ACCESS

BLUEPRINT

What **FHA** is **Doing** to Expand Access to Mortgage Credit for Underserved Borrowers

BLUEPRINT for ACCESS

Qualified Borrowers Are Underserved

The economic crisis significantly constrained credit making it tough for anyone with less than perfect credit to obtain a mortgage.

According to the Urban Institute, the average credit score for loans sold to the GSEs is 752. According to Equifax and Moody's, there are currently 13 million people with credit scores ranging from 580 to 640. Shutting these consumers out of the market hurts families and undermines our efforts to build more stable communities, create pathways to the middle class, and increase homeownership opportunities for minority and low-wealth borrowers.

A healthy mortgage market serves all qualified borrowers. FHA is committed to finding ways to responsibly increase access for underserved borrowers.

Principles to Responsibly Expand Access

To increase access, we must identify and implement responsible ways for creditworthy borrowers to obtain mortgage credit. This includes:

- **Encouraging Housing Counseling**
  Responsible access can be enhanced by ensuring borrowers are well-educated about the home- buying and mortgage finance process.

- **Establishing Clear Rules of the Road**
  Lenders must be able to quantify the risk of making a mortgage loan. Taking steps to establish clear quality assurance policies helps ensure lenders can make loans without fear of unanticipated consequences.

- **Avoiding Unsound Lending Practices**
  Facilitating access does not mean returning to the days of unsound lending practices. It means building on the reforms already implemented that support safe lending practices.

It's Time for Action

At FHA, we are turning the principles for expanding access into ACTION. Through Homeowners Armed with Knowledge (HAWK) and Quality Assurance initiatives, we are taking a targeted approach to expanding access and affordability while pushing back on the notion that is impossible to manage risk and enhance access at the same time.

Homeowners Armed with Knowledge (HAWK)

Housing Counseling works. Research shows a strong correlation between housing counseling and mortgage performance. Delinquency rates for borrowers who have received counseling are 29 % lower for first-time homebuyers and 15% lower overall. Consumers who participate in housing counseling get individualized, objective advice on understanding the rights and responsibilities of homeownership, addressing credit and savings barriers, and meeting their overall housing and financial goals.

Recognizing the impact housing counseling can have on increasing the pool of responsible borrowers while reducing risk to the FHA fund, we are implementing an initiative—HOMEOWNERS ARMED WITH KNOWLEDGE (HAWK)—that will encourage much wider use of housing counseling. Through HAWK, FHA is helping to make responsible homeownership available and sustainable for families. HAWK for New Homebuyers will help increase access to credit for first-time homebuyers underserved by the current mortgage market.

Under the four-year pilot program, homebuyers who commit to housing counseling will qualify for tangible savings on their FHA-insured loans. FHA proposes that Homeowners who complete housing counseling before signing a contract to purchase a home and who complete additional pre-closing housing counseling will receive a 50 basis point reduction in the upfront FHA mortgage insurance premium (MIP) and a 10 basis point reduction in the annual FHA MIP. Choosing to participate in post-closing counseling and a track record of timely mortgage payments will bring even greater benefits. After two years with no serious delinquencies, participants receive an additional 15 basis point reduction in annual MIP.

On the average FHA loan balance of $180,000, these reductions can add up to nearly $9,800 in savings over the life of the loan. All of the details of the HAWK for New Home Buyers pilot program will open to comment as part of Federal Register Notice so the final MIP reductions may change based on those comments.

The HAWK program is a strong step toward integrating housing counseling into the home buying process and ensuring broad access to housing counseling services. And HAWK helps make FHA loans more affordable to first-time homebuyers, building a better foundation for middle-class homeownership.

