounts for approximately 11 percent of all FHA home purchase endorsements. However, California's share of endorsements declined to less than 1 percent by 2006. It has since increased to an average of 13 percent over the last 3 fiscal years. The shift in geographic concentration reveals FHA's continued importance in addressing regional market conditions, particularly in periods of economic stress and constrained liquidity.

Exhibit III-4
FHA Home Purchase Mortgage Shares and Endorsement Shares for Top-Ten States for FHA Activity[a]

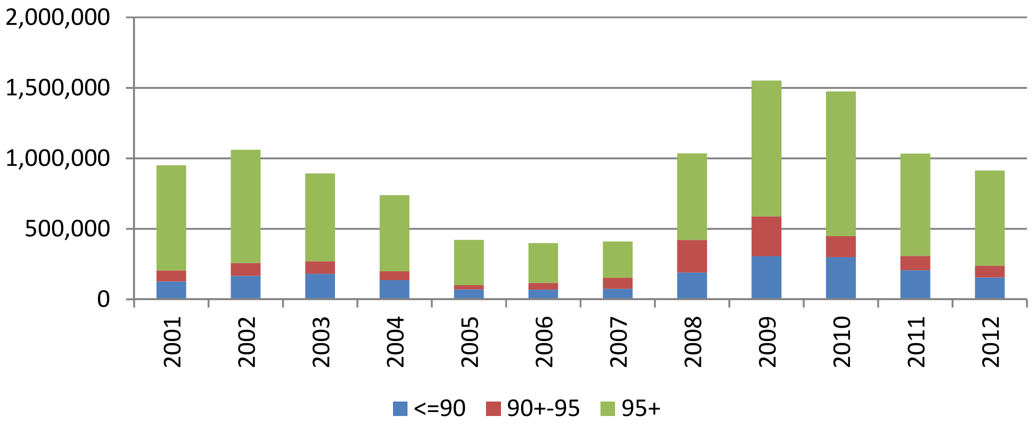
State	Mortgage Market Shares Within States					Endorsement Shares Across States					
	1993-2012	2001	2006	2010	2011	1993-2012	2001	2006	2010	2011	2012
US	14.6%	16.0%	5.0%	32.7%	27.1%						
CA	13.6	13.6	0.5	36.0	31.8	10.7%	11.1%	0.8%	11.9%	13.7%	13.4%
TX	18.7	19.2	9.1	35.1	29.1	9.7	9.5	15.9	9.5	9.1	10.1
FL	11.4	12.9	2.3	37.2	30.7	6.3	6.8	3.9	6.2	6.7	6.4
IL	13.6	14.6	5.8	33.1	27.6	4.0	4.3	5.9	3.5	3.5	3.7
GA	16.0	19.0	2.1	40.0	32.2	3.8	3.8	3.1	3.3	3.2	3.2
OH	15.2	17.5	8.0	35.7	28.4	3.7	3.7	5.3	3.8	3.4	3.5
MD	17.0	19.6	7.5	38.9	32.6	3.3	3.7	2.1	3.0	3.0	2.8
CO	12.4	13.1	5.2	26.7	24.9	3.3	3.2	3.3	3.4	3.6	3.6
VA	13.3	15.0	3.7	29.2	25.3	3.2	3.1	3.4	3.0	3.2	3.2
AZ	15.9	17.9	3.4	31.7	25.6	3.2	3.4	2.9	2.5	2.4	2.5

[a]All data is based on loan counts.
Source: Home Mortgage Disclosure Act (HMDA) data; analysis by the U.S. Department of HUD/FHA.

3. Loan-to-Value Ratio

Exhibit III-5 shows the distribution of FHA endorsements by loan-to-value (LTV) ratio. Due to the significant utilization of FHA-insured loans by first time homebuyers and lower wealth borrowers, the majority of FHA endorsements have historically had LTV ratios above 95 percent. Exhibit III-5 displays average LTV ratios since 2001, showing the continual importance of FHA to families with limited wealth.

Exhibit III-5
Distribution of FHA Endorsements
by Loan-to-Value Ratio



Source: U.S. Department of HUD/FHA.

4. Credit Quality

The average credit score of FHA borrowers declined slightly from 701 in FY 2011 to 698 for FY 2012. A three-year rise in average credit scores for new FHA-insured borrowers peaked in the second quarter of the fiscal year, at an average credit score of 704. During the second quarter of 2012, nearly 34 percent of borrowers had scores at or above 720 compared to less than 10 percent during the second quarter of 2008, as shown in Exhibit III-6. The average credit score for purchase loans was 700 in FY 2012 compared to 696 in FY 2011. Even with the recent decline from the peak it should be noted that credit scores as a whole for FHA are still at historically high levels.

Exhibit III-6
Distribution of FHA Borrower Credit Scores by Fiscal Year and Quarter[a]
(rows add to 100%)

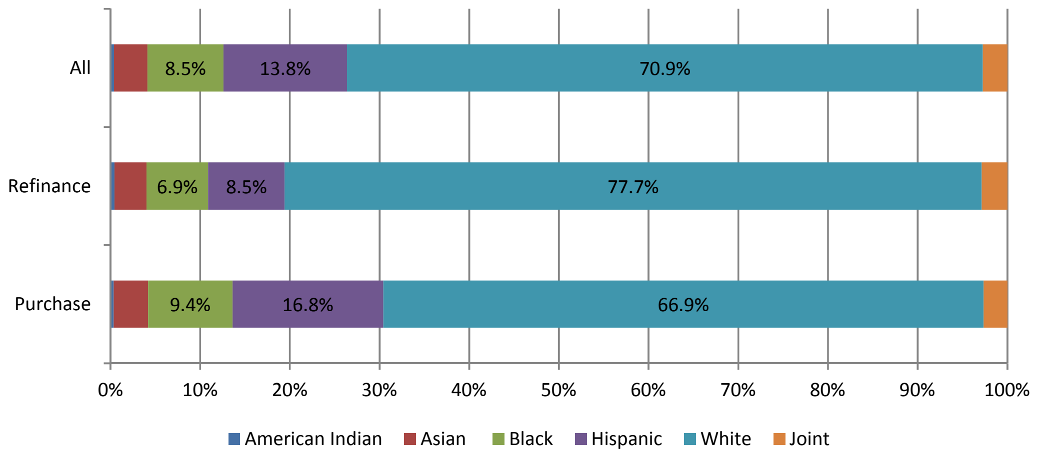
Fiscal Year	Quarter	Credit Score Categories					
		720-850	**680-719**	**640-679**	**580-639**	**300-579**	**N/A[b]**
2008	Oct-Dec	9.3%	9.1%	18.8%	36.2%	23.0%	3.7%
	Jan-Mar	9.9	9.9	19.4	35.6	22.0	3.2
	Apr-Jun	15.2	13.2	22.7	33.8	12.8	2.3
	Jul-Sep	19.1	16.1	24.6	31.9	6.9	1.4
2009	Oct-Dec	20.5	17.2	24.6	31.6	5.2	0.9
	Jan-Mar	24.3	19.0	25.0	27.5	3.4	0.9
	Apr-Jun	29.7	21.2	25.9	20.8	1.5	0.8
	Jul-Sep	33.4	22.1	25.8	16.9	1.0	0.8
2010	Oct-Dec	33.5	22.5	26.4	16.1	0.7	0.8
	Jan-Mar	33.9	22.8	26.8	15.2	0.5	0.8
	Apr-Jun	35.0	22.7	26.8	14.4	0.4	0.7
	Jul-Sep	34.9	22.7	26.7	14.7	0.4	0.7
2011	Oct-Dec	37.1	23.3	26.2	12.4	0.4	0.6
	Jan-Mar	37.8	24.2	28.6	8.6	0.2	0.5
	Apr-Jun	35.4	23.8	30.7	9.5	0.2	0.4
	Jul-Sep	33.1	23.8	31.1	11.4	0.3	0.4
2012	Oct-Dec	33.0	23.9	31.3	11.2	0.2	0.4
	Jan-Mar	33.9	23.9	31.0	10.6	0.2	0.3
	Apr-Jun	33.2	24.2	32.3	9.7	0.2	0.3
	Jul-Sep	30.9	25.3	34.2	9.1	0.2	0.3

[a]Credit scores are co-branded between the three major credit repositories (Equifax, Experian, Transunion) and Fair-Isaac Corporation. Values can range from 300-850. They are grouped here according to the "decision" score used for loan underwriting. That score represents the weakest borrower on a loan application, when there are multiple applicants. Streamline refinance loans do not require full underwriting and so they are not represented here.
[b]Borrowers without credit histories can be underwritten for FHA insurance using alternative, non-traditional forms of credit history.
Source: US Dept of HUD/FHA

5. Minority Homeowners and Homebuyers

FHA provided significant support in FY 2012 for minority homebuyers and minority homeowners seeking to refinance their properties to reduce monthly housing costs (Exhibit III-7). Among those borrowers who disclosed their race, 33 percent of FHA home purchase endorsements and 22 percent of FHA refinance loans were made to minority borrowers. Hispanic/Latino borrowers represented 17 percent of FHA home purchase endorsements and nine percent of refinance loans. African American borrowers represented 9 percent of home purchase and seven percent of refinance loans.

Exhibit III-7
Racial Composition of FHA Single-Family Home Endorsements in FY 2012



Source: U.S. Department of HUD/FHA.

According to the 2011 HMDA data, FHA continues to lead the market in support of minority homeownership. While FHA insurance was used for approximately 27 percent of all home purchase mortgages in 2011, FHA accounted for 50 percent of home purchase mortgages for African American borrowers and 49 percent for Hispanic/Latino borrowers.

Exhibit III-8
Home Purchase Loans and Racial Shares Across Market Segments in 2011

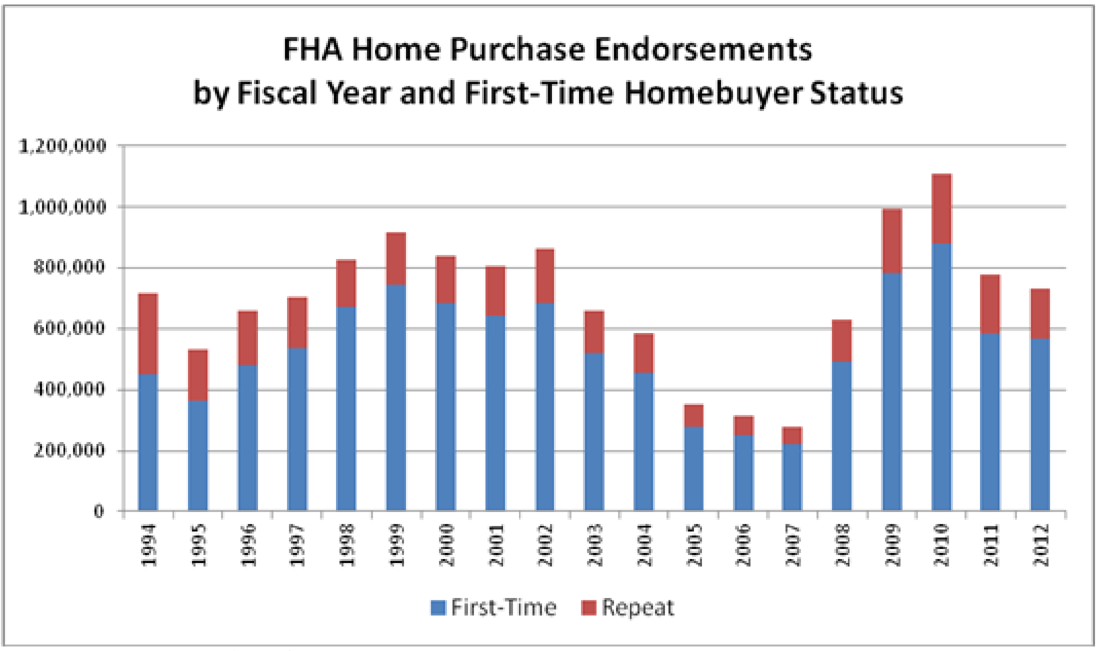
		Market Segments Shares in rows add to 100%			
Race or Ethnicity	**Number of Loans**	**Conventional[a]**	**FHA**	**VA**	**RHS**
All Borrowers	2,575,653	61.1%	27.2%	7.4%	4.3%
American Indian	8,659	48.2	37.1	9.3	5.3
Asian	145,314	79.2	17.5	2.6	0.7
African American	124,910	29.9	50.1	15.9	4.2
Hispanic/Latino	247,166	39.6	48.5	7.7	4.2
White	1,815,460	63.7	24.2	7.1	5.0
Not Disclosed	227,268	69.6	21.4	7.5	1.6
Joint	6,876	50.9	30.2	14.7	4.2

[a]Conventional loans include those originated for sale to Fannie Mae or Freddie Mac, all loans without any federal government guarantee.
Source: U.S. Department of HUD/FHA and HMDA Data. HMDA data analysis compiled by HUD.

6. First-Time Homebuyer

FHA's single-family insurance program has historically been used as a pathway for many households to achieve homeownership. Over the past four fiscal years, FHA has made homeownership possible for over 3.5 million borrowers and 2.8 million of those were first-time buyers. First-time homebuyers accounted for 78 percent of all FHA endorsements in 2012, up from 75 percent in 2011. Using annual surveys performed by the National Association of Realtors and HUD data on FHA, it is estimated that FHA supported 41 percent of all first-time homebuyers in 2011.[1] This share was up slightly in 2011 from 2010.

