109TH CONGRESS
2d Session

HOUSE OF REPRESENTATIVES

REPORT
109–571

ZERO DOWNPAYMENT PILOT PROGRAM ACT OF 2006

JULY 17, 2006.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. OXLEY, from the Committee on Financial Services, submitted the following

R E P O R T

together with

DISSENTING VIEWS

[To accompany H.R. 3043]

[Including cost estimate of the Congressional Budget Office]

The Committee on Financial Services, to whom was referred the bill (H.R. 3043) to authorize the Secretary of Housing and Urban Development to carry out a pilot program to insure zero-downpayment mortgages for one-unit residences, having considered the same, report favorably thereon with an amendment and recommend that the bill as amended do pass.

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49–006

AMENDMENT

The amendment is as follows:

Strike all after the enacting clause and insert the following:

SECTION 1. SHORT TITLE.

This Act may be cited as the "Zero Downpayment Pilot Program Act of 2006".

SEC. 2. PILOT PROGRAM FOR INSURANCE FOR ZERO-DOWNPAYMENT MORTGAGES.

(a) MORTGAGE INSURANCE AUTHORITY.—Section 203 of the National Housing Act (12 U.S.C. 1709) is amended by inserting after subsection (k) the following new subsection:

"(l) ZERO-DOWNPAYMENT MORTGAGES PILOT PROGRAM.—

"(1) INSURANCE AUTHORITY.—The Secretary may insure, and commit to insure, under this subsection any mortgage that meets the requirements of this subsection and, except as otherwise specifically provided in this subsection, of subsection (b).

"(2) ELIGIBLE SINGLE FAMILY PROPERTY.—To be eligible for insurance under this subsection, a mortgage shall involve a property upon which there is located a dwelling that is designed principally for a 1- to 3-family residence and that, notwithstanding subsection (g), is to be occupied by the mortgagor as his or her principal residence, which shall include—

"(A) a 1-family dwelling unit in a multifamily project and an undivided interest in the common areas and facilities which serve the project;

"(B) a 1-family dwelling unit of a cooperative housing corporation the permanent occupancy of the dwelling units of which is restricted to members of such corporation and in which the purchase of such stock or membership entitles the purchaser to the permanent occupancy of such dwelling unit; and

"(C) a manufactured home that meets such standards as the Secretary has established for purposes of subsection (b).

"(3) MAXIMUM PRINCIPAL OBLIGATION.—

"(A) LIMITATION.—To be eligible for insurance under this subsection, a mortgage shall involve a principal obligation in an amount not in excess of 100 percent of the appraised value of the property plus any initial service charges, appraisal, inspection and other fees in connection with the mortgage as approved by the Secretary.

"(B) INAPPLICABILITY OF OTHER LOAN-TO-VALUE REQUIREMENTS.—A mortgage insured under this subsection shall not be subject to subparagraph (B) of paragraph (2) of subsection (b) or to the matter in such paragraph that follows such subparagraph.

"(4) ELIGIBLE MORTGAGORS.—The mortgagor under a mortgage insured under this subsection shall meet the following requirements:

"(A) FIRST-TIME HOMEBUYER.—The mortgagor shall be a first-time homebuyer. The program for mortgage insurance under this subsection shall be considered a Federal program to assist first-time homebuyers for purposes of section 956 of the Cranston-Gonzalez National Affordable Housing Act (42 U.S.C. 12713).

"(B) COUNSELING.—

"(i) REQUIREMENT.—The mortgagor shall have received counseling, prior to application for the loan involved in the mortgage, by a third party (other than the mortgagee) who is approved by the Secretary, with respect to the responsibilities and financial management involved in homeownership. Such counseling shall be provided to the mortgagor on an individual basis by a representative of the approved third party counseling entity, and shall be provided in person to the maximum extent practicable.

"(ii) TOPICS.—Such counseling shall include providing to, and discussing with, the mortgagor—

"(I) information regarding homeownership options other than a mortgage insured under this subsection, other zero- or low-downpayment mortgage options that are or may become available to the mortgagor, the financial implications of entering into a mortgage (including a mortgage insured under this subsection), and any other information that the Secretary may require; and

"(II) a document that sets forth the amount and the percentage by which a property subject to a mortgage insured under this subsection must appreciate for the mortgagor to recover the principal amount of the mortgage, the costs financed under the mortgage, and the estimated costs involved in selling the property, if the mortgagor were to sell the property on each of the second, fifth, and tenth anniversaries of the mortgage.