Quality Assurance

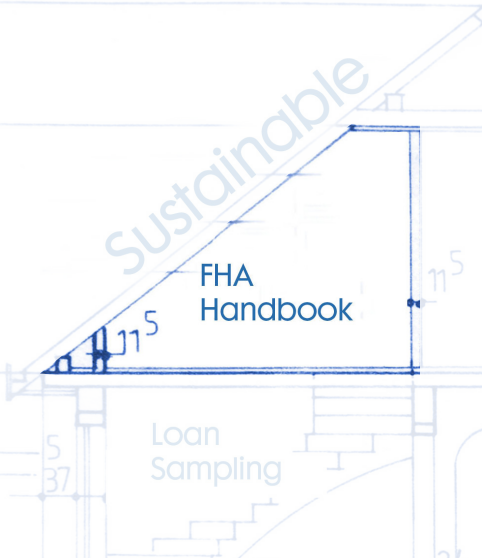
What is quality assurance? For FHA, it is making sure every loan is originated according to our credit guidelines. Why is quality assurance important? Good quality assurance processes enhance access for potential borrowers because lenders can originate loans confidently—knowing their mortgages meet FHA standards. This is especially important in the current environment where lenders are adding credit overlays, restricting who qualifies for FHA mortgages. Lenders tell us they add credit overlays for a variety of reasons. Fear of back-end enforcement actions is often cited.

That is why we are making important enhancements to our quality assurance processes. We want to work with lenders to provide clarity and transparency in FHA's policies to encourage lending to qualified borrowers across the credit spectrum. We believe changing the way in which we provide policy direction and monitor lender compliance and performance better protects FHA and reduces uncertainty for lenders in their interactions with HUD. Our initial efforts are paying-off as some lenders are already beginning to reduce credit overlays.

As more lenders move in this direction, we want to create a policy and quality assurance framework that ensures that underwriting quality and compliance with FHA's requirements sufficiently protect FHA from manufacturing risk. Under this framework, FHA is focusing on four areas: clarifying policy, enhancing our approach to assessing loan quality, sampling a larger variety of loans, and supplementing our lender performance metrics.

Clarifying Policy—The New FHA Handbook

One initiative undertaken by FHA has been the reconciliation of more than 900 mortgagee letters and other policy guidance into a single, authoritative document that will serve as the definitive guide on all aspects of FHA's Single Family programs. In October 2013, FHA posted the first section, Application through Endorsement, of the new Handbook for feedback. Throughout 2014, FHA will publish several other sections of the handbook, including Doing Business with FHA, Oversight and Compliance, guidance for Appraisers, Condominium policies, and Servicing.



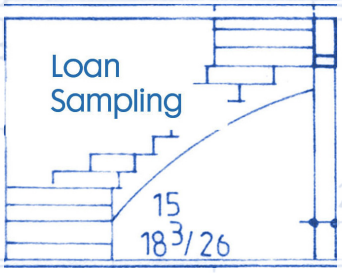
Our goal with the new Handbook is to establish clear, consistent policies and guidelines that make it easier for lenders to follow our guidance, enhancing their ability to confidently originate loans for a larger number of FHA-eligible borrowers.

Loan Quality Assessment

FHA is developing a new methodology for evaluating underwriting defects. The new criteria will be more descriptive—identifying a limited number of specific defects, their related causes, and levels of severity. Categorizing loan defect severity levels simplifies the compliance process as it allows lenders to better assess the risk posed by a specific deficiency. Additionally, assessing the quality of loans under this framework will allow lenders to more easily address the root causes of defects.

Loan Sampling

Currently, FHA primarily selects higher-risk loans for review, e.g. loans evidencing payment challenges. FHA recognizes that this risk-based approach does not accurately reflect a lenders overall underwriting quality as it is primarily focused on non-performing loans. Going forward, we plan to expand our evaluation of loans to include random sampling of performing loans closer to the time of endorsement. This approach provides a more balanced view of underwriting quality.



Lender Performance Management

FHA currently calculates a Lender Compare Ratio for all lenders. This ratio is geographically based, comparing the rate of early defaults and claims for single family loans in a geographic area to other mortgagees in the same area.

FHA plans to introduce an additional national lender performance metric. This new Supplemental Performance Metric will assess lender performance based on the lender's default rate within three credit score bands and compare it to an FHA target rate, rather than to the lender's peers. Like the Compare Ratio, the new metric will be reported in Neighborhood Watch. Introduction of the new performance metric, along with existing metrics and standards, will provide a more comprehensive assessment of lender performance. The draft Supplemental Performance Metric will be posted for review and feedback at Single Family Housing's Policy "Drafting Table" on HUD's website before being more formally implemented.