Exhibit III-9

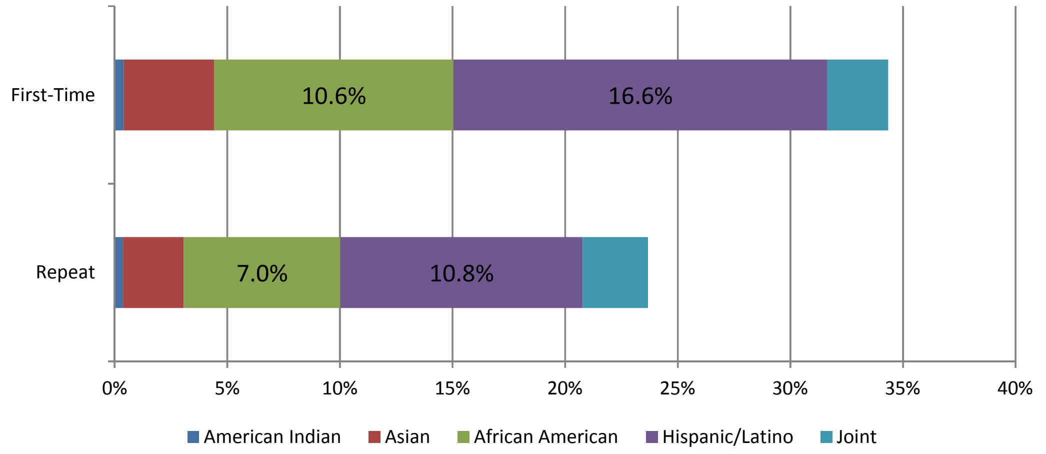


Source: U.S. Department of HUD/FHA.

[1] Survey results are published in the National Association of Realtors Profile of Home Buyers and Sellers 2010, and Profile of Home Buyers and Sellers 2011 reports.

Minority borrowers accounted for a higher share of endorsements for first-time homebuyers than repeat homebuyers. For example, Hispanics accounted for nearly 17 percent of endorsements for first-time homebuyers in 2012 compared to approximately 11 percent of endorsements for repeat homebuyers.

Exhibit III-10
Minority Share of 2012 Home Purchase Endorsements by First-Time Buyer Status

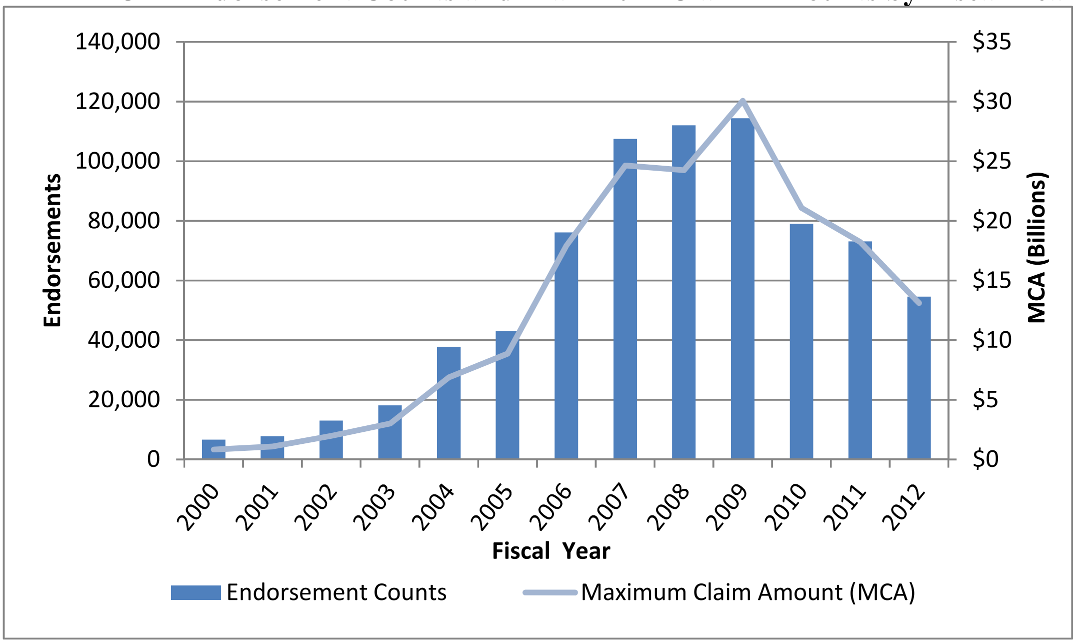


Source: U.S. Department of HUD/FHA.

7. Reverse Mortgages (HECM)

FHA's reverse mortgage product, the Home Equity Conversion Mortgage (HECM), permits senior homeowners to tap accumulated home equity without the burden of monthly payments or the necessity to sell their home.[2] HECM insurance endorsements in FY 2012 were down by 25 percent from FY 2011 levels, to 54,591 loans, as shown in Exhibit III-11. FY 2012 marks the third consecutive year in which HECM volume declined, as the combined effects of policy revisions to the product and changes within the industry have reduced participation in the program.

Exhibit III-11
FHA HECM Endorsement Counts and Maximum Claim Amounts by Fiscal Year[a]

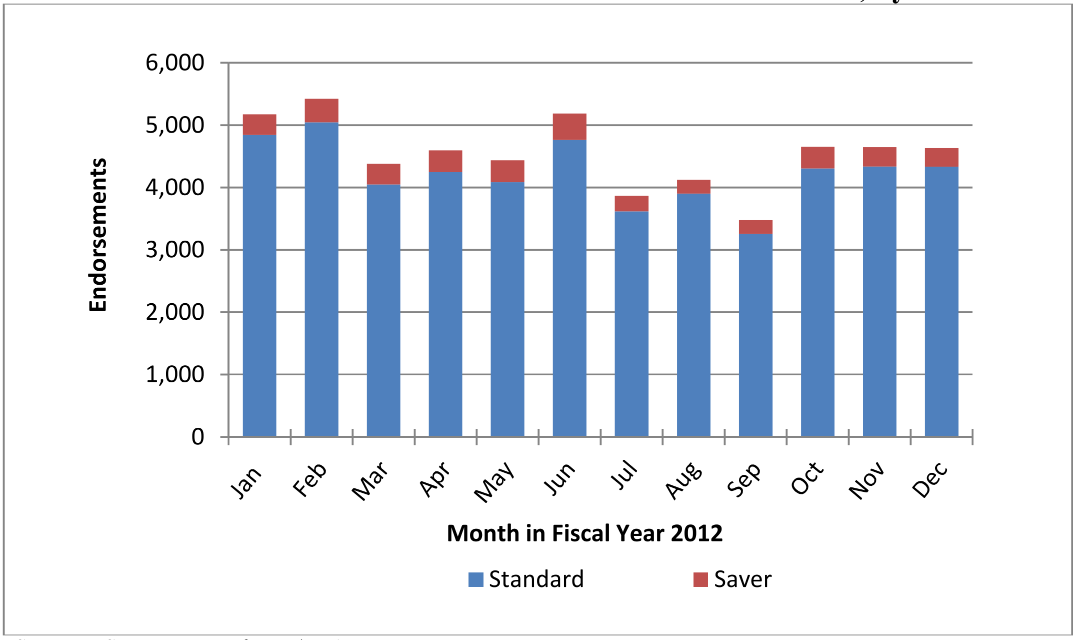


[a]Maximum Claim Amount represents the largest dollar amount of an insurance claim FHA will pay on any given loan. It is calculated as 98 percent of the appraised value of the home at the time of loan origination.
Source: U.S. Department of HUD/FHA.

HUD introduced a new HECM option in FY 2011, called HECM Saver. HECM Saver provides for a near-zero initial insurance premium in exchange for the homeowner agreeing to a lower equity take-out limit. In FY 2012, Saver volumes have remained steady throughout the year such that they now represent 7 percent by count and over 10 percent of insured dollars, as shown in Exhibit III-12. The higher dollar share is due to the fact that Saver is attracting seniors with higher valued homes—57 percent higher, on average.

[2] Information on the FHA HECM program can be found at: http://portal.hud.gov/hudportal/HUD?src=/program_offices/housing/sfh/hecm/hecmhome

Exhibit III-12
FY 2012 HECM Standard and Saver Endorsement Counts, by Month



Source: U.S. Department of HUD/FHA

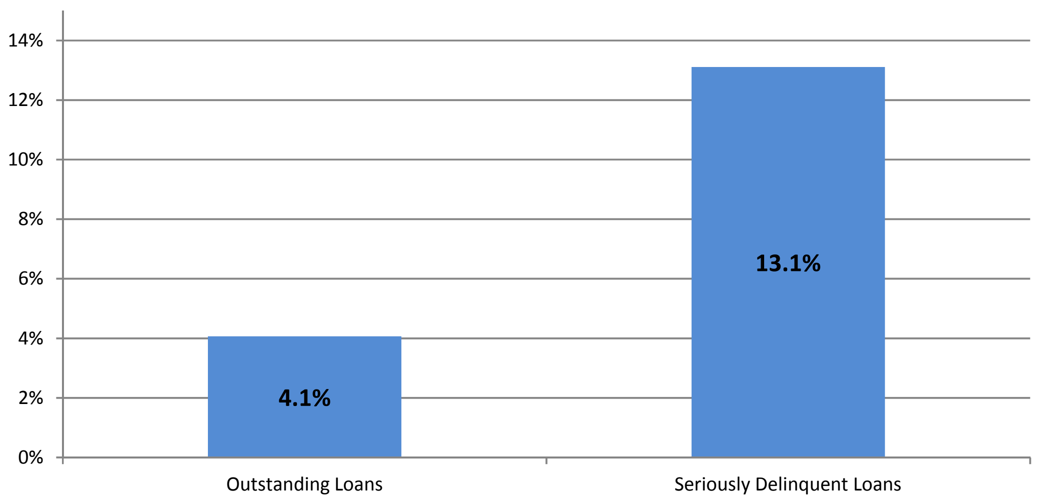
B. PERFORMANCE OF FHA-INSURED MORTGAGES (FORWARD LOANS)

The previous section discussed the characteristics of recent books of business at origination. As has been the case every year, starting with FY 2010, the expectation is that the books of business insured after 2009 will contribute very positively to the health and stability of the MMI Fund, in contrast to the severely stressed books of business insured prior to 2010. Once again, the Actuary this year projects increasingly stronger performance for loans insured each year since FY 2010. This section provides greater detail on the performance of recent books of business.

1. Seller-Funded Downpayment Loans

As in previous years, the Actuary projects substantial losses resulting from loans which utilized seller-funded downpayment assistance. Prohibited by Congress starting in January of 2009, seller-funded downpayment assistance programs used nonprofit conduits to provide funds for use by a purchaser in satisfying FHA-mandated downpayment contribution requirements. Prior to the elimination of seller-funded downpayment assistance programs, the share of borrowers using their own funds for downpayments had fallen below 50 percent. Loans with seller-funded downpayment assistance account for a disproportionate share of outstanding FHA mortgages that are currently seriously delinquent.[3] Seller-funded downpayment loans account for only 4 percent of the outstanding portfolio but 13 percent of all seriously delinquent loans (see Exhibit III-13 below). Over the life of the loans, seller-funded downpayment loans are expected to cost the FHA MMI fund over $15 billion. The Actuary estimates that if FHA had not participated in seller-funded downpayment loans then the net economic value of the MMI fund would be positive $1.77 billion. More details regarding the valuation of the MMI fund will be discussed in section III.

Exhibit III-13
Seller-Funded Downpayment Assistance Loans

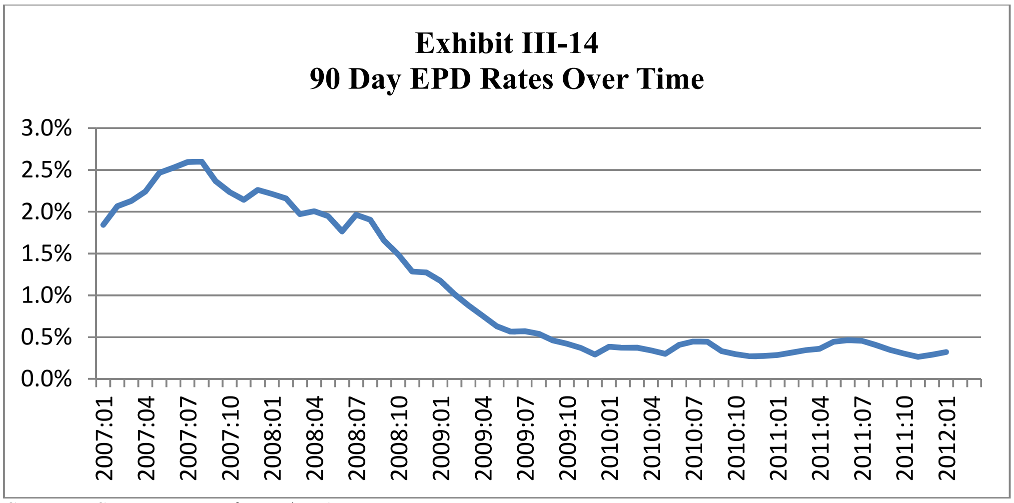


Source: U.S. Department of HUD/FHA.