"(iii) 2- AND 3-FAMILY RESIDENCES.—In the case of a mortgage involving a 2- or 3-family residence, such counseling shall include (in addition to the information required under clause (ii)) information regarding real estate property management.

"(5) OPTION FOR NOTICE OF FORECLOSURE PREVENTION COUNSELING AVAILABILITY.—

"(A) OPTION.—To be eligible for insurance under this subsection, the mortgagee shall provide mortgagor, at the time of the execution of the mortgage, an optional written agreement which, if signed by the mortgagor, allows, but does not require, the mortgagee to provide notice described in subparagraph (B) to a housing counseling entity that has agreed to provide the notice and counseling required under subparagraph (C) and is approved by the Secretary.

"(B) NOTICE TO COUNSELING AGENCY.—The notice described in this subparagraph, with respect to a mortgage, is notice, provided at the earliest time practicable after the mortgagor becomes 60 days delinquent with respect to any payment due under the mortgage, that the mortgagor is so delinquent and of how to contact the mortgagor. Such notice may only be provided once with respect to each delinquency period for a mortgage.

"(C) NOTICE TO MORTGAGOR.—Upon notice from a mortgagee that a mortgagor is 60 days delinquent with respect to payments due under the mortgage, the housing counseling entity shall at the earliest time practicable notify the mortgagor of such delinquency, that the entity makes available foreclosure prevention counseling that may assist the mortgagor in resolving the delinquency, and of how to contact the entity to arrange for such counseling.

"(D) ABILITY TO CURE.—Failure to provide the optional written agreement required under subparagraph (A) may be corrected by sending such agreement to the mortgagor not later than the earliest time practicable after the mortgagor first becomes 60 days delinquent with respect to payments due under the mortgage. Insurance provided under this subsection may not be terminated and penalties for such failure may not be prospectively or retroactively imposed if such failure is corrected in accordance with this subparagraph.

"(E) PENALTIES FOR FAILURE TO PROVIDE AGREEMENT.—The Secretary may establish and impose appropriate penalties for failure of a mortgagee to provide the optional written agreement required under subparagraph (A).

"(F) LIMITATION ON LIABILITY OF MORTGAGEE.—A mortgagee shall not incur any liability or penalties for any failure of a housing counseling entity to provide notice under subparagraph (C).

"(G) NO PRIVATE RIGHT OF ACTION.—This paragraph shall not create any private right of action on behalf of the mortgagor.

"(H) DELINQUENCY PERIOD.—For purposes of this paragraph, the term 'delinquency period' means, with respect to a mortgage, a period that begins upon the mortgagor becoming delinquent with respect to payments due under the mortgage and ends upon the first subsequent occurrence of such payments under the mortgage becoming current or the property subject to the mortgage being foreclosed or otherwise disposed of.

"(6) INAPPLICABILITY OF DOWNPAYMENT REQUIREMENT.—A mortgage insured under this subsection shall not be subject to paragraph (9) of subsection (b) or any other requirement to pay on account of the property, in cash or its equivalent, any amount of the cost of acquisition.

"(7) MMIF MONITORING.—In conjunction with the credit subsidy estimation calculated each year pursuant to the Federal Credit Reform Act of 1990 (2 U.S.C. 661 et seq.), the Secretary shall review the program performance for mortgages insured under this subsection and make any necessary adjustments, which may include altering mortgage insurance premiums subject to subsection (c)(2), adjusting underwriting standards, and limiting the availability of mortgage insurance under this subsection, to ensure that the Mutual Mortgage Insurance Fund shall continue to generate a negative credit subsidy.

"(8) UNDERWRITING.—For a mortgage to be eligible for insurance under this subsection:

"(A) IN GENERAL.—The mortgagor's credit and ability to pay the monthly mortgage payments shall have been evaluated using the Federal Housing

Administration's Technology Open To Approved Lenders (TOTAL) Mortgage Scorecard, or a similar standardized credit scoring system approved by the Secretary, and in accordance with procedures established by the Secretary.