GETTING THERE: THE ACCESS TIMELINE[1]

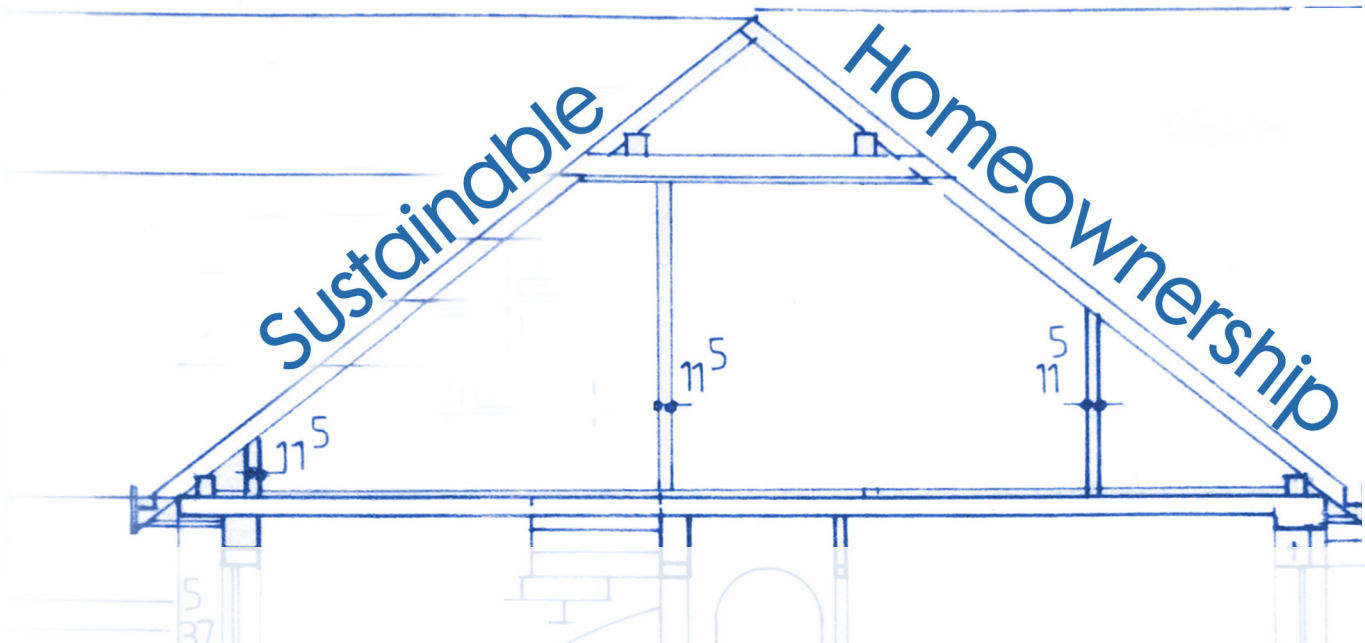
SUMMER 2014

- **HAWK**
  - o Publish Federal Register (FR) Notice
  - o Publish Mortgagee Letter, Housing Notice, and Final FR Notice
- **Quality Assurance Framework**
  - o Loan Defect Taxonomy Stakeholder Engagement
  - o Post Lender Performance Metric[2]
- **FHA Handbook[3]**
  - o Post For Feedback: Doing Business with FHA and Oversight and Compliance Sections
  - o Post For Feedback: Appraiser, Condominiums, and 203K Sections
  - o Publish: Application-Endorsement (Origination) Section

FALL 2014

- **HAWK**
  - o Implement Phase One of HAWK Pilot Project
- **Quality Assurance Framework**
  - o Loan Defect Taxonomy Preview
- **FHA Handbook**
  - o Post For Feedback Servicing and Loss Mitigation Sections

[1]Many of these proposals are included in the President's budget. Implementation timelines may be impacted by passage of the budget and available resources.
[2]The Lender Performance Metric will be posted on the FHA drafting table
[3]All Handbook sections will be posted on the FHA drafting table



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