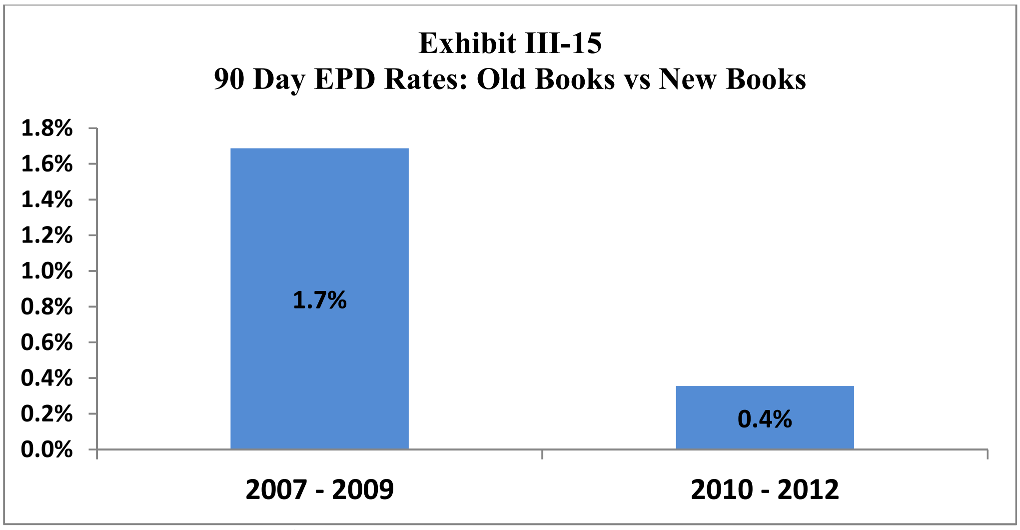
[3] Serious delinquency is defined as loans that are 90 days or more delinquent or in-foreclosure or bankruptcy.

2. Early Payment Defaults

Exhibit III-14 depicts early payment default (EPD) rates, which are defined here as the percentage of loans that become 90 days or more delinquent within the first six payment cycles of the loan. Like the claim rate curve, the EPD rate is a leading indicator that can signal how a book will perform. The overall EPD rate peaked in 2007 at 2.6 percent and has since declined to approximately 0.3 percent. To further illustrate the difference in performance between the older books of business and the newer vintages, Exhibit III-15 depicts the average EPD rates for the 2007-2009 and the 2010-2012 books of business. The EPD rates for the 2007-2009 are nearly 5 times higher than that of the 2010-2012 books.



Source: U.S. Department of HUD/FHA.



Source: U.S. Department of HUD/FHA

3. Seriously Delinquent Rates by Vintage

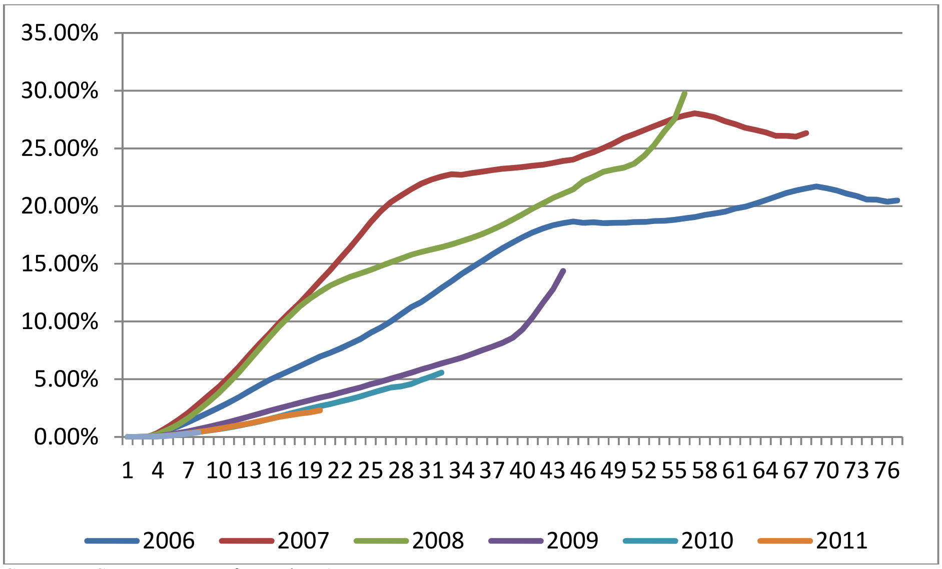
Seriously delinquent rates provide additional evidence that the quality of recent vintages has improved. Exhibit III-16 and Exhibit III-17 demonstrate that vintages starting in 2009 are performing dramatically better than those before. For example, after one year of age, the 2009-2011 vintages are performing approximately four times better than those in 2007 and 2008. After two years of age, the 2010 vintage is performing four times better than 2008 and five times better than 2007. Early signs from the 2012 vintage indicate a continued improvement in seriously delinquent rate versus prior years, signaling an overall continued shift in the quality of the portfolio.

Exhibit III-16
Seriously Delinquent Rates by Vintage (Excluding Streamline Refis)

Age (Years)	2006	2007	2008	2009	2010	2011
1	3.5%	6.1%	5.6%	1.5%	1.0%	1.0%
2	8.5%	17.5%	14.2%	4.3%	3.5%	
3	15.2%	23.0%	17.6%	7.5%		
4	18.5%	25.0%	23.0%			
5	19.5%	27.4%				
6	21.1%					

Source: U.S. Department of HUD/FHA

Exhibit III-17
Seriously Delinquent Rates by Vintage (Excluding Streamline Refis)

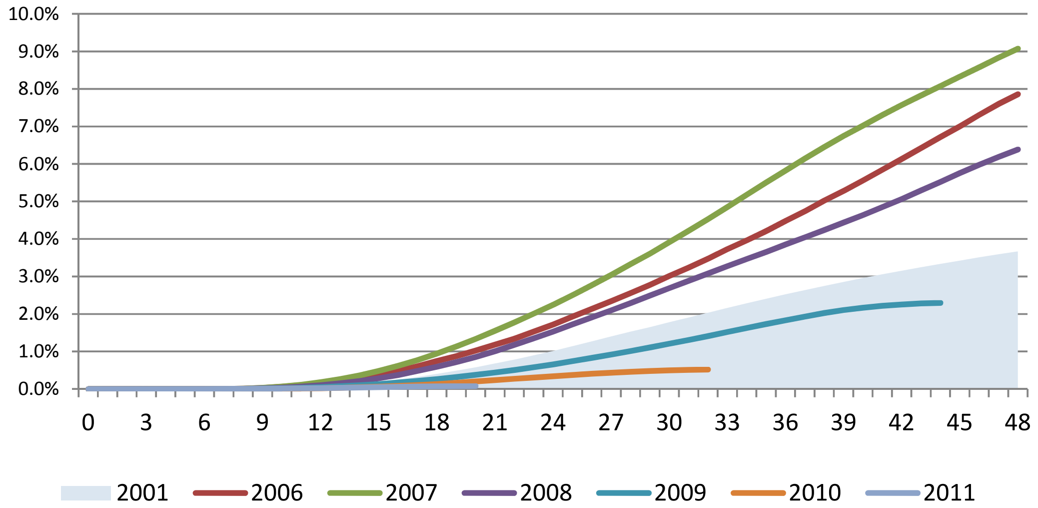


Source: U.S. Department of HUD/FHA

4. Claim Rates by Vintage

The cumulative claim rate curve in Exhibit III-18 shows that the 2009 through 2011 books of business (based on calendar year of origination) are performing better than the 2001 book of business (depicted as the shaded area in Exhibit III-18). The 2001 book of business is considered as a benchmark for the performance of a typical book of business for FHA. The higher performance of the 2009-2011 books of business is a leading indicator that those books of business will perform well and help balance the strain placed on the Fund by older books of business. The 2009 book stands as a transition year between the very poor books insured in 2008 and earlier, in contrast to the very strong books insured in 2010 and after.

Exhibit III-18
Cumulative Claim Rate Curve



Source: U.S. Department of HUD/FHA.

C. CHALLENGES FACING HOME EQUITY CONVERSION MORTGAGES

More borrowers maximizing upfront draw: The introduction of HECM mortgage backed securities (MBS) by Ginnie Mae in FY2008 began the evolution of the HECM program away from a predominately variable-rate line-of-credit program with a wide variety of cash-draw amounts and patterns, to a fixed-rate program where the vast majority of borrowers take out 80 percent or more of the maximum amount possible in one initial cash draw. Research performed by the independent actuaries indicates that HECM loans with such high up-front draws are twice as likely to have a tax-and-insurance default as are loans with initial draws of 60 percent, and four times as high as those with initial draws of 40 percent of the maximum allowed.

Tax and insurance (T&I) defaults: For many homeowners, taking all eligible cash upfront results in insufficient cash flow in later years for property upkeep, taxes and insurance. This impacts program performance by increasing defaults resulting from borrowers being unable or unwilling to make tax and insurance payments. The incidence of T&I defaults has increased in recent years and is incorporated into the Actuarial valuation.

Increased Loan Conveyance Rates: The conveyance rate upon termination increased sharply during this past year. Research indicates that this was directly tied to falling home prices. Owners and estate executors faced with mortgage balances greater than property value at the time of borrower exit from the home are less willing to engage in marketing and sale of the property than are those with positive equity in the home. In such cases, there is no financial benefit from managing the property sale and so those responsible for the home are more likely to convey the property to HUD for sale. Traditionally, about 70 percent of property sales were handled by owners or estate executors. This past year rather, about 70 percent were instead conveyed to HUD. Property management and marketing costs associated with the disposition of homes conveyed to HUD typically cost approximately 12 percent of property value and thus increase the severity of loss for FHA. The actuarial projections now include consideration of how conveyance rates vary with changes in house prices when estimating the economic value of the HECM portfolio.

Longevity risk: Mortality and termination speeds are now estimated to be slower than in previous expectations, increasing the likelihood that loan balances will exceed property values at time of loan termination. Using these updated longevity predictions results in a lower economic value for the HECM portfolio in the actuarial calculations.

IV. The Financial Status of the MMI Fund

A. CURRENT FINANCIAL STATUS

The Mutual Mortgage Insurance (MMI) Fund operates with two primary sets of financial accounts.[4] First, all business transactions related to insurance operations are maintained in a series of Financing Accounts at the U.S. Treasury.[5] Then, secondary reserves for unexpected claim expenses are maintained in a separate Capital Reserve Account, which is also held at the U.S. Treasury. The Capital Reserve Account is unique to MMI Fund operations. It was established to assist in managing to the two-percent capital ratio requirement enacted by Congress in 1990. FHA's MMI Fund programs, however, like all federal government direct-loan and loan-guarantee programs, operate with what is called "permanent and indefinite budget authority." That provides access to the U.S. Treasury for any funds needed to pay extraordinary claim obligations. Thus, FHA programs are never in jeopardy of lacking sufficient funds to pay insurance claims. That would be true even in the absence of a Capital Reserve Account.

1. Account Balances

At the end of FY 2012, the MMI Fund had $38.4 billion in combined account balances with the U.S. Treasury. Of that total, $35.1 billion was in the Financing Accounts and $3.3 billion in the Capital Reserve Account. They represent liquid assets available for cash needs. The combined balances are referred to as the capital resources of the MMI Fund shown below in Exhibit IV-1.

Actual net Capital Resources at the end of FY 2012 were approximately $30.4 billion which is right in line with what was predicted last year by the independent actuaries.[6] Of note, Exhibit IV-1 reflects significant movement of funds from the Capital Reserve Account to the Financing Accounts over the past four years. Those fund transfers were conducted as part of the annual budget re-estimate process overseen by the Office of Management and Budget (OMB), and were performed in order to build dedicated loss reserves against anticipated future net claim expense outlays for outstanding loan guarantees. Some transfers were to create loss reserves for the HECM program, which first entered the MMI Fund in FY2009 and thus had no opportunity to build reserves prior to the financial crisis.

[4] There are two additional sets of accounts that are independent of the insurance operations, and for which funds are directly appropriated by the Congress each year. The first is the set of Program Accounts which cover all personnel and administrative expenses for FHA operations. The other is the Liquidating Account, which represents remaining cash flows each year on pre-1992 insurance endorsements. The year 1992 marks implementation of the Federal Credit Reform Act of 1990 and introduction of the Financing Accounts.

[5] There are individual Financing Accounts maintained for each annual book of business, or what are called budget cohorts. There are also separate accounts for forward loans and for HECM.

[6] The MMI fund has cash and investments totaling $38.4 billion as of September 30, 2012. Of the $38.4 billion, $35.1 billion is in the MMI Financing Account. To accurately reflect the *net* resources in the MMI Financing Account of $27.1 billion, a manual adjustment has been made to netting out other assets (primarily loans receivable and properties) and other liabilities (primarily borrowings).

Exhibit IV-1
FHA MMI Fund Account Balances by Quarter, FY 2009 – FY 2012[a]
(billions)

Fiscal Year	Quarter Ending in	Capital Reserve Account[b]	Financing Account[c]	Total Capital Resources[d]
2008	September	$19.30	$9.00	$28.20
2009	December	19.6	9.3	28.9
2009	March	19.9	9.7	29.6
2009	June	10	20.9	30.9
2009	September	10.7	21.1	31.8
2010	December	11.4	21.2	32.6
2010	March	12	20.2	32.2
2010	June	3.5	29.6	33.1
2010	September	4.4	28.9	33.3
2011	December	6.3	26.4	32.7
2011	March	7.7	23.9	31.6
2011	June	2.8	28.9	31.7
2011	September	4.7	29	33.7
2012	December	5.7	27.6	33.3
2012	March	7	25.3	32.3
2012[e]	June	9.8	21.9	31.6
2012[f]	September	3.3	27.1	30.4

[a]Only September 2008, 2009, and 2011 represent audited figures.

[b]This is an on-budget account that records net receipts provided by FHA to the federal budget, since 1992. Balances are held in cash and (nonmarketable) Treasury securities. The securities earn interest for FHA.

[c]This is a series of off-budget cash accounts used to manage insurance operation collections and disbursements.

[d]Total Capital Resources is the sum of Capital Reserve and Financing Account balances, and it represents the sum of cash and investments at the Treasury that can be immediately liquidated into cash. It does not represent total assets of the MMI Fund.