"(B) MULTI-UNIT PROPERTIES.—In the case of a mortgage involving a property upon which there is located a dwelling that is designed principally for a 2- or 3-family residence, the mortgagor meets such additional underwriting standards as the Secretary may establish.

"(9) APPROVAL OF MORTGAGEES.—To be eligible for insurance under this subsection, a mortgage shall have been made to a mortgagee that meets such criteria as the Secretary shall establish to ensure that mortgagees meet appropriate standards for participation in the program authorized under this subsection.

"(10) DISCLOSURE OF INCREMENTAL COSTS.—

"(A) REQUIRED DISCLOSURE.—For a mortgage to be eligible for insurance under this subsection, the mortgagee shall provide to the mortgagor, at the time of the application for the loan involved in the mortgage, a written disclosure, as the Secretary shall require, that specifies the effective cost to a mortgagor of borrowing the amount by which the maximum amount that could be borrowed under a mortgage insured under this subsection exceeds the maximum amount that could be borrowed under a mortgage insured under subsection (b), based on average closing costs with respect to such amount, as determined by the Secretary. Such cost shall be expressed as an annual interest rate over the first 5 years of a mortgage.

"(B) COORDINATION.—The disclosure required under this paragraph may be provided in conjunction with the notice required under subsection (f).

"(11) LOSS MITIGATION.—

"(A) IN GENERAL.—Upon the default of any mortgage insured under this subsection, the mortgagee shall engage in loss mitigation actions for the purpose of providing an alternative to foreclosure to the same extent as is required of other mortgages insured under this title pursuant to the regulations issued under section 230(a).

"(B) ANNUAL REPORTING.—Not later than 90 days after the end of each fiscal year, the Secretary shall submit a report to the Congress that compares the rates of default and foreclosure during such fiscal year for mortgages insured under this subsection, for single-family mortgages insured under this title (other than under this subsection), and for mortgages for housing purchased with assistance provided under the downpayment assistance initiative under section 271 of the Cranston-Gonzalez National Affordable Housing Act (42 U.S.C. 12821).

"(12) ADDITIONAL REQUIREMENTS.—The Secretary may establish any additional requirements for mortgage insurance under this subsection as may be necessary or appropriate.

"(13) PILOT PROGRAM LIMITATIONS.—

"(A) ANNUAL.—In any fiscal year, the aggregate number of mortgages insured under this subsection may not exceed 10 percent of the aggregate number of mortgages and loans insured by the Secretary under this title during the preceding fiscal year.

"(B) TERM OF PROGRAM.—The aggregate number or mortgages insured under this subsection may not exceed 50,000.

"(14) PROGRAM SUSPENSION.—

"(A) IN GENERAL.—Subject to subparagraph (C), the authority under paragraph (1) to insure mortgages shall be suspended if at any time the claim rate described in subparagraph (B) exceeds 3.5 percent. A suspension under this subparagraph shall remain in effect until such time as such claim rate is 3.5 percent or less.

"(B) FHA TOTAL SINGLE-FAMILY ANNUAL CLAIM RATE.—The claim rate described in this subparagraph, for any particular time, is the ratio of the number of claims during the 12 months preceding such time on mortgages on 1- to 4-family residences insured pursuant to this title to the number of mortgages on such residences having such insurance in force at that time.

"(C) APPLICABILITY.—A suspension under subparagraph (A) shall not preclude the Secretary from endorsing or insuring any mortgage that was duly executed before the date of such suspension.

"(15) SUNSET.—No mortgage may be insured under this subsection after September 30, 2010, except that the Secretary may endorse or insure any mortgage that was duly executed before such date.

"(16) GAO REPORTS.—The Comptroller General of the United States shall submit a report to the Congress not later than 2 years after the date of the enactment of this subsection, and annually thereafter, regarding the performance of mortgages insured under this subsection.

"(17) IMPLEMENTATION.—The Secretary may implement this subsection on an interim basis by issuing an interim rule, except that the Secretary shall solicit public comments upon publication of such interim rule and shall issue a final rule implementing this subsection after consideration of the comments submitted.".

