

Summary of the “Housing and Economic Recovery Act of 2008”

A. The “Federal Housing Finance Regulatory Reform Act of 2008”

This title strengthens and modernizes the regulation of the housing government-sponsored enterprises – Fannie Mae and Freddie Mac (the enterprises) and the Federal Home Loan Banks (FHLBs or Banks) – and expands the housing mission of these GSEs. In addition, it creates a new program at Federal Housing Administration (FHA) that will help at least 400,000 families save their homes from foreclosure by providing for new FHA loans after lenders take deep discounts.

I. Safety and Soundness Regulation of the Housing GSEs

The “Federal Housing Finance Regulatory Reform Act of 2008” establishes a new, independent, “world class” regulator for Fannie Mae, Freddie Mac, and the Federal Home Loan Banks. The legislation endows this regulator with broad new authority, equivalent to the authority of other federal financial regulators, to ensure the safe and sound operations of the GSEs, including the power to:

- establish capital standards;
- establish prudential management standards, including internal controls, audits, risk management, and management of the portfolio;
- enforce its orders through cease and desist authority, civil money penalties, and the authority to remove officers and directors;
- restrict asset growth and capital distributions for undercapitalized institutions;
- put a regulated entity into receivership; and
- review and approve (subject to notice and comment) new product offerings of the enterprises.

II. Mission Improvement

The new legislation also significantly enhances the affordable housing component of the GSEs’ mission, and expands the number of families Fannie Mae and Freddie Mac (the enterprises) can serve by raising the loan limits in high cost areas above the standard conforming limit to 115 percent of median house price up to 150 percent of the conforming loan limit. Currently, this would be \$625,500. The limit will be adjusted for inflation.

For the enterprises, the legislation tightens targeting requirements of the affordable housing goals, and rewrites those goals to ensure that the enterprises provide liquidity to both ownership and rental housing markets for low and very-low income families. The legislation requires the enterprises to serve a variety of underserved markets, such as rural areas, manufactured housing, and the preservation market. The legislation improves reporting requirements for affordable housing activities, including the expansion of the public use database, and strengthens the new regulator’s ability to enforce compliance with the housing goals.

Finally, the legislation creates a new Housing Trust Fund and a Capital Magnet Fund, financed by annual contributions from the enterprises, which will be used for the construction of affordable rental housing.

For the Federal Home Loan Banks (FHLBs), the legislation requires new affordable housing goals similar to those that apply to the enterprises for FHLB mortgage purchase programs. The legislation also requires the FHLBs to create a public use database for such programs. Treasury-certified Community Development Financial Institutions (CDFIs) are made eligible to join FHLBs. Finally, community financial institution members of the FHLBs may use FHLB advances for community development purposes.

III. Treasury Emergency Authority

The legislation contains several temporary provisions requested by Secretary of the Treasury Paulson designed to shore up the confidence of the financial markets in Fannie Mae, Freddie Mac, and the Federal Home Loan Banks, including the authority for Treasury to purchase debt securities issued by the GSEs and the authority for Treasury to purchase common stock of the enterprises with the agreement of the companies. This authority expires on December 31, 2009. Before exercising these temporary powers, the Treasury would have to determine that actions taken under this authority are necessary to:

- protect the taxpayer;
- provide stability to the financial markets; and,
- prevent disruptions in the availability of mortgages.

The Treasury would set the terms and conditions regarding any use of the temporary authority, including requiring that repayments to the government receive priority or preference. In addition, the emergency authority gives the Director of the Federal Housing Finance Agency (FHFA) the authority over executive compensation, whether or not the government exercises its temporary authority to purchase debt or stock.

Finally, the legislation requires the new Director to consult with Governors of the Federal Reserve when developing regulations or guidance regarding capital, portfolios, and prudential management standards, taking into consideration the risks posed by the regulated entities to the financial system. This requirement also expires on December 31, 2009.