[e]Under the requirements of Federal Credit Reform accounting, $6.8 billion was transferred in June 2012 from the Capital Reserve Account to the Financing Account, as part of the annual budget re-estimate process. Those transferred amounts became earmarked funds to cover possible future net claim losses. If they are not needed, they will be transferred back to the Capital Reserve Account in a future budget re-estimate.

[f]The MMI fund has cash and investments totaling $38.4 billion as of September 30, 2012. Of the $38.4 billion, $35.1 billion is in the MMI Financing Account. To accurately reflect the *net* resources in the MMI Financing Account of $27.1 billion, a manual adjustment has been made to Exhibit IV-1 netting out other assets (primarily loans receivable and properties) and other liabilities (primarily borrowings).

Source: U.S. Dept of HUD/FHA; October 2012.

2. Core Insurance Operation Cash Flows in FY 2012

Core insurance operation cash flows are the net of collections (insurance premiums, property sale receipts, and other income, including $1.2 billion in settlement receipts) minus disbursements (insurance claims, property maintenance, and other expenses), as shown in Exhibit IV-2. Actual core insurance operations had a net outflow of $2.8 billion this year. To put this into context, while FHA paid out a record $18 billion in claims in FY 2012, the net draw-down of capital resources was only $2.8 billion.

Exhibit IV-2
FHA MMI Fund Financing Account Insurance Operations Cash Flows in FY2012, by Quarter[a] (millions)

	Quarter 1	Quarter 2	Quarter 3	Quarter 4	Fiscal Year Totals
Collections					
Premiums	$1,942	$2,019	$2,329	$2,393	$8,683
Property Sale Receipts	$1,648	$1,435	$1,606	$2,090	$6,779
Note Sale Collections	($1)	$0	$5	$23	$27
Other[c]	$42	$20	$16	$1,136	$1,214
Total	$3,631	$3,474	$3,956	$5,642	$16,703
Disbursements					
Claims[b]	($3,733)	($4,358)	($5,370)	($4,783)	($18,244)
Property Maintenance	($326)	($270)	($291)	($364)	($1,251)
Other	-	-	($1)	-	($1)
Total	($4,059)	($4,628)	($5,662)	($5,147)	($19,496)
Net Operations Cash Flow	($428)	($1,154)	($1,706)	$495	($2,793)

[a]These are unaudited figures; totals may not add due to rounding.

[b]Claim payments shown here include conveyance, pre-foreclosure sale, note sales, and loss mitigation actions.

[c]This includes the mortgage settlement amounts of $1.12 billion recognized in August 2012.

Source: U.S. Dept of HUD/FHA; October 2012.

B. ASSESSMENT OF THE INDEPENDENT ACTUARY

The National Housing Act requires that HUD contract for an independent actuarial study of the MMI Fund each year.[7] The two portfolios of the MMI Fund—forward (single-family) and reverse (HECM) mortgages—are fundamentally different in characteristics and performance, so they are analyzed in two separate reports. For FY 2012, the same contractor was selected for both studies.[8] The final written reports are available online in the FHA Office of Housing Reading Room at www.hud.gov.[9]

The actuarial studies use statistical models to develop 30-year projections of default, claim, loss-on-claim, and prepayment rates on current and future books of business. Those models are estimated using historical patterns of FHA-insured loan performance under a wide variety of economic conditions. They are applied to active loans, and they use commercially-available forecasts of home prices and interest rates to predict loan performance in the future. The resulting projections determine business-operation cash flows needed to estimate the economic value of the Fund.

This year, the actuarial study applied a stochastic method to estimate the net present value (NPV) of future cash flows. The move to a stochastic method represents one of the advancements that have been made to the actuarial modeling process this year. In previous studies, the net present value of cash flows was computed along a single path of house prices and interest rates. This year, 100 equally likely paths were generated to develop a wide variety of possible economic conditions, creating what is known as a Monte Carlo simulation. The discounted, net present value (NPV) of cash flows was computed for each path. They were then averaged to obtain an overall estimate of the expected NPV that provides the base-case estimate.

The outcome of the complete actuarial study modeling effort is the estimated "economic net worth" of the MMI Fund, which is defined by the National Housing Act as capital resources plus the present value of future cash flows of the MMI Fund.[10] The calculation of economic net worth is repeated for each of the next seven years by adding projected endorsements each year, forecasting their cash flows and adding them to those of the current portfolio, and then reassessing economic net worth on the updated portfolio at the end of each fiscal year. Economic net worth represents additional resources directly available to FHA for absorbing claim expenses above-and-beyond those already anticipated in the present-value-of-future-cash-flow calculations. Those calculations are for the remaining life of all outstanding loan guarantees and can extend for more than 30 years on HECM loans. Economic net worth is the numerator of

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[7] See 12 USC 1708(a)(4).
[8] Integrated Financial Engineering Group, Inc. was the contractor utilized for these reports. In the two previous years, the actuarial study for the HECM portfolio was conducted by IBM while Integrated Financial Engineering performed the forward-loan study.
[9] See http://www.hud.gov/offices/hsg/hsgrroom.cfm.
[10] See 12 USC 1711(f)(4). The statute refers only to capital resources (liquid assets) and the present value of future cash flows. The actuarial studies, however, include value of properties in inventory and net accounts receivable and payable in their calculation of capital resources rather than in the present value of future cash flows. This is because they do not predict these items, but rather take their values from the values used by FHA in its annual financial statements.

the statutory capital ratio measure. The denominator is the outstanding dollar volume of active insurance contracts.

This section will first discuss the findings of the actuarial study holistically, and then discuss the details of both the forward and HECM programs separately.

1. Economic Net Worth and Capital Ratio Estimates (Total Insured Portfolio)

The fundamental actuarial valuation of the MMI Fund is provided in Exhibit IV-3. It combines the current net asset position of the portfolio (net capital resources) with estimates of the present value of future cash flows—projected mortgage insurance premium (MIP) revenue minus projected credit losses for the current portfolio. The sum of the two is economic net worth (ENW), as defined by the National Housing Act.[11] ENW, in turn, is divided into the value of the outstanding, insured portfolio to calculate a capital ratio.

This fiscal year, the MMI Fund capital reserve ratio fell below zero to *negative* 1.44 percent. The actuarial assessments estimate that the economic value of the Fund as of the end of FY 2012 is *negative* \$16.3 billion against an active portfolio of \$1.13 trillion. The economic value of the forward portfolio was estimated at *negative* \$13.5 billion, the HECM portfolio at *negative* \$2.8 billion. These economic values represent capital reserve ratios of *negative* 1.28 percent and *negative* 3.58 percent respectively.

[11] See 12 USC 1711(f).

Exhibit IV-3
Actuarial Assessments for FY 2012 (millions)

	FY 2011	FY 2012		
	Summary[a]	Single Family	HECM[b]	MMI Fund
Beginning-of-Year Positions[c]				
Cash		$25,532	$4,236	$29,768
Investments		$4,129	$0	$4,129
Properties and Mortgages		$2,458	$23	$2,481
Other Assets and Receivables		$18	($1)	$17
Total Assets		$32,137	$4,258	$36,395
Liabilities (Accounts Payables)		($4,228)	($12)	($4,240)
Capital Resources at Beginning of Year		$27,909	$4,246	$32,155
FY 2012 Activity				
Net Gain from Investments		$2,272	$148	$2,420
Net Insurance Income		($5,429)	$330	($5,098)
Net Change in Value of Property Inventory		($454)	$77	($377)
Net Change in Accounts Payable		$156	($14)	$142
Settlement Funds		$1,120	$0	$1,120
Capital Resources at End-of-Year	$32,431	$25,574	$4,787	$30,362
Actuarial Calculations[d]				
Present Value of Future Cash Flows on Outstanding Insurance		($39,052)	($7,586)	($46,638)
Economic Net Worth	$2,551	($13,478)	($2,799)	($16,277)
Capital Ratio Calculations				
End-of-year Amortized Insurance-in-Force[e]	$1,077,526	$1,053,329	$78,214	$1,131,543
Capital Ratio[f]	0.24%	-1.28%	-3.58%	-1.44%

[a]Data in this column are from the FY 2011 Actuarial Reviews of the Single-Family and HECM programs of the MMI Fund

[b]HECM amounts appear small because HECM is only included in the MMI Fund starting with FY 2009 insurance endorsements.

[c]Beginning of year positions are from FHA's audited FY 2011 financial statements with the exception of the HECM transfer amounts.

[d]Actuarial calculations for Single-Family and HECM come from the respective FY 2012 Actuarial Reviews.

[e]Amortized Insurance-in-Force represents outstanding loan balances for forward loans and maximum claim amounts for HECM. Dollar amounts shown here for 2012 represent end-of-year estimates made by the independent actuaries before end-of-year data was available.

[f]The National Housing Act (12 USC 1711(f)) defines the capital ratio calculation as being the ratio of economic net worth to outstanding loan balances.

Source: U.S. Dept of HUD/FHA; October 2012.

The MMI Fund capital ratio is expected to be positive by FY 2014 and reach 2.0 percent during FY 2017 in the base-case estimate, as shown by Exhibit IV-4. These forecasts assume no changes in policy or other actions by FHA that might accelerate the time to recovery. Section V outlines FHA's Action Plan to accelerate this time change.

Exhibit IV-4

Annual Projections of MMI Fund Economic Net Worth and Capital Ratio under Base-Case Estimates, 2012 – 2019

Fiscal Year	Insurance in Force (billions)	Economic Net Worth (billions)	Capital Ratio
2012	$ 1,131	-$16.3	-1.4%
2013	1,230	-5.3	-0.4
2014	1,291	2.0	0.2
2015	1,314	9.7	0.7
2016	1,352	19.7	1.5
2017	1,401	30.7	2.2
2018	1,441	42.0	2.9
2019	1,467	53.9	3.7

Source: FY 2012 Actuarial Reviews of the MMI Fund; analysis by U.S. Department of HUD/FHA.

3. Attribution of Economic Value (Forward Loans)

Forward loans comprise the vast majority of the loan guarantee portfolio of the MMI Fund, with an active insurance-in-force of $1.05 trillion. This year the Actuary projects the economic value of the forward portfolio to be *negative* $13.5 billion, compared to $1.2 billion last year. The low capital ratio today reflects an expectation that FHA's current pool of insured loans still has significant foreclosure and claim activity yet to occur. Projected losses are particularly large for the fiscal year 2007-2009 loans. Those loan cohorts were impacted by the severe recession and accompanying increases in unemployment, and by large volumes of seller-funded down payment loans. Those loans are projected to cost the Fund $15 billion as they continue to experience elevated rates of insurance claim. In fact, the Actuary estimates that, if FHA had not insured any seller-funded-downpayment loans, the net economic value of the MMI Fund would be positive $1.77 billion today. In contrast to the drain caused by those older loans, the Actuary expects fiscal years 2010 through 2012 endorsements to produce significant net revenues that can be used to offset mounting losses from earlier books of business. The contrast in quality between these two vintage eras—pre- and post-2009— is demonstrated by Exhibit IV-5.

Exhibit IV-5
Lifetime Economic Value by Endorsement Vintage (Forward Loans)

Vintage	Original Loan Balances ($billion)	Present Value of Premium Revenue	Present Value of Credit Losses	Economic Value (%)	Economic Value ($billion)
1992 - 2006	**$1,190**	**3.5%**	**5.1%**	**(1.6%)**	**($19.5)**
2007 - 2009	**564**	**3.8%**	**11.0%**	**(7.2%)**	**(40.6)**
2010 - 2012	**721**	**6.0%**	**2.9%**	**3.1%**	**22.7**
Total	**$2,475**	**4.3%**	**5.8%**	**(1.5%)**	**($37.4)**

Source: FY 2012 Actuarial Reviews of the MMI Fund; analysis by U.S. Department of HUD/FHA.