(b) MORTGAGE INSURANCE PREMIUMS.—The second sentence of subparagraph (A) of section 203(c)(2) of the National Housing Act (12 U.S.C. 1709(c)(2)(A)) is amended by striking "In" and inserting "Except with respect to a mortgage insured under subsection (l), in".

(c) GENERAL INSURANCE FUND.—Section 519(e) of the National Housing Act (12 U.S.C. 1735c(e)) is amended by striking "and 203(i)" and inserting ", 203(i), and 203(l)".

(d) GAO STUDY OF EXPANDED OR EXTENDED PROGRAM.—If at any time authority to insure mortgages under section 203(l) of the National Housing Act (as added by subsection (a) of this section) is—

(1) expanded to more than 50,000 mortgages, or

(2) extended to a date after September 30, 2010, including any permanent extension of such authority,

the Comptroller General of the United States shall conduct a study of the financial soundness, at such time, of the Mutual Mortgage Insurance Fund and the effects of such expansion or extension on such financial soundness, and shall submit a report to the Congress regarding the conclusions of such study not later than 60 days after the date of the enactment of the law providing for such expansion or extension.

PURPOSE AND SUMMARY

H.R. 3043, the Zero Downpayment Pilot Act of 2005, would authorize a Federal Housing Administration (FHA) pilot program for a mortgage insurance product, limited to 50,000 mortgages nationwide, without a downpayment requirement by a potential borrower or third party. After 5 years, GAO would report on whether the agency was able to develop a product that minimized risks and thereby limited defaults and foreclosures for otherwise very creditworthy families who have no downpayment funds at the time of a real estate settlement, while at the same time testing whether the agency could develop appropriate underwriting and agency review.

BACKGROUND AND NEED FOR LEGISLATION

Studies demonstrate the single biggest obstacle to homeownership is an inability to have enough cash to meet downpayment and closing costs. This program, when enacted, will be available to first-time homebuyers that meet the Federal Housing Administration's (FHA) underwriting requirements and who could easily afford monthly payments, but have not had an opportunity to save for a downpayment. As a pilot program, the number of FHA-insured zero-downpayment mortgages may not exceed 50,000.

Further, as a control on whether the demonstration accelerates or places FHA-insured mortgages at greater risk of default or foreclosure, this pilot program will end if at any time the claim rate exceeds 3.5 percent, and will remain suspended as long as the claim rate is 3.5 percent or less. These measures will allow many families access to an FHA-insured zero-downpayment product and will provide data for use in determining the long-term fate of the FHA zero-downpayment program, all while protecting the FHA portfolio.

Since the creation of the Federal Housing Administration (FHA) under the National Housing Act in 1934 (Pub. Law 73–479), downpayments have been a requirement of potential borrowers seeking to purchase loans insured by the Federal government. Theoretically, downpayment requirements were established to assure the lender that a borrower would be less likely to default or risk foreclosure on a home if there was some personal investment stake. Recently, some conventional mortgage lending products, purchased by the secondary markets or held in institutional investment portfolios, dropped to zero-downpayments, contingent on certain underwriting conditions.

Because certain conventional markets created zero downpayment products with minimal risks, there is a question on whether downpayments originally thought as necessary to gauge the creditworthiness or risk of the borrower are even necessary. Seventy-two years after FHA was created, technology has advanced as a science on how to predict creditworthiness and risk of borrowers based on past credit behavior. Hence, credit scores and other assessment tools are central to mortgage underwriting. The pilot program envisioned by H.R. 3043 would allow the agency an opportunity to use advanced technology and underwriting mechanisms to test whether FHA could provide mortgage insurance to creditworthy families who have not paid a downpayment at the time of the real estate settlement. A sample of 50,000 FHA mortgages would provide adequate data points for the agency to determine whether its underwriting and risk assessment controls are adequate. If successful, a well-thought zero downpayment product would provide another affordable homeownership option for working families and communities.

The Committee is aware of work conducted by the Department of Housing and Urban Development's Inspector General, which suggested that mortgages made through non-profit gift downpayment programs carry default rates far above average defaults and claims. According to the Government Accountability Office, in 2004, about 30 percent of FHA single-family loans used downpayment assistance from a non-profit group, compared with 5.8 percent in 2000. During that same time, FHA default rates for mortgage holders that receive downpayment assistance have steadily increased. This correlation suggests that the non-profit gift downpayment programs are largely responsible for this increase in default rates.