IV. Mortgage Broker and Originator Licensing

The “Secure and Fair Enforcement for Mortgage Licensing Act (SAFE Act) creates greater accountability and transparency by establishing a uniform licensing and registration system for all loan originators, including mortgage brokers and loan officers. Under this provision, all loan originators at federally-regulated institutions will have to be registered through the nationwide system, and all other loan originators will be required to be licensed by the State or through a HUD-backup system if a state does not establish a licensing system. To meet the requirements under this provision, within 12 months, states will have to develop licensing requirements to ensure that applicants meet minimum standards including educational

requirements, background checks, and testing. If a state does not establish a licensing system that meets the minimum requirements, HUD is directed to establish a licensing system for loan originators in the state. Under this provision, borrowers and lending institutions will be able to access information about all loan originators, including their background and history as a loan originator.

B. Summary of the "HOPE for Homeowners Act of 2008"

The "HOPE for Homeowners Act of 2008" creates a new, temporary, voluntary program within FHA to back FHA-insured mortgages to distressed borrowers. The new mortgages offered by FHA-approved lenders will refinance the loans of distressed owner-occupants at risk of losing their homes to foreclosure at significant discounts. In exchange, homeowners will share future appreciation with FHA.

The program is built on **five principles**:

1. **Long-term affordability.** The program is built on the idea, expressed by Federal Reserve Chairman Bernanke, that creating new equity for troubled homeowners is likely to be a more effective way to avoid foreclosures. New loans will be based on a family's ability to repay the loan, ensuring affordability and sustainable homeownership.
2. **No investor or lender bailout.** Investors and/or lenders will have to take significant losses in order to benefit from the proceeds of the loans refinanced with government insurance. However, these losses would be less than the losses associated with foreclosure.
3. **No windfall for borrowers.** Borrowers will share their new equity and future appreciation equally with FHA. Borrowers will pay for the FHA insurance.
4. **Voluntary participation.** This will be a voluntary program. No lenders, servicers, or investors will be compelled to participate.
5. **Restore confidence, liquidity, and transparency.** Credit markets are fearful and frozen in part because banks and other financial institutions do not know what their subprime mortgages and related securities are worth. The uncertainty is forcing lenders to hoard capital and stop the lending necessary for economic growth. This program will help restore confidence and get markets flowing again.

Program Oversight. The new program will be overseen by a Board made up of the Secretary of HUD, the Secretary of the Treasury, the Chairman of the Federal Reserve Board, and the Chairman of the Federal Deposit Insurance Corporation (FDIC). The Board will have the authority to develop standards within the framework of the legislation.

Eligible Borrowers. Only owner-occupants who are unable to afford their mortgage payments are eligible for the program. No investors or investor properties will qualify. Homeowners must certify, under penalty of law, that they have not intentionally defaulted on their loan to qualify for the program and must have a mortgage debt-to-income ratio greater than 31 percent as of March 1, 2008. Lenders must document and verify borrowers' income with the IRS.

New Loan Amount. The size of the new FHA-insured loan will be the lesser of the amount the borrower can afford to repay, as determined by the current affordability requirements of FHA, or 90 percent of the current value of the home. Loans must be 30-year, fixed rate loans.

Equity & Appreciation Sharing. In order to avoid a windfall to the borrower created by the new 90% loan-to-value FHA-insured mortgage, the borrower must share the newly-created equity and future appreciation equally with FHA. This obligation will continue until the borrower sells the home or refinances the FHA-insured mortgage. Moreover, the homeowner's access to the newly created equity will be phased-in over 5 years.

Eligible Mortgages. In order to protect against adverse selection, the program prohibits the Secretary from paying an insurance claim whenever the representations and warranties required to be made by lenders are violated, or in cases in which a borrower has an early payment default and misses the first payment. The Act provides the Board the authority to establish other protections against adverse selection, such as requiring "seasoning" for certain higher risk loans before they can be insured under the program. Appraisers of property insured by FHA must be certified by the state where the property is located, or by a nationally recognized professional appraisal organization, and have "demonstrated verifiable education" in FHA appraisal requirements.

Existing Subordinate Liens. Before participating in this program, all subordinate liens must be extinguished. This will have to be done through negotiation with the first lien holder.

Qualified Safe Harbor. The legislation provides servicers with an incentive to participate in the program by offering a safe harbor against legal liability.