The difference in last year's projected 2012 capital position compared to this year's projection is summarized in Exhibit IV-6:

Exhibit IV-6
Summary of Changes (Forward Loans)
Estimate of 2012 Economic Value from Last Year's 2012 Expectation

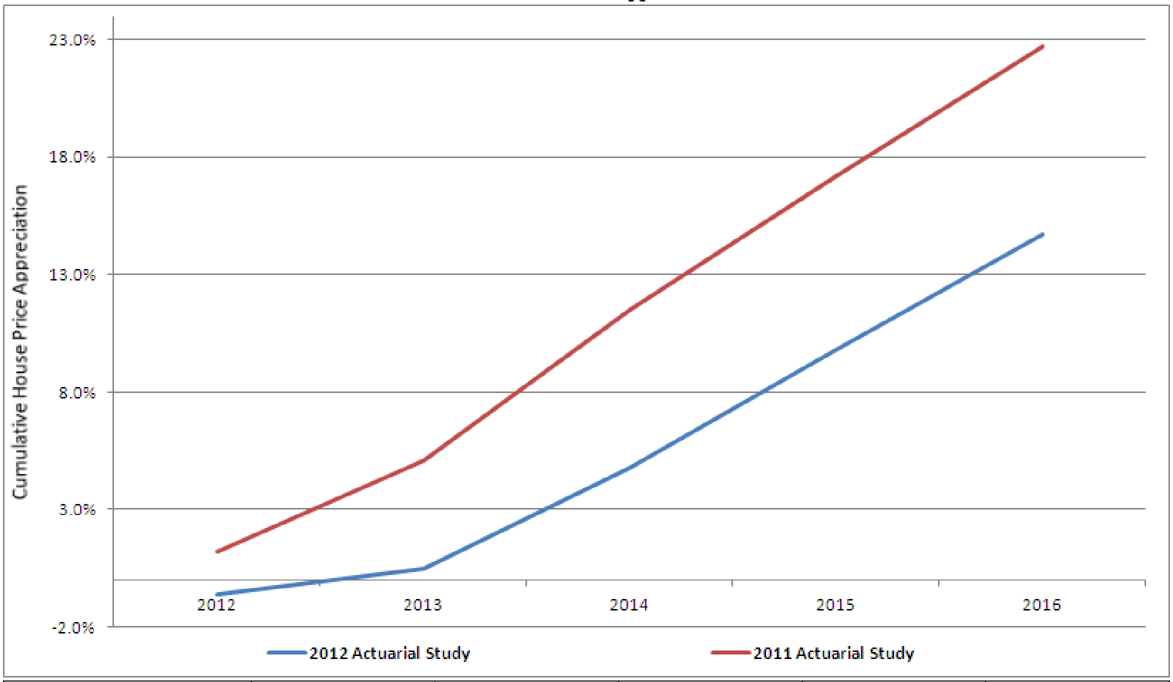
	Impact ($billion)	Explanation
2012 volume	$3.3	The FY 2012 volume was higher than had been anticipated last year ($212 bil vs. $156 bil), primarily due to low interest rates spurring refinance activity.
Changes to loss severity model	($10.2)	Shares of Pre-foreclosure sale (PFS or short sales) and REO in claim predictions are now explicitly modeled, and each has its own loss rate forecast. PFS share of claims is now less than half of what was implied in past models. Also, model structure changes removed an artificial cap on the effect of declining home prices on REO loss rates.
Less optimistic House Price Appreciation (HPA)	($10.5)	HPA projections are 8% lower over the first five years than they were in the 2011 actuarial study (see chart on following page). This effect would be substantially reduced were the actuarial forecasts able to use price indices that fully capture improvements already seen in home prices this year.
Lower interest rates	($8.0)	Rates are projected to be 1.5 - 2.5% lower over the next two years than they were in the 2011 projections. As explained in the text below, this results in $2.6 billion in lost revenue from faster loan prepayment as well as an additional $5.4 billion in claims costs.
Miscellaneous	$2.6	Net impact of eleven other adjustments.
Net Change to Economic Value*	($22.8)	$22.8 billion represents about a 2.3% difference in portfolio value from last year's estimate of where we would be now.

* 2011 actuarial study projected a $9.35 billion capital position by 2012 compared to -$13.48 projected in this year's analysis, a $22.8 billion difference.

The difference in value attributed to the three primary forecast or modeling changes is described in more detail below:

a. **Less optimistic house price appreciation (HPA).** First, the Moody's Analytics July 2012 house price forecast, which was used in this year's actuarial study, predicted significantly lower levels of appreciation in the near term than did the forecast used in last year's actuarial study (Exhibit IV-7). This results in a cumulative difference in projected house price appreciation of 8 percentage points over the first five years alone. Thus, this downward revision in house price forecasts from last year to this year accounted for an estimated $10.5 billion in reduced economic value compared to the actuary's 2011 projection of what the Fund's economic value would be as of the end of FY 2012.

Exhibit IV-7
FHA Single Family Portfolio Geographically Weighted
Cumulative House Price Appreciation Rates



	2012	2013	2014	2015	2016
2011 Actuarial Study	1.20%	5.10%	11.50%	17.20%	22.70%
2012 Actuarial Study	-0.60%	0.50%	4.80%	9.80%	14.70%
Cumulative Difference	-1.80%	-4.60%	-6.70%	-7.40%	-8.00%

Source: Moody's Analytics, July 2011 and July 2012 forecasts of the FHFA All-Transactions HPI, metropolitan area series; analysis by the U.S. Department of HUD/FHA.

Second, the actuarial study uses the All-Transactions home price index (HPI), produced by the Federal Housing Finance Agency (FHFA), which captures metropolitan statistical area (MSA) level house price trends. The actuarial study uses this forecast in order to better capture geographic trends in home prices and FHA activity. However, forecasts of the All-Transactions HPI do not yet show the house-price growth recorded by the FHFA in its more commonly cited Purchase-Only HPI. For example, the Moody's Analytics FY 2012 estimate of national house price growth in the All-Transactions series used by the actuarial study (July 2012 forecast) is *negative* 0.6 percent. Moody's comparable estimate of the FY 2012 house price change in the national Purchase-Only HPI is a positive 1.4 percent. This disparity in HPI series' is the result of heightened activity in the Home Affordable Refinance Program (HARP) at Fannie Mae and Freddie Mae. HARP activity is biased toward geographic areas that have been more severely impacted by the housing recession. The All-Transactions HPI includes all refinance activity, while the Purchase-Only HPI includes none of it.

The disparity between movements in the All-Transactions and Purchase-Only HPI series have only increased in more up-to-date forecasts by Moody's Analytics. In their most recent national forecasts (November 2012), the Purchase-Only HPI is expected to have a FY 2012 growth of 3.3 percent, while the All-Transactions HPI Is expected to have a fiscal year decline of 1.7 percent. For calendar year 2012 the difference between the two is even more pronounced, with the Purchase-Only HPI expected to show growth of 4.1 percent while the All-Transactions HPI is expected to experience a decline of 2.2 percent. Given the timing of the actuarial study, none of the value from these recent improvements was able to be captured.

b. Continuation of historically low interest rates: Mortgage interest rates in the 2013-2014 period are now projected to be 1.5-2.5 percentage points lower than was projected by the 2011 actuarial study (Exhibit IV-8). This results in an estimated $8 billion reduction in economic value, which comes from two types of borrower actions. First, lower interest rates cause a substantial increase in claim payments as borrowers with loans originated prior to FY 2012, and with above-market interest rates, consider their housing to be over-priced. For many, returning to renter status in order to lower housing expenses becomes a viable consideration. In the actuarial forecasts, default rates increase by eight percent on the critical FY 2008 – 2011 cohorts as a result of the way in which low interest rates create situations where borrowers believe they are paying too much for housing. Net economic value then declines by $5.4 billion. The second factor at play with continuing low interest rates in the early years of the forecast period is increased prepayment speeds. More borrowers with above-market mortgage interest rates will refinance their homes, leaving fewer active loans remaining from the current portfolio, and decreasing premium revenues accordingly. The actuarial study projects that faster prepay speeds will reduce economic value by $2.6 billion.

Exhibit IV-8
10-Year Treasury Rate Forecasts for the Current and Prior Review

c. **Refinements to the Actuarial Model:** First, changes to the structure of the loss-on-claim model removed what was effectively a cap on how much falling house prices could impact forecasted loss rates, as recent FHA claims experience show a greater share of higher loss claims. The result was a $5 billion reduction in estimated economic value. Additionally, based on recommendations made by the GAO, HUD's Inspector General and others, the Actuary adopted a more refined model, adjusting the way losses from defaulted loans are reflected in the economic value of the MMI Fund, resulting in an estimated $5 billion in reduced economic value. Shares of pre-foreclosure sale (PFS or Short Sales) and REO in claim predictions are now explicitly modeled, and each has its own loss-rate forecast. The PFS share of claims is now less than half of what was implied in last year's actuarial study. Loss severities on short sales tend to be about 20 percentage points lower than those on REO dispositions, creating substantial savings for FHA.

4. Calculation of Economic Value (Forward Loans)

To provide context for addressing the details of the actuarial assessments, it is helpful to review the three major financial components of the MMI calculation. It should be noted that the Actuarial predictions are ***absent any changes made by HUD***. HUD can positively influence future value projections by implementing targeted policy initiatives. The current Action Plan explaining such initiatives is addressed in Section V. The three major financial components of MMI calculation are:

a. **Future Mortgage Insurance Premium (MIP) Revenues from Outstanding Current Loan Guarantees**. These are projected to generate $32.7 billion in revenue on a present value (PV) basis.
b. **Expected Future Net Credit Losses**. The PV of credit losses is now $71.8 billion, up by $14.5 billion from the 2011 actuarial projection. These estimates are of claim payments net of property recoveries.
c. **Capital resources of $25.6 billion**. These represent cash, liquid assets (bonds held at Treasury), and saleable assets (notes and properties) that together create cash available for claim payments before any future revenues are added.

A comparison of the Actuarial results for MMI Fund Forward loans in 2012 and 2011 is presented below in Exhibit IV-9.

Exhibit IV-9
Economic Value of the Forward Portfolio
Comparison of 2012 and 2011 Actuarial Assessments
(all dollars are in billions)

	2012	2011	Difference
(1) PV MIP Revenue	$ 32.7	$ 30.3	$ 2.4
Less: (2) PV Credit Losses	(71.8)	(57.3)	(14.5)
Equals: NPV Future Cash Flows	(39.1)	(27.0)	(12.1)
Plus: (3) Capital Resources	25.6	28.2	(2.6)
Equals: Economic Value	(13.5)	1.2	(14.7)
Divided by: Insurance in Force	1,053	1,009	44
Equals: Economic Value (%)	(1.28%)	0.1%	(1.44%)

Source: FY 2012 Actuarial Reviews of the MMI Fund; analysis by U.S. Department of HUD/FHA.

As can be seen from Exhibit IV-9, the change in capital position this year is the result of the increase in projected net credit losses by $14.5 billion. Changes in revenue projections and starting capital resources effectively offset one another. While the number of forecasted claim actions remained largely unchanged from last year, projected loss rates on those claims (Loss Given Default or LGD) increased measurably. This change was caused by both economic forecasts and modeling refinements, and it stands out as the major driver of the decline in net economic value for the MMI Fund this year.

5. Economic Net Worth by Book-of-Business (Forward Loans)

The (single-family) books-of-business insured prior to 2010 are expected to generate large losses for the MMI Fund. The peak book for losses per-dollar of insured loans is 2007, the year that also has experienced the greatest total decline in home values. When that book is finally closed, its total cost is expected to exceed 11.3 percent of the initial dollar volume of loans insured. Though the 2008 book has a lower loss-per-dollar (7.7 percent), that book was three times as large as 2007, and therefore, has expected dollar losses that are more than twice those of 2007 book ($13.2 billion versus $6.4 billion).

In addition to being originated near the peak of the housing bubble, the 2007 - 2008 books were also heavily affected by seller-funded down-payment-assistance (SFDPA) loans. Those loans became ineligible for FHA insurance starting with originations in FY 2009, and they essentially disappear from new endorsements starting in January 2009.[12] However, their ongoing effect on the financial status of the MMI Fund is still measurable, as they are expected to result in 25 percent of the losses in those vintages.[13] The Actuary estimates that economic net worth of the MMI Fund would be higher by over $15 billion without SFDPA loans.[14] Thus, if FHA had not insured any SFDPA loans, the net economic value of the MMI fund would be positive $1.77 billion today.

While credit losses are the story of this actuarial study, insurance premium revenue also plays a critical role in the recovery of the health of the MMI Fund. Premium rate increases were among several measures taken by HUD to position FHA for rebuilding the two percent required capital within the near future. With home prices substantially below peak levels, and interest rates historically low, these premium rate increases have not unduly jeopardized FHA's role in providing an affordable option for low-to-moderate income home buyers. The four MIP increases that have been implemented under this Administration have, to date, bolstered the MMI Fund capital position by more than $10 billion.

To put current premium rates in context, the independent actuarial study estimates that if the entire portfolio had today's rates, although it would not be above the Congressionally mandated 2 percent, the capital reserve ratio would be positive by nearly 1.6 percent. In other words, although not large enough to maintain a 2 percent capital cushion through a similar housing crisis, current premium rates would permit FHA to withstand another severe housing crisis, even with the current mix of legacy and new-book loans.

Exhibits IV-10 and IV-11 illustrate how actions taken to date on credit policy and loan guarantee pricing have significantly improved the trajectory of the MMI Fund. Exhibit IV-10 shows credit losses and premium revenue as percentages of total endorsement volumes for each book. Starting with the 2007 vintage, credit losses as a percentage of endorsements have declined sharply while, at the same time, premium revenues have steadily increased as a percentage of endorsements. Beginning with the 2010 vintage, and continuing through 2012, expected lifetime premium revenues exceed expected credit losses as newly implemented credit and pricing policies take effect. Exhibit IV-11 pieces together expected lifetime premium revenues and credit losses to depict the net economic value of each book, per the new actuarial estimates. This view further shows the improved trend of Fund finances. The 2010-2012 vintages have positive and increasing net economic value.

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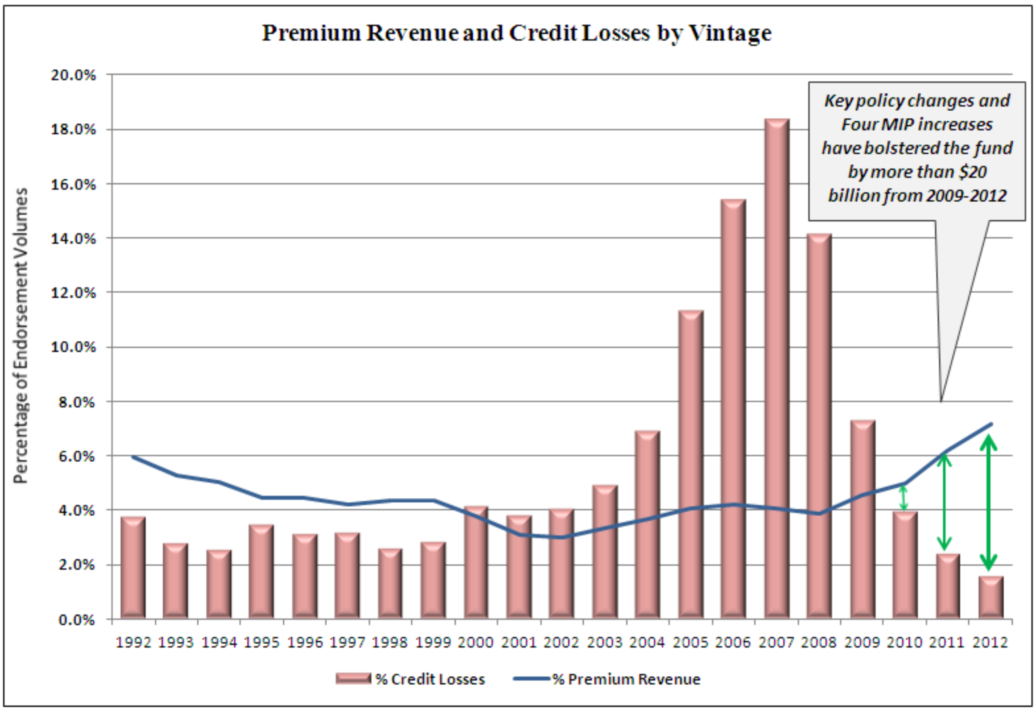
[12] Congress banned use of FHA insurance on such loans in the Housing and Economic Recovery Act of 2008.