In addition to HUD- and GAO-expressed concerns regarding the non-profit gift downpayment programs, the Internal Revenue Service has raised concerns over how some organizations administer non-profit gift programs and is in the process of reassessing the status of these programs. Consequently, the IRS recently issued a Ruling in which it determined that organizations providing downpayment assistance grants to homebuyers from funds largely provided by home sellers do not qualify as tax-exempt charities. The IRS further acknowledges that there are some programs, such as churches, which operate a legitimate model using non-home seller proceeds that will continue to retain their tax-exempt status.

The IRS ruling provides FHA lenders with clarity necessary to evaluate downpayment assistance gifts in FHA transactions. H.R. 3043 will allow FHA flexibility to test these products under its own underwriting scrutiny without third-party factors that could influence defaults and foreclosures. Due to this observation, it is critical that FHA be able to offer similar programs to first-time homebuyers with greater financial controls such as pre-purchase counseling and additional counseling should an individual default on their loan.

Allowing FHA to enter this market will lead to greater oversight, more influence and better outcomes for those choosing to participate. Further, the FHA-insured zero-downpayment product created by this legislation will be administered as a pilot program. This will allow the program to be studied, in order to determine the effects, if any, of this product on the Mutual Mortgage Insurance Fund (MMIF). To this end, the legislation calls for GAO reporting.

Hearings

The Subcommittee on Housing and Community Opportunity held a legislative hearing on June 30, 2005 on "H.R. 3034, the Zero Downpayment Pilot Program Act of 2005." The following witnesses testified: Ms. Janis Bowdler, Housing Policy Analyst, National Council of La Raza, Washington, DC; Mr. Robert Newman, Executive Vice Chairman, AmeriDream, Inc., Gaithersburg, Maryland; Mr. Michael F. Petrie, President, P/R Mortgage & Investment Corporation, Indianapolis, Indiana, testifying as Chairman, Mortgage Bankers Association, Washington, DC; Mr. William B. Shear, Director of Financial Markets and Community Investment, U.S. Government Accountability Office; Mr. David F. Wilson, President Wilson Construction LLC, Ketchum, Idaho, testifying as President, National Association of Home Builders.

Committee Consideration

The Committee on Financial Services met in open session on May 24, 2006, and ordered reported H.R. 3043, the Zero Downpayment Pilot Act of 2005, as amended, to the House by a voice vote.

Committee Votes

Clause 3(b) of rule XIII of the Rules of the House of Representatives requires the Committee to list the record votes on the motion to report legislation and amendments thereto. No record votes were taken in conjunction with the consideration of this legislation. A motion by Mr. Oxley to report the bill, as amended, to the House with a favorable recommendation was agreed to by a voice vote. During the consideration of the bill the following amendments were considered:

An amendment by Ms. Lee, No. 1, dealing with the Community Partners Next Door Program, was offered and withdrawn.

An amendment by Mr. Feeney, No. 2, requiring a GAO study of expanded or extended programs, was agreed to by a voice vote.

Committee Oversight Findings

Pursuant to clause 3(c)(1) of rule XIII of the Rules of the House of Representatives, the Committee held hearings and made findings that are reflected in this report.

Performance Goals and Objectives

Pursuant to clause 3(c)(4) of rule XIII of the Rules of the House of Representatives, the Committee establishes the following performance related goals and objectives for this legislation:

H.R. 3043, the Zero Downpayment Pilot Act of 2005, would authorize a Federal Housing Administration (FHA) pilot program for a mortgage insurance product, limited to 50,000 mortgages nationwide, without a downpayment requirement by a potential borrower or third-party. After 5 years, GAO would report on whether the agency was able to develop a product that minimized risks and thereby limited defaults and foreclosures for otherwise very creditworthy families who have no downpayment funds at the time of a real estate settlement, while at the same time testing whether the agency could develop appropriate underwriting and agency review.