Program Size. The program is authorized to insure up to \$300 billion in mortgages and is expected to serve approximately 400,000 homeowners.

Program Sunset. The program will begin October 1, 2008 and sunset on September 30, 2011. CBO say the program will net nearly \$250 million for taxpayers. The program is paid for by using part of the Affordable Housing Trust Fund; the GSE bill provides a further \$2 billion cushion for the government by establishing a reserve fund at Treasury over ten years. If the program costs less than projected, the unused funds are returned to the Affordable Housing Trust Fund. If the program more than pays for itself (as was the case during the Roosevelt Administration), any excess savings are dedicated to reducing the national debt.

C. Summary of the "Foreclosure Prevention Act of 2008"

The Foreclosure Prevention Act contains the following provisions:

- **FHA Modernization.** To ensure that additional families can access the FHA program, which provides safe, fixed-rate mortgages, this title includes reforms to modernize, streamline and expand the reach of the FHA program. Under this legislation, the FHA loan limit is increased from 95 percent to 115 percent of area median home price with a cap at 150% of GSE limit (currently, \$625,500), allowing families in all areas of the country to

access homeownership through FHA. Downpayments of 3.5 percent will be required for any FHA loan and counseling requirements are enhanced to help provide for stable homeownership. The seller-funded downpayment assistance plan, which has been cited by the HUD Inspector General, the Government Accountability Office (GAO), and the IRS as having serious problems leading to large losses for FHA, would be shut down. Without this provision, the FHA program might have been pushed into the red, requiring an appropriation for the first time in its history.

- **Assisting Communities Devastated by Foreclosures.** Homes that have been foreclosed upon and are sitting unoccupied lead to declines in neighboring house values, increased crime and significant disinvestment. To ensure that communities can mitigate these harmful effects of foreclosures, \$3.92 billion is provided to communities hardest hit by foreclosures and delinquencies. These supplemental Community Development Block Grant Funds will be used to purchase foreclosed homes, at a discount, and rehabilitate or redevelop the homes to stabilize neighborhoods and stem the significant losses in house values of neighboring homes.
- **Providing Pre-Foreclosure Counseling for Families in Need.** To help families avoid foreclosure, this legislation provides \$150 million in additional funding for housing counseling. These funds will be distributed by the Neighborhood Reinvestment Corporation by the end of 2008 to ensure families can quickly get the help they need. As many as 250,000 additional families are expected to connect with their mortgage servicer or lender to explore options that will keep them in their homes as a result of these counseling funds. In addition, \$30 million is provided to help provide legal services to distressed borrowers.
- **Enhancing Mortgage Disclosure.** To ensure that consumers are provided with timely and meaningful disclosures in connection with mortgages, the legislation expands the types of home loans subject to early disclosures (within three days of application) under the Truth In Lending Act (TILA) to include all mortgages, including refinances and home equity loans. The legislation requires that disclosures be provided no later than 7 days prior to closing so borrowers can shop for another loan if not satisfied with the terms. The bill requires a new disclosure that informs borrowers of the maximum monthly payments possible under their loan, and also doubles the range of statutory damages for TILA violations to \$400 to \$4000.
- **Preserving the American Dream for Our Nation's Veterans.** To assist returning soldiers avoid foreclosure, this bill lengthens the time a lender must wait before starting foreclosure from three months to nine months after a soldier returns from service and also provides returning soldiers with one year relief from increases in mortgage interest rates. In addition, the Department of Defense is required to establish a counseling program to ensure veterans and active service members can access assistance if facing financial difficulties. Also included is a provision that increases the VA loan guarantee amount, so that veterans have additional homeownership opportunities. The legislation contains provisions to do the following: increase benefits paid to veterans with disabilities such as blindness for the purpose of adapting their housing; provide a moving benefit to servicemen and women who are forced to move out of rental housing because the owner of the housing was foreclosed on; provide that veterans benefits received in a lump sum are treated the same for the purposes of

eligibility for housing assistance as monthly benefits; and to allow the Veterans Administration to provide for improvements and structural alterations to homes of veterans with service-connected disabilities.

NOTE: a summary of the tax provisions is available from the Senate Finance Committee.