[13] Their on-going effect is not only in remaining home purchase loans that could still result in an insurance claim, but also through streamline refinancing that brought many of the 2005-2008 loans into the 2009 and even 2011 books.

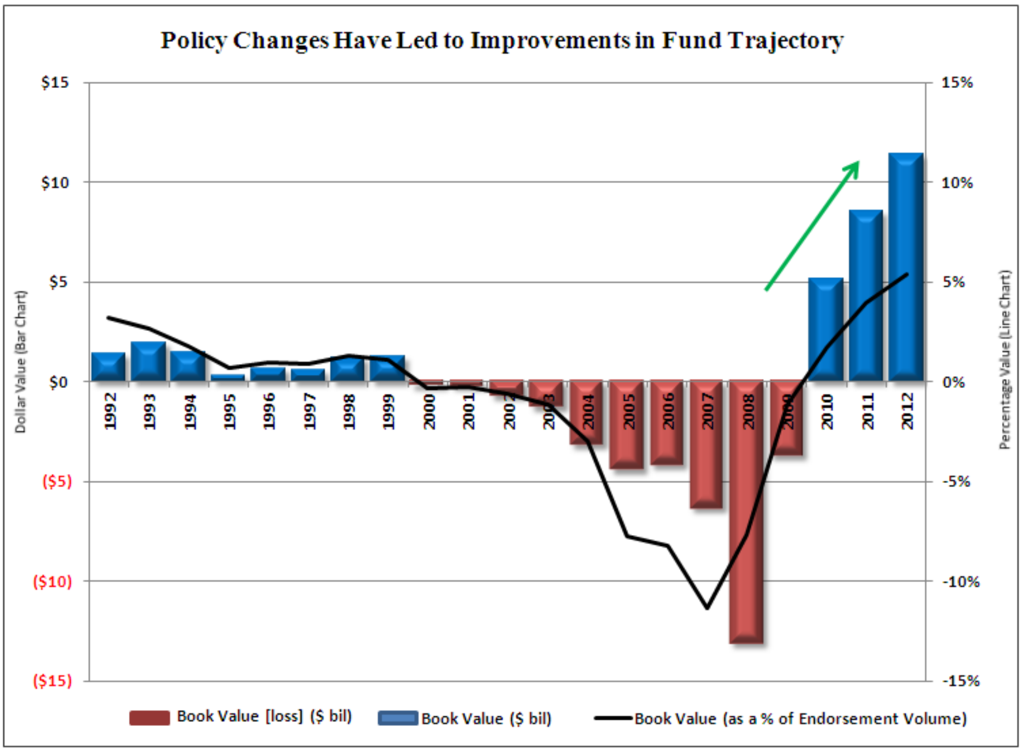
[14] The net expected cost of those loans, as projected by the independent actuaries, grew by $1.8 billion over the past year to $15 billion.

Exhibit IV-10



Source: FY 2012 Actuarial Reviews of the MMI Fund; analysis by U.S. Department of HUD/FHA.

Exhibit IV-11
Economic Net Worth by Book-of-Business



Source: FY 2012 Actuarial Reviews of the MMI Fund; analysis by U.S. Department of HUD/FHA.

6. Expected Economic Net Worth and the Capital Ratio over Time (Forward Loans)

The Actuarial analysis projects that the MMI Fund capital ratio for the forward-loan portfolio will again be positive by 2014, and will reach 2.0 percent some time in FY 2017. That is shown in Exhibit IV-12. The actuarial forecasts assume no changes in policy or other actions by FHA that might accelerate time to recovery. Section V of this report outlines FHA's Action Plan to accelerate the timeline to full recovery.

Exhibit IV-12

Actuarial Projections of Present and Future Capital Ratios for Forward Loans

Fiscal Year	Insurance in Force (billions)	Economic Net Worth (billions)	Capital Ratio
2012	$ 1,053	-$13.5	-1.3%
2013	1,137	-2.6	-0.2
2014	1,186	4.2	0.4
2015	1,195	11.5	1.0
2016	1,217	21.0	1.7
2017	1,248	31.4	2.5
2018	1,270	42.5	3.3
2019	1,277	54.3	4.2

Source: FY 2012 Actuarial Reviews of the MMI Fund; analysis by U.S. Department of HUD/FHA.

Two key drivers are behind the actuarial forecast of continuous improvements in the capital ratio. First, premium rates put in place over the last three years are expected to provide greater net resources than did those in place from 1992 to 2010. It was in July 2010 that HUD sought, and Congress authorized, additional flexibilities in premium rate charges. The expected value of today's premium rates, when applied to each new dollar of insurance in FY 2012, is about 7 percent, according to the new actuarial calculations. This is almost double the average collections on loans insured from 1992 to 2010.[15] In combination with key policy changes, such as the enactment of a two-tiered credit-score-and-LTV eligibility rule, these actions are estimated to have bolstered the MMI Fund by more than $20 billion on just the 2009-2012 endorsements. The new FY 2013 cohort just starting to form is projected to add approximately $11 billion in additional economic net worth for the Fund.

7. Fund Performance under Alternative Scenarios (Forward Loans)

The realized economic value of the Fund will vary from the Actuary's estimate if actual drivers of loan performance deviate from base-case projections. This section compares the base-case

[15] These calculations respect the frequency and timing of loan termination events across the life of the cohort, as projected in the base-case scenario. Forecast premium revenues are discounted to calculate a present value as of today.

economic value derived from Monte Carlo simulations with seven alternative scenarios. The base-case of the actuarial study is the mean or average expected economic value of the Fund across 100 randomly generated economic paths. The first five alternative scenarios reviewed here are percentile marks among the Actuary's 100 simulated paths. They correspond to those economic paths that yield the 10th best, 25th best, 25th worst, 10th worst and the singular worst projected economic values.

There are two additional scenarios studied by the Actuary, and we present a comparison of the base-case forecast with those as well. They represent singular, deterministic economic paths with no random fluctuations. First is the Moody's Protracted Slump Scenario, the most stressful alternative scenario forecasted by Moody's Analytics in July 2012. Second is a Low Interest Rate Scenario, representing a continuation of the historically low interest rate environment prevailing at the end of FY 2012. As discussed earlier, the value of the Fund based on the Actuary's model is particularly sensitive to lower-than-anticipated interest rates.

Exhibit II-13a summarizes the comparative results of the seven alternative scenarios.

Exhibit IV–13
Projected MMI Fund Economic Values, Forward Loans
Comparing the Baseline to Seven Alternative Scenarios
($ Millions)

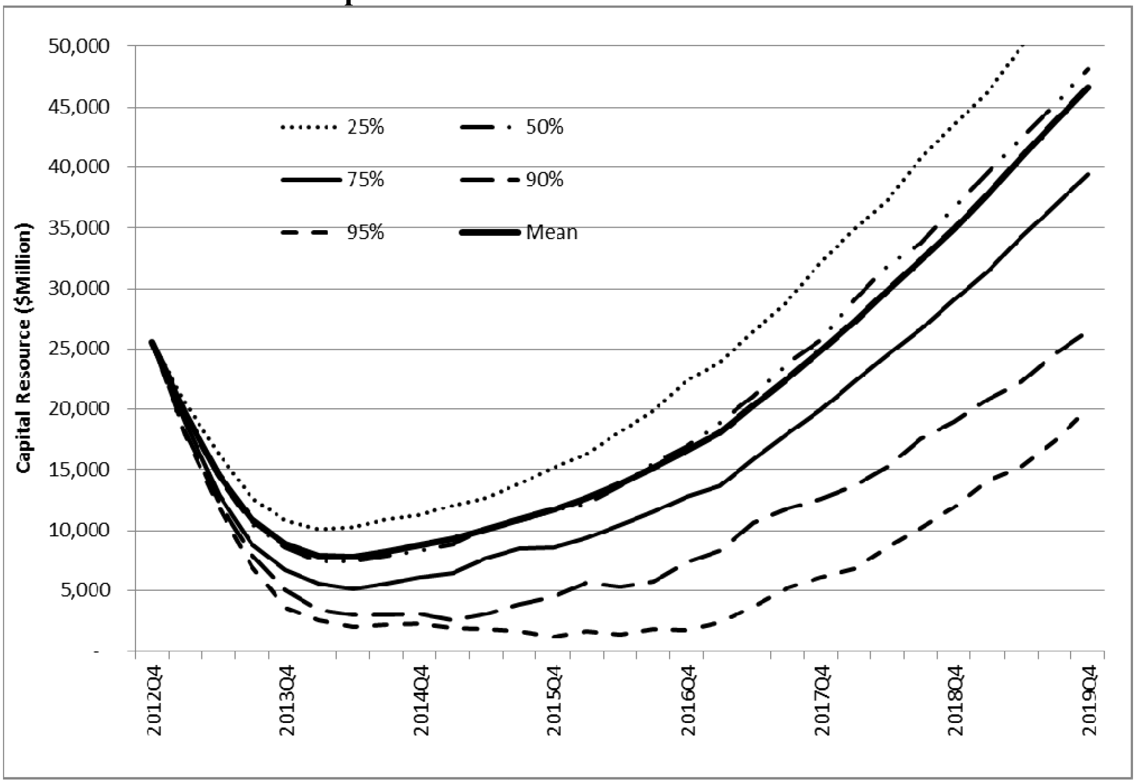
Fiscal Year	Results of Monte Carlo Simulations						Additional Comparisons	
	Baseline	10th Best	25th Best	25th Worst	10th Worst	Worst	Moody's Protracted Slump	Low Interest Rates
2012	-13,478	2,827	-6,126	-19,497	-25,083	-65,305	-65,409	-31,058
2013	-2,585	18,987	2,849	-10,427	-16,617	-59,585	-54,295	-19,332
2014	4,223	30,803	8,273	-5,563	-11,576	-57,502	-42,681	-5,272
2015	11,525	38,095	14,641	829	-4,537	-55,436	-34,603	8,717
2016	20,984	45,974	20,147	8,715	2,318	-53,889	-28,914	16,969
2017	31,352	54,281	26,798	15,403	7,249	-53,456	-23,948	24,002
2018	42,502	62,898	38,815	24,599	14,235	-52,247	-18,331	32,131
2019	54,251	71,711	52,636	38,351	25,105	-49,675	-12,000	41,291

Source: IFE Group, FY2012 Independent Actuarial Reviews of the MMI Fund portfolios, Forward Loans and HECM.

Exhibit IV-14 illustrates the difference between *negative* net economic value and *negative* cash or working-capital position. As described earlier in this section, FHA paid out a record $18 billion in claims in FY 2012, yet net capital resources only declined by $2.8 billion. Cash inflow from ongoing insurance operations covered the balance. That included premium revenue from newly insured loans in FY 2012. As FHA continues to operate, the way in which its financial position will change over time is actually more important than the capital ratio estimate at a point in time. Assuring that new books-of-business are actuarially sound and can contribute net capital resources to bolster Fund finances is of primary importance today, along with limiting potential loss exposure on outstanding loan guarantees.

Exhibit IV-14, which depicts forward loan Capital Resources under various points in the distribution of simulated economic values and includes new insurance endorsements, shows that between cash from operations, cash balances currently in the MMI Fund Financing Accounts, and the Capital Reserve Account balance, FHA would have resources to pay its claims even up to the 95th percentile scenario in the Actuary's simulation analysis. That represents the 5th worst outcome of the 100 random economic paths. To put this in perspective, this scenario projects that forward loans in the Fund, under current policies and premium rates, could lose an additional $42 billion in economic value over time (above and beyond the base case assumption of losses) and still not run out of capital resources.

Exhibit IV-14
Capital Resources under Alternate Scenarios



Source: IFE Group, Actuarial Review of the FHA MMI Fund Forward Loans for Fiscal Year 2012.

8. Reverse Mortgages (HECM)

FHA's reverse mortgage loans, Home Equity Conversion Mortgage (HECM) loans were included in the MMI Fund beginning in 2009 and comprise a significantly smaller share of the total MMI portfolio of loan guarantees ($78 billion compared to $1.05 trillion for forward loans). This year, the independent actuary projects the economic value of the HECM portfolio to be *negative* $2.8 billion, compared to (positive) $1.4 billion last year. This is shown in Exhibit IV-15.

Exhibit IV-15
Actuarial Estimates of the Economic Value of the MMI Fund HECM Portfolio, Comparing 2012 to 2011
(dollars are in billions)

	2012	2011	Difference
Insurance in Force	$ 78.2	$ 68.4	$ 9.8
NPV Future Cash Flows	(7.6)	(2.9)	(4.8)
Add Capital Resources	4.8	4.22	0.6
Economic Value ($bill)	(2.8)	1.4	(4.1)
Economic Value (%)	(3.6%)	2.0%	(5.6%)

Source: Actuarial Review of the FHA MMI Fund HECM Loans for FY 2012; analysis by U.S. Department of HUD/FHA.