NEW BUDGET AUTHORITY, ENTITLEMENT AUTHORITY, AND TAX EXPENDITURES

In compliance with clause 3(c)(2) of rule XIII of the Rules of the House of Representatives, the Committee adopts as its own the estimate of new budget authority, entitlement authority, or tax expenditures or revenues contained in the cost estimate prepared by the Director of the Congressional Budget Office pursuant to section 402 of the Congressional Budget Act.

COMMITTEE COST ESTIMATE

The Committee adopts as its own the cost estimate prepared by the Director of the Congressional Budget Office pursuant to section 402 of the Congressional Budget Act of 1974.

CONGRESSIONAL BUDGET OFFICE ESTIMATE

Pursuant to clause 3(c)(3) of rule XIII of the Rules of the House of Representatives, the following is the cost estimate provided by the Congressional Budget Office pursuant to section 402 of the Congressional Budget Act of 1974:

JUNE 1, 2006.

Hon. MICHAEL G. OXLEY,
Chairman, Committee on Financial Services,
House of Representatives, Washington, DC.

DEAR MR. CHAIRMAN: The Congressional Budget Office has prepared the enclosed cost estimate for H.R. 3043, the Zero Downpayment Pilot Program Act of 2005.

If you wish further details on this estimate, we will be pleased to provide them. The CBO staff contact is Susanne S. Mehlman.

Sincerely,

DONALD B. MARRON,
Acting Director.

Enclosure.

H.R. 3043—Zero Downpayment Pilot Program Act of 2005

Summary: H.R. 3043 would authorize—through fiscal year 2010—a new loan guarantee program under the Federal Housing Administration (FHA) that would allow first-time home buyers to purchase a home without a down payment. Currently, FHA's single-family loan guarantee program requires home buyers to make a down payment of at least 3 percent of the sales price.

CBO estimates that implementing this legislation would cost $65 million over the 2007–2010 period, assuming future appropriation actions consistent with the bill. FHA's loan guarantee programs are discretionary federal credit programs that require appropriation action each year to establish a dollar limitation on the value of loans that may be guaranteed and to provide a credit subsidy appropriation for those FHA programs estimated to have a positive subsidy rate.

Enacting this bill could affect direct spending and receipts because the bill would provide the Secretary of Housing and Urban Development (HUD) with the authority to establish penalties against borrowers who fail to meet certain requirements under the bill. CBO estimates that any increase in civil or criminal penalties would not be significant.

H.R. 3043 contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act and would impose no costs on state, local, or tribal governments.

Estimated Cost to the Federal Government: The estimated budgetary impact of H.R. 3043 is shown in the following table. The costs of this legislation fall within budget function 370 (mortgage and housing credit). For this estimate, we assume the bill will be enacted near the end of fiscal year 2006.

	By fiscal year, in millions of dollars					
	2007	2008	2009	2010	2011	2012
SPENDING SUBJECT TO APPROPRIATION						
FHA and GNMA Spending Under Current Law: [1]						
Estimated Authorization Level	−1,013	−333	−327	−331	−344	−353
Estimated Outlays	−1,013	−333	−327	−331	−344	−353
Proposed Changes:						
Net Subsidy Cost for Zero Down-Payment Loans:						
Estimated Authorization Level	0	14	23	20	16	0
Estimated Outlays	0	14	23	20	16	0
GNMA Offsetting Collections:						
Estimated Authorization Level	0	−2	−2	−2	−2	0
Estimated Outlays	0	−2	−2	−2	−2	0
Total Changes:						
Estimated Authorization Level	0	12	21	18	14	0
Estimated Outlays	0	12	21	18	14	0
Total FHA and GNMA Spending Under H.R. 3043:						
Estimated Authorization Level	−1,013	−321	−306	−313	−330	−353
Estimated Outlays	−1,013	−321	−306	−313	−330	−353

[1] The figures for 2006 are CBO's current estimates of budget authority and outlays for these programs under the enacted appropriation levels for this year. The 2007–2011 level are CBO's baseline estimates of the amount of offsetting collections generated by FHA's single-family program and GNMA's single-family MBS program.

Note.—GNMA = Government National Mortgage Association; MBS = Mortgage-Backed Securities.

Basis of estimate: The budgetary impact of the zero down-payment loan program would depend on how many households would use this provision to help them become homeowners and the likelihood that such borrowers would default on the mortgages. CBO estimates that implementing H.R. 3043 would cost FHA $14 million in 2007 and $73 million over the 2007–2010 period to pay for the estimated subsidy cost of the zero down-payment program. We also estimate that new federal loan guarantees made under the new program (about 60 percent of all zero down-payment loans) would be included in the Government National Mortgage Association's (GNMA's) Mortgage-Backed Securities (MBS) program, resulting in the collection of additional negative subsidy receipts of $8 million over the 2007–2010 period. Thus, CBO estimates that the net federal cost of the new program would be $65 million over the 2007–2010 period, including effects on both FHA and GNMA programs.

There also would be a cost associated with the Government Accountability Office (GAO) studies that are required under this bill. However, CBO estimates that those costs would be less than $500,000 each year. Each of these budget effects are discussed below.

Proposed zero down-payment mortgage guarantee program

The new loan guarantees would be available to home buyers purchasing various types of one-to-three family residences, such as single-family homes and condominiums, through September 30, 2010. Borrowers who want to participate in this pilot program would be required to attend individual counseling sessions related to financial management skills for homeowners prior to applying for the loans. Under the bill, the number of zero down-payment loans insured by FHA each year could not exceed 10 percent of the total number of single-family FHA loan guarantees made during the preceding year, and no more than 50,000 loans could be insured over the life of the program. This legislation also would allow FHA to charge up-front and annual fees up to the levels set under current law (2.25 percent and 0.55 percent of the loan amount, respectively) for the existing single-family program.

Demand for the zero down-payment program

According to FHA, mortgage banking associations, and industry experts, the number of private entities supporting down-payment assistance programs and zero down-payment programs in recent years has grown, indicating a growing demand for programs that help home buyers who cannot afford down payments. For example, the Nehemiah Corporation, which is the oldest and largest nonprofit provider of down-payment assistance in the country, provided assistance to over 5,500 home buyers in 1998 compared to 20,000 home buyers in 2005. Furthermore, the National Association of Realtors reports that 43 percent of all first time homebuyers in 2005 financed their home purchases with a zero down-payment mortgage.

This bill would limit the loan volume for the zero down-payment program to no more than 10 percent of single-family loan guarantees made by FHA in the preceding year (i.e., 33,000 to 37,000 loans estimated per year) and to no more than 50,000 loans over the life of the pilot program. CBO expects that demand for a zero down-payment loan guarantee program would be strong and, based on information from FHA, expects that 50,000 loans with a face value of about $6 billion to $7 billion (known as the loan volume) could be guaranteed over the 2007–2010 period. CBO estimates that the number of loans guaranteed each year of the program would be roughly the same, though CBO expects that fewer loans would be guaranteed during the initial year of the pilot program, as FHA would need some time to make the administrative changes necessary to support the new program.

Choice between traditional FHA guarantee and zero down-payment program

According to FHA, about 70 percent of its borrowers are first time home buyers, and an increasing number of them are using some form of down-payment assistance (e.g., gifts from relatives or grants from nonprofit entities). On average, these borrowers represent about 40 percent of FHA's first-time home buyers making the minimum 3 percent down payment. CBO estimates that about 90,000 FHA borrowers who are first-time home buyers will use some form of down-payment assistance each year.

From the perspective of the FHA borrower, there would be both advantages and disadvantages to using the new zero down-payment program instead of the existing single-family program. On the one hand, under the new program the borrower would not need to seek gifts from relatives or use down-payment assistance programs, which can result in the borrower paying an increased amount for the home. On the other hand, the fees under the zero down-payment program would be higher than the regular FHA program, the borrower would have no equity in the home, and the borrower would be required to attend financial counseling, though, in some cases, the borrower may readily accept the potential benefits of meeting with a counselor and consider the assistance to be an advantage. CBO estimates that about 40 percent of the 50,000 borrowers expected to participate in the pilot program would have used the existing single-family program if the proposed zero down-payment program did not exist. We estimate that this shift of about 20,000 borrowers or $3 billion worth of loan guarantees over the 2007–2010 period from the existing single-family program to the new zero down-payment program would reduce the subsidy cost of the FHA program, as discussed below.

Credit risk associated with the zero down-payment program

Zero down-payment loans are viewed by private-sector lenders as having a higher risk of default than traditional mortgages with downpayments according to several industry experts involved with the secondary-mortgage market, trade associations, and down-payment assistance programs. For private lenders, the borrower's loan-to-value (LTV) ratio indicates how much equity a borrower initially has in the home and serves as one of the predictors of the likelihood of default. On average, borrowers with less equity (that is, higher LTV ratios) have higher default rates than borrowers with more equity. Such borrowers are more vulnerable to adverse events, such as job loss and falling house prices. Under the proposed zero down-payment program, borrowers would become homeowners with zero or negative equity because borrowers could finance their up-front premiums and closing costs, resulting in LTV ratios of 103 percent or more.

To compensate for this risk of default, FHA as indicated that it would not change the credit standards (e.g., debt-to-income ratios and payment-to-income ratios) for zero down-payment borrowers. Instead, FHA would charge such borrowers higher loan-guarantee fees than those charged to borrowers under FHA's current single-family program. CBO assumes that FHA would charge zero down-payment borrowers the highest fees authorized under current law. That is, the up-front fees for the new program would be 2.25 percent of the loan value and annual fees would be 0.55 percent of the loan value. (In comparison, borrowers in the existing program pay an up-front premium of a 1.5 percent and annual premiums of 0.5 percent.)

Financial counseling

Based on information from industry experts and credit studies, CBO expects that the counseling required under this legislation could contribute to better loan performance and consequently fewer defaults. We estimate that the claims rate for the zero down-payment loans could be lowered by about 25 percent compared to the claims rate for loans receiving some type of down-payment assistance, resulting in a cumulative claim rate of about 20 percent for the zero down-payment loans. Despite these higher fees and the mandatory counseling, however, CBO expects that default costs could still exceed the value of the higher fees.

Program suspension

This bill would require FHA to suspend the zero down-payment program if more than 3.5 percent of the loans in the program are foreclosed in one year. CBO estimates that defaults for the new program would average about 1 to 2 percent each year and that the cumulative default rate over a 30-year period would be close to 20 percent. This restriction on the number of defaults could limit the number of loans FHA insures each year if the number of foreclosures is greater than we estimate. But other factors, such as changing consumer demand for the program due to higher interest rates, could also lead to a smaller loan volume in the program. The zero down-payment program would be considered a discretionary program that could be suspended by FHA at any time. For this estimate, CBO assumes that the necessary subsidies are provided each year through the appropriation process and that the subsidies are spent each year.

Subsidy cost

CBO estimates that implementing the zero down-payment program would result in a net cost of $12 million in 2007 and $65 million over the 2007–2010 period, reflecting changes to FMA and GNMA programs. The estimated loan subsidy costs—which are treated as discretionary spending—would be recorded in the budget each year when the subsidy appropriation is provided.

FHA Costs. Budget procedures for federal credit programs require that funds must be appropriated in advance to cover the subsidy cost of the loan guarantees, as estimated on a present value basis. CBO estimates that the new program would have a subsidy rate of about 1.85 percent, compared to our estimate of the 2007 subsidy rate of −0.37 percent for FHA's existing single-family program. This estimated subsidy rate assumes that FHA would charge the maximum fees allowable under current law (2.25 percent for the up-front fee and 0.55 percent for the annual fee) and that the cumulative claims rate for the program would be about 20 percent, or two times the claim rate for the average FHA loan. With a subsidy rate of 1.85 percent, CBO estimates that the zero down-payment program would cost $125 million over the 2007–2010 period.

This estimated subsidy cost would be partially offset by some expected savings associated with borrowers shifting from the existing single-family program to the zero down-payment program. The borrowers that would shift to the new program would tend to have a greater risk of default than the average FHA loan. CBO estimates that the shift of these borrowers to the new program would leave the remaining portfolio of single-family loan guarantees in a better financial position with an overall slightly more negative subsidy rate. CBO estimates that the negative subsidy associated with the existing single-family program would decrease by about 0.1 percent beginning in 2007, resulting in additional offsetting collections of about $50 million over the 2007–2010 period. Hence, the net change in FHA subsidy costs over the period would be about $75 million.

GNMA Offsetting Collections