



Notice: Request for Comment

July 27, 2010

**DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
[Docket No. FR-5404-N-01]**

Federal Housing Administration Risk Management Initiatives: Reduction of Seller Concessions and New Loan-to-Value and Credit Score Requirements

Background and Summary:

Established by Congress in 1934 as a governmental mortgage insurance company, the Federal Housing Administration (FHA) protects mortgage lenders from risk of loss, thereby enabling them to extend credit to homeowners and homebuyers. Over the last 2 years, the volume of FHA insurance increased rapidly as private sources of mortgage finance retreated from the market. FHA's share of the single-family mortgage market today is approximately 30 percent—up from 3 percent in 2007, and the dollar volume of insurance written has jumped from the \$56 billion issued in 2007 to more than \$300 billion in 2009. Accordingly, the Mutual Mortgage Insurance Fund (MMIF) capital ratio has fallen below its statutorily mandated threshold.

Consistent with HUD's responsibility under the National Housing Act to ensure that the MMIF remains financially sound, the notice solicits public comment on three proposed initiatives that will contribute to the restoration of the MMIF capital reserve account. The changes proposed in the notice are designed to preserve both the historical role of the FHA in providing a home financing vehicle during periods of economic volatility and HUD's social mission of helping underserved borrowers. FHA proposes to tighten only those portions of its underwriting guidelines that have been found to present an excessive level of risk to both homeowners and FHA.

FHA Proposes to:

- 1) Introduce a minimum credit score for eligibility, as well as reduce the maximum loan-to-value ratio (LTV) for borrowers with lower credit scores.
- 2) Reduce the amount of closing costs a seller (or other interested party) may pay on behalf of a homebuyer financing the purchase of a home with FHA mortgage insurance.
- 3) Tighten underwriting standards for mortgage loans that are manually underwritten.

How to submit comments:

Please submit your comment letter by **August 16, 2010** through the League at regcomments@ncleague.org. Your response will be forwarded to HUD. Please address your letter to the Regulations Division, Office of General Counsel, Department of Housing and Urban Development, 451 7th Street, SW., Room 10276, Washington, DC 20410–0500.

If you have any questions, please contact [Lauren Whaley](#), the League’s Director of Legislative and Regulatory Affairs at 800-822-8859, ext 3205.

Proposed Changes:

These initiatives are intended to reduce the risk to, and assist in the return of, FHA’s MMIF capital ratio to its mandated threshold. In addition, the initiatives will help to continue FHA’s traditional role as a stabilizing force in the housing market during troubled economic times and remain a source of mortgage credit for low- and moderate income homebuyers.

Credit Scores – Borrowers with credit scores of less than 500 would no longer qualify for FHA loans. Those with scores between 500 and 579 would be required to make a minimum 10 percent down payment. Currently, there is no overall minimum credit score requirement, although those with scores under 500 must make the minimum 10 percent down payment. Maximum FHA-insured financing (96.5 percent LTV for purchase transactions and 97.75 percent LTV for rate and term refinance transactions) would be available only to borrowers with credit scores at or above 580.

- What will be the impact of the new credit score requirements?
- Will this pose problems for credit unions that may not use scores in their underwriting process?
- The scores outlined in the proposal refer to FICO scores. What should the numerical requirements be for other credit scoring systems that you may use?

Maximum Seller Concessions – The amount of the buyer’s closing costs that may be paid by the seller would be reduced from 6 percent to 3 percent of the lesser of the sales price or appraised value. Concessions that exceed FHA’s 3 percent cap would be required to result in a dollar-for-dollar reduction in the sales price for the purpose of calculating the maximum FHA loan amount. Included in the proposal is a table showing that borrowers who received more than 3 percent in seller concessions had a significantly higher risk of losing their homes.

- Do you have any comments with regard to the decrease in the maximum permitted seller concessions?

Underwriting Standards for Manually Underwritten Loans – FHA loans may be manually underwritten in certain situations, such as when the borrower has a very limited or nontraditional credit history, a credit score may not have been issued by the credit bureau, or when the credit score is based on limited information. In these situations, the proposal would require consideration of the borrower’s credit history, LTV and debt-to-income (DTI) ratios.

On *all* manually underwritten mortgage loans, borrowers will be required to have minimum cash reserves equal to one monthly mortgage payment, which includes principal, interest, taxes, and insurance(s).

Maximum LTV and DTI ratios will be set at 31 percent and 43 percent, respectively.

Borrowers with credit scores above 620 or higher may exceed the qualifying ratios of 31/43 percent, not to exceed 35/45 percent provided that they are able to meet at least one of the compensating factors listed in the proposal. To exceed the qualifying ratios of 35/45 percent, not to exceed 37/47 percent, borrowers must meet at least two compensating factors.

- Do you have any comments with regard to the underwriting standards for manually underwritten loans?

Sources:

[Department of Housing and Urban Development’s Request for Comment](#)