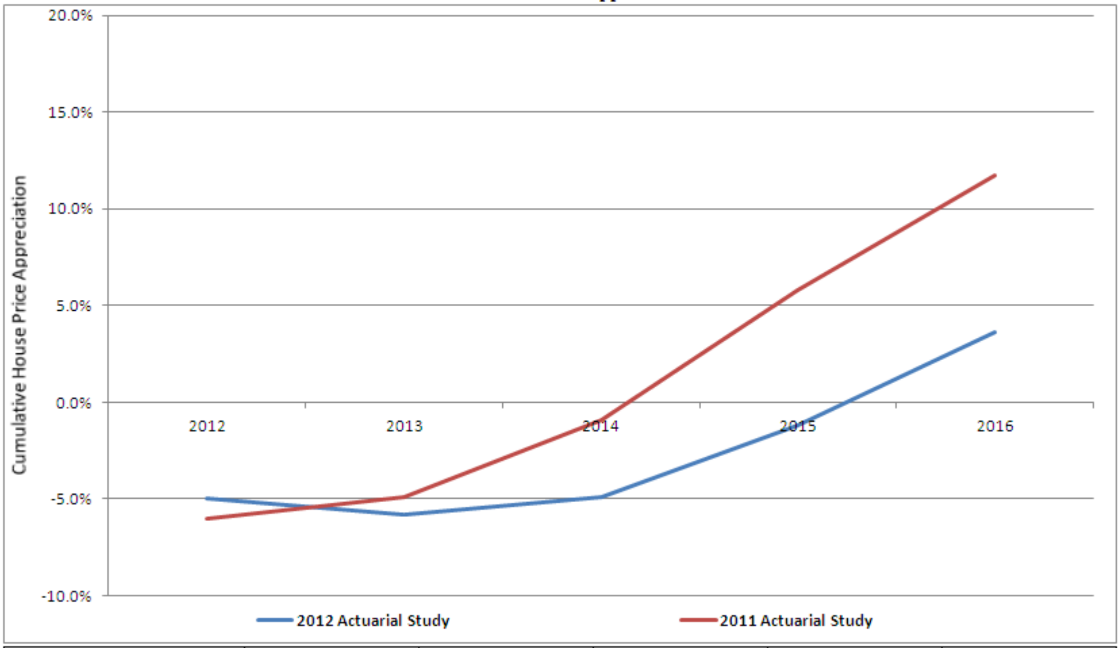
The three major reasons for the year-over-year decline in estimated capital position for HECMs are:

- **Updated mortality and termination speeds:** Expected termination rates are slower than were projected last year, reducing economic value by $1.9 billion. Survivorship beyond year 10, and especially beyond year 15, means a greater chance of loan balances exceeding property values and HUD realizing a loss upon loan termination.

- **Higher rate of property conveyance at termination:** Traditionally, about 70 percent of property sales were handled directly by owners or estate executors. Today, however, about 70 percent of (non-refinance) loan terminations result in the conveyance of properties to HUD. When this happens, FHA incurs transaction costs from the management and marketing of the property. Those sum to around 12 percent of the property value. The new actuarial estimates use a projections model for rates of conveyance as a function of economic conditions. That change reduces the value of the Fund by $1.9 billion.

- **Less optimistic baseline house price appreciation (HPA) rates:** As discussed in the section on forward loans above, the Moody's Analytics July 2012 forecast of house price growth was significantly lower than the projections used in the FY2011 actuarial study. Cumulative growth through the first 5 years of the forecast period are about 9 percentage points lower this year (see Exhibit IV-16), reducing economic value by $0.5 billion. The relative magnitude of impact to the HECM portfolio differs from forward loans as the geographic distributions of the two portfolios differ from one another. In addition, the change in house price forecast has a different effect on HECM loans in that HECM valuation is more dependent upon long-term price trends, whereas forward loan valuations are more influenced by near-term forecasts.

Exhibit IV-16
FHA HECM Portfolio Geographically Weighted
Cumulative House Price Appreciation Rates



	2012	2013	2014	2015	2016
2011 Actuarial Study	-6.0%	-4.9%	-0.9%	5.8%	11.7%
2012 Actuarial Study	-5.0%	-5.8%	-4.9%	-1.2%	3.6%
Cumulative Difference	1.0%	-0.9%	-4.1%	-7.1%	-8.1%

Source: Moody's Analytics, July 2011 and July 2012 forecasts of the FHFA All-Transactions HPI, metropolitan area series; analysis by the U.S. Department of HUD/FHA.

V. Actions Taken to Strengthen the Fund

A. CHANGES TO POLICIES AND PRACTICES MADE TO DATE

Throughout the tenure of this Administration, FHA has taken aggressive and decisive actions to improve the health and trajectory of the MMI Fund, while ensuring continued access to mortgage credit for American families. The changes made to FHA policy since 2009 (see Appendix A for full list of changes) are projected to have improved the economic value of the Fund by at least $20 billion. That FHA's capital ratio has remained positive until this time is only due to the reforms to risk management, credit policy, lender enforcement, and consumer protections made over the past four years – the most sweeping changes to policy in FHA's nearly 80 year history. The loans made during this Administration remain the most profitable in agency's history. As a result, we have been able to continue providing access to homeownership for millions of American families while managing the challenging problems of loans impacted by the severe recession – particularly those insured between 2007-2009 – that are still on FHA's books. In filling the void left by the severe constriction in private lending, FHA has contributed significantly to bringing the housing market from the brink of collapse where it is positive and growing again.

B. PLANNED ACTIONS TO FURTHER STRENGTHEN THE FUND

While FHA has enacted substantial reforms under the current Administration, this year's actuarial review makes clear that loans made prior to and at the outset of the recent crisis continue to weigh heavily on the health of the MMI Fund. Therefore, building upon the significant efforts already undertaken to protect and preserve the MMI Fund, FHA will also pursue a series of additional actions to continue improving the Fund's trajectory over both the short and long term. Collectively, these changes are projected to provide billions of economic value for the MMI Fund in FY 2013.

1. Reduce Losses from Legacy Books of Business

The changes made since 2009 to FHA's lender oversight, credit policies, and premium pricing have yielded substantial improvements in the quality of new loans endorsed by FHA. But significant opportunity remains to reduce the impact on the Fund of poorly performing legacy loans severely impacted by the recession, and to provide greater assistance for distressed borrowers as they seek to recover and find meaningful assistance in dealing with their delinquent loans. With a majority of FHA's projected losses attributable to loans insured from 2007-2009, FHA will take several additional steps to maximize recovery in the areas of loss mitigation and asset management.

The Actuary projects nearly $60 billion in claims costs for FHA from seriously delinquent loans that will go to claim by the end of FY 2014, largely arising from loans insured between 2007 and 2009. As a result, reducing the severity of losses derived from these loans will exert a noticeable impact to Fund performance over the next few years. Throughout the past fiscal year, FHA has been executing on an overall asset management strategy aimed at ramping up REO alternatives. REO alternatives (primarily short sales) comprised about 15%-20% of total dispositions since

2010, yielding average loss severities about 20% lower than REO. In recent months, FHA also unveiled its Distressed Asset Stabilization Program (DASP), another promising REO alternative. These and other actions have had a measurable effect, as loss severities have already fallen by 9% in the last year. A further reduction in loss severity from approximately 66% to 61% would decrease the net loss experienced by FHA on expected claims from $38.8 billion to $35.8 billion, a savings of $3 billion. Therefore, starting in FY 2013, FHA will take a number of additional steps to improve loss severities associated with defaulted FHA-insured loans.

a. Re-design of FHA Modification Treatments to Better Assist Delinquent Homeowners

FHA will seek to minimize losses to the Fund by establishing revised standards for repayment plans, standard modifications, and FHA-HAMP loss mitigation products. FHA loss mitigation policies will be geared towards greater payment relief for borrowers, targeting payment reductions of at least 20% for FHA-HAMP modifications, which will result in more sustainable payment outcomes for borrowers over the long term. This approach will yield lower claim costs for FHA while also reducing prepayment speeds for insured loans, both of which will positively impact the MMI Fund.

b. Streamlining of the FHA Short-sale Policy

Although FHA is deeply committed to providing loss mitigation alternatives to borrowers which permit them to retain their homes, home retention is simply not an option for some borrowers. For these borrowers, pre-foreclosure sales (short-sales) offer an opportunity for a "graceful exit" from their property that many borrowers deem preferable to foreclosure. FHA will introduce a streamlined pre-foreclosure sale policy which removes certain barriers for borrowers in obtaining a short sale on their FHA-insured mortgage. This change is expected to increase the number of defaulted loans that end in short sales rather than foreclosures. Because losses from short-sales are substantially lower than from the traditional FHA REO process, the shift of greater numbers of distressed homeowners to short-sale dispositions rather than foreclosures will yield better results for the MMI Fund while allowing distressed borrowers to start anew without having to go through the difficult and costly foreclosure process.

c. **Expansion of the Claim without Conveyance Pilot Program**

FHA has conducted a pilot whereby properties secured by non-performing FHA-insured loans are offered for sale by the lender who has completed the foreclosure process. At a reserve price slightly below the outstanding unpaid principal balance of the loan, the properties are sold to third party purchasers without ever being conveyed to FHA. FHA's analysis has shown that this method of disposing of these properties yielded lower losses for the MMI Fund than selling them through FHA's normal REO disposition process, as carrying costs associated with preserving, managing, and marketing an REO property were eliminated. FHA has successfully piloted this program for over 12 months and has had success in select markets. FHA intends to expand the program and manage the reserve price to levels appropriate to market conditions for those locations where recoveries are substantially lower than the national average.

d. Proactive Strategies to Further Improve Recoveries

In addition to the policy and programmatic changes outlined above, FHA will also take several innovative and proactive steps to increase utilization of loss mitigation options and reduce unnecessary asset disposition losses. First, beginning in 2013, FHA will launch a large-scale proactive marketing campaign to promote modification and short-sale strategies for delinquent borrowers. This effort is expected to increase utilization of these programs, which will permit more borrowers to become aware of and take advantage of these opportunities, while reducing foreclosures and decreasing associated losses for FHA. In addition, FHA will also pursue more creative strategies to dispose of REO properties in geographies where traditional asset disposition methods yield net negative recoveries for FHA. This approach will both save money for FHA on unnecessary losses as well as contribute to community stabilization initiatives in cities hit hard by the recession.

2) Further Strengthen the Quality and Impact of New Endorsements

While much has been done under the current Administration to improve the performance and revenue of new FHA endorsements, there are further opportunities to strengthen new books to ensure the long term health of the MMI Fund. In the second quarter of FY 2013, FHA will implement the following policies for new originations.

a. Revised Premium Cancellation Policy

Under a policy change made in 2001, FHA has been cancelling required mortgage insurance premiums (MIPs) on loans for which the outstanding principal balance reaches less than 78% of the original principal balance. However, FHA remains responsible for insuring 100% of the unpaid principal balance of a loan for the entire life of the loan, such loan life often extending far beyond the cessation of MIP payments. As written, the timing of MIP cancellation is directly tied to the contract mortgage rate, not to the actual loan LTV. The current policy was put in place at a time when it was assumed that home price values would not decline, but today we know that LTV measured by appraised value in a declining market can mean that actual LTVs are far lower than amortized mortgage LTV, resulting in higher losses for FHA on defaulted loans. Analyses conducted by FHA's Office of Risk Management projects lost revenue of approximately $10 billion in the 2010-2012 vintages as a result of the current cancellation policy. The same analyses also suggest that 10%-12% of all claims losses will occur after MIP cancellation. Therefore, beginning with new loans endorsed after the policy change becomes effective later in FY 2013, FHA will once again collect premiums on FHA loans for the entire period during which they are insured, permitting FHA to retain significant revenue that is currently being forfeited prematurely.

b. MIP Increase

Consistent with FHA's continued efforts to balance its countercyclical role in the nation's mortgage market with its responsibility to manage the Fund, FHA will increase annual mortgage insurance premiums by an additional 10 basis points. While the new loans being made today are profitable to FHA and we do not want to over-burden or constrict access to credit as the housing market continues to mend, we also must to ensure that we are 1) rebuilding adequate reserves for the future and 2) phasing out of our counter-cyclical role by reducing FHA's footprint in the marketplace and helping to facilitate the return of private capital. FHA has played a vital part in ensuring access to credit for borrowers and liquidity in the market, yet its current outsized role should and will decrease. Indeed, its market share has declined yearly since a peak in 2009. This premium increase –$13 per month for the average FHA borrower – which FHA will enact in 2013 will add significant revenue to the Fund and ensure that FHA does not take on additional market share, while at the same time being modest enough that it doesn't impact borrower access to credit or threaten our emerging housing recovery.

c. Future Credit Policy and Pricing Changes

While much has already been done to improve the quality of new FHA endorsements, the effectiveness of which are clear in the performance and projected value of loan cohorts insured since 2010, FHA is continually evaluating its portfolio to identify and mitigate risks, and to provide enhancements that benefit both consumers and the Fund. Based upon these evaluations, FHA is also developing additional proposals which will further assist in strengthening the MMI Fund. More details will be provided when these policies are announced in the coming months.

d. Housing Counseling Incentive Policy

Significant evidence has shown that housing counseling improves the success of home buyers – particularly first time homebuyers. FHA intends to develop new policies which incentivize, or in some cases require, borrowers to complete a pre-purchase housing counseling program prior to the purchase of a home using FHA-insured financing. We will work during this fiscal year to craft and receive feedback on the precise contours of this initiative. This endeavor will ultimately improve outcomes for both borrowers and FHA, reducing losses to the Fund as higher numbers of new borrowers attain successful home purchases.

3) Stabilize and Strengthen the HECM Program

Changes in borrower utilization of the HECM program and the modeling changes employed by the actuary this year show substantial stress in the HECM program. In order to mitigate the negative impact of the 2013 ad future HECM books on the MMI Fund, FHA is taking aggressive actions in both the near and long terms to ensure that consumers are better protected and able to sustain their reverse mortgage, while also protecting the Fund.

a. Immediate Steps to Reduce Losses in the Near Term

Given current regulatory authority, FHA has limited ability to address root cause issues and will, therefore, be forced to make blunt changes to the program. FHA will take immediate action to reduce the amount borrowers are permitted to draw at the time of origination of their HECM loan and better align the program with its objective of enabling seniors to age-in-place. These changes will protect FHA from losses and reduce the likelihood of borrower defaults due to nonpayment of property taxes and insurance.

In addition, FHA will consolidate the Fixed Rate Standard program with the Fixed Rate HECM Saver product, resulting in a reduction of the maximum amount of funds available to a HECM borrower. Further, the principal limit factors that are used to determine the maximum amount a homeowner may borrow using the remaining HECM products will be reduced across the board (i.e. Fixed/ARM Saver, ARM Standard).

Additionally, in an effort to reduce losses associated with the conveyance and disposition of properties mortgaged with a HECM, FHA will issue new incentives for estate executors of HECM borrowers to dispose of properties themselves rather than conveying them to HUD. Executors are permitted to either sell such properties or convey them to HUD. Reversing the historical trend, over the past few years, larger numbers of executors have been choosing to convey these properties to FHA rather than sell them, adding costs and reducing recoveries for FHA. By incentivizing the sale of properties by executors, FHA is able to avoid property management, maintenance, and marketing costs associated with the REO disposition process, thereby reducing losses to the Fund on these properties.

b. Longer-term Changes to Permanently Strengthen the Program

Over a longer term, either through the granting of the legislative authority described below or via the much longer rule making process, FHA will also pursue other material changes to ensure the long-term viability of the HECM program. These measures include:

- Limiting the draw at origination to mandatory obligations (i.e. closing costs, mortgage liens and federal debt), providing greater flexibility in addressing the individual needs of borrowers than the across-the-board reductions to principal limit factors described above, while still protecting the Fund from losses on loans where the maximum loan amount is drawn up-front;
- Performing a financial assessment of borrowers as a basis for loan approval and determining the suitability of various HECM products to protect consumers from acquiring loans not fit for their situation; and
- Establishing a tax and insurance set-aside to ensure sufficient equity or an annuity is available to pay taxes and insurance on the mortgaged property so that defaults resulting from nonpayment of taxes and insurance can be avoided.

4) Obtain Additional Statutory Authority to Strengthen FHA

In addition to the administrative actions outlined above which FHA will implement under its existing authorities, HUD is also calling upon Congress to act on a series of proposals that will further enhance FHA's capabilities to manage risk and protect the MMI Fund. The proposals outlined below will enhance FHA's ability to hold lenders accountable for non-compliance with FHA policy and provide greater flexibility for FHA to make changes to policies and procedures as emerging needs and trends are identified. As a result, FHA will better be able to avoid unnecessary losses before they occur.

a. **Indemnification Authority for Direct Endorsement Lenders:** This provision, which FHA has been seeking since 2010, would allow FHA to seek indemnification from Direct Endorsement lenders, which represent 70% of all FHA approved lenders. Currently FHA only has authority to require indemnification for lenders with Lender Insurance (LI) approval. In granting this authority, FHA will be able to obtain indemnification from all of its approved lenders for loans that do not comply with its guidelines.

b. **Revised Indemnification Authority**: This change would eliminate the "knew or should have known" standard with regard to fraud or misrepresentation. While the Government-Sponsored Enterprises require lenders to retain all fraud related risk, FHA only holds lenders accountable for fraudulent activity if they "knew or should have known" of its occurrence. Providing proof to meet this standard limits FHA's ability to require lenders to be accountable for fraud in FHA-insured loans, and its removal would significantly improve FHA's ability to avoid unnecessary losses arising from fraudulent activity.

c. **Authority to Terminate Origination and Underwriting Approval:** This legislation would give FHA enhanced ability to review lender performance and, if a lender is found to have an excessive rate of early defaults or claims, would provide greater flexibility in terminating the approval of the lender to originate or underwrite single family mortgages for FHA insurance. FHA has been seeking this authority since 2010.

d. **Revised Compare Ratio Requirement:** This provision would revise the statute governing the Credit Watch Termination Initiative to provide greater flexibility in establishing the metric by which FHA compares lender performance so that it more effectively captures the true performance of a lender during all market conditions, minimizing further poor performance by FHA lenders while reducing uncertainty for them. Specifically, this legislation would allow the Secretary to compare the rate of early defaults and claims for insured single family mortgage loans originated or underwritten by a lender with those same rates for other lenders on any basis the Secretary determines appropriate, such as geographic area, varying underwriting standards, or populations served. Further, the provision would permit the Secretary to implement such comparisons via regulations, notice, or Mortgagee Letter.

e. **Authority to Transfer Servicing:** In order to facilitate more effective loss mitigation, this change would give FHA the authority to require any of the following actions when a servicer is at or below a servicer tier ranking score (TRS) of III, or when the Secretary deems the action necessary to protect the interests of the MMI Fund: (1) transfer servicing from the current servicer to a specialty servicer designated by FHA; (2) require a servicer to enter into a sub-servicing arrangement with an entity identified by FHA; and/or (3) require a servicer to engage a third-party contractor to assist in some aspect of loss mitigation (e.g. borrower outreach). Such authority would permit FHA to better avoid losses arising from poor servicing of FHA-insured loans, yielding better results for both borrowers and FHA.

f. **Authority to Manage the HECM Program by Mortgagee Letter:** This provision would allow FHA to take specific actions via Mortgagee Letter to more effectively manage the HECM program. In light of the HECM portfolio's sensitivity to changing market conditions, this change would provide FHA with the flexibility to make necessary changes as soon as trends or issues are identified within the HECM program.

VI. Conclusion

The findings of the 2012 actuarial study indicate that FHA continues to face stress from legacy books of business insured prior to 2010, while books insured since that time exhibit increasingly positive characteristics. As a result of economic forecasts which project slower house price appreciation and lower interest rates than were forecasted last year, coupled with refinements to modeling changes on outcomes for defaulted loans, the outlook for the expected performance of legacy books of business has again worsened over the past year.

However, the report also confirms that the steps FHA has taken since the start of this Administration have been both necessary and effective. This can be seen in the significantly improved performance of more recent vintages of insured loans. As this report shows, performance for the FY 2010 through FY 2012 books of business is far superior to those originated in FY 2009 and prior. Prudent credit policy and pricing changes have bolstered the fund by adding more than $20 billion in economic value from 2010 through 2012. The 2012 vintage is predicted to have the highest credit and pricing quality in FHA's history.

Although the changes FHA has made have substantially improved the long term health of the MMI Fund, there is still more work to be done. Going forward, FHA will to continue to work to strengthen the Fund by further refining its risk and asset management strategies and credit and pricing policies. This report has laid out a comprehensive set of proposals to achieve all of these initiatives. FHA will continue to focus on increasing its capital resources while at the same time supporting the fragile housing market recovery. FHA is committed to emerging from this crisis financially stronger than it was before so that it can continue its nearly 80-year mission of providing access to homeownership for qualified, low-to-moderate income, underserved and first time homebuyers.

VII. Appendix A: Summary of FHA Policy Changes under the Current Administration

1. **Changes implemented via mortgagee letter with an implementation date of January 1, 2010:**
    a. Modifications to streamline refinance documentation requirements
    b. New appraisal standards
    c. Submission of audited financial statements required for supervised lenders

2. **Mortgage insurance premium (MIP) increase and adjustments to upfront/annual MIP relationship**
    a. 1/12/2010 – Increased Upfront MIP to 2.25%
    b. 10/4/2010 –
        i. Lowered up front MIP to 1%
        ii. Raised annual MIP to 85 to 90 basis points
    c. 4/18/2011 – Increased annual MIP by 25 basis points
    d. 4/9/2012 –
        i. Increased upfront MIP from 1% to 1.75%
        ii. Increased annual MIP by 10 basis points
    e. 6/11/2012 – Increased annual MIP for loans in excess of $625,500 by 25 basis points

3. **New downpayment/credit score requirements**
    a. Mortgagee Letter effective October 4, 2010
        i. Loans to borrowers with a FICO of 579 or lower require a minimum 10% downpayment
        ii. Loans to borrowers with a FICO of 580 or above require current minimum 3.5% downpayment
        iii. Minimum FICO of 500

4. **Enhanced underwriting requirements**
    a. Mortgagee Letter effective April 1, 2012
        i. Updated documentation requirements for self-employed borrowers
        ii. Offered new guidance on disputed accounts
        iii. Expanded the definition of family members for identity of interest transactions

5. **Changes to the HECM Program**
    a. Mortgagee Letter effective October 4, 2010
        i. Introduced HECM Saver, which provides a lower upfront premium (.01%) and a lower max principal limit
        ii. Increased annual MIP to 1.25%
        iii. Adjusted the HECM Principal Limit Factors, resulting in lower maximum principal limits
    b. Mortgagee Letter published January 3, 2011

i. Provided detailed guidance regarding the property charge loss mitigation requirements for HECM loans

6. **Increased enforcement for FHA-approved lenders**
    a. Enforcement actions taken against lenders
        i. Heightened enforcement of HUD requirements for FHA-approved lenders has yielded over:
            1. 1,600 lenders withdrawn from FHA's program as a result of violations of FHA approval, origination, or servicing requirements.
            2. Imposition of more than $13.8 million dollars in civil money penalties and administrative payments for FHA-approved lenders
    b. Mortgagee Letter effective January 21, 2010
        i. Enhanced monitoring of lender performance and compliance with FHA guidelines and standards.
        ii. Expanded the Credit Watch Termination Initiative to include evaluation of lender underwriting performance in addition to origination performance
    c. Implementation of statutory authority through regulation of section 256 of the National Housing Act to enforce indemnification provisions for lender's using delegated insuring process
        i. Final rule published January 25, 2012, with an effective date of February 24, 2012
        ii. A Mortgagee letter and Lender Insurance guide will soon be issued to implement this new rule.
    d. Additional authority sought by FHA through legislation:
        i. Amendment of section 256 of the National Housing Act to apply indemnification provisions to all Direct Endorsement lenders. This would require all approved underwriting mortgagees to assume liability for all of the loans that they underwrite
        ii. Legislative authority permitting HUD maximum flexibility to establish separate "areas" for purposes of review and termination under the Credit Watch initiative. This would provide authority to withdraw originating and underwriting approval for a lender nationwide or in a specific area on the basis of the performance of its regional branches

7. **Changes to FHA lender approval requirements**
    a. Final rule published week of April 20, 2010
        i. Increased net worth requirements for approved mortgagees. All new lender applicants for FHA programs must possess a minimum net worth of $1 million. Effective one year from enactment of the rule, current FHA approved lenders, with the exception of small businesses, must possess a minimum net worth of $1 million. Current FHA-approved small business lenders must possess a minimum net worth of $500,000. Effective three years after enactment of the rule,

approved lenders and applicants to FHA single-family programs, regardless of size, must have a net worth of $1 million plus 1% of total loan volume in excess of $25 million
   ii. Eliminated independent FHA approval of mortgage brokers who originate but do not underwrite loans. FHA-approved mortgagees who underwrite loans retain strict liability for all loans, regardless of origination via their retail operations or through their sponsored mortgage brokers
   iii. Codified requirements for submission of audited financial statements by supervised mortgagees
b. Mortgagee Letter published on January 5, 2011
   i. Required mortgagees that possess NMLS IDs to provide those to FHA for both lender approval and loan origination processes
c. Mortgagee Letter effective July 28, 2011, provided alternative financial reporting requirements for small supervised lenders to decrease burdens associated with FHA's lender approval and renewal processes

8. Updated Quality Control Requirements for Direct Endorsement Lenders
a. Mortgagee Letter effective January 5, 2011
   i. Updated FHA's quality control requirements to include new requirements related to Sponsored Third Party Originators, reporting of fraud and material deficiencies, and recording of sales or transfers of FHA mortgages

9. Refinance Program Policy
a. Mortgagee Letter published February 14, 2011
   i. Extensive guidance regarding requirements and changes for FHA Standard and Streamlined refinance programs
b. Mortgagee Letter published March 6, 2012
   i. For borrowers who are current on their loans, FHA reduced the upfront and annual MIPs for Streamline refinances of FHA-insured loans endorsed on or before May 31, 2009 to permit these borrowers to take advantage of historically low interest rates, reducing their payments and decreasing risk to FHA

10. Consolidated and updated FHA condominium policy
a. Mortgagee Letter issued June 30, 2011, and effective August 29, 2011
   i. Consolidate guidelines published in 2009;
   ii. Provide a single source of information for the Condominium Approval and Recertification Process;
   iii. Update, consolidate and clarify existing condominium policy guidance; and
   iv. Expand FHA's flexibility to consider exceptions at the individual project level
b. Mortgagee Letter to be issued in summer 2012 to revise updated guidance

11. Reduction in allowable seller concessions

a. Proposed policy change published in June of 2010
    i. Received over 1,000 comments, prompting extensive additional analysis which led to substantial revisions to the rule
    ii. New proposed rule published February 23, 2012

12. Enhanced and expanded loan sale program

a. Effective with the quarterly sale that took place in September 2012, FHA expanded the 601 Note Sales Program, now known as the Distressed Asset Stabilization Program, providing the opportunity for better outcomes for borrowers, communities and FHA on non-performing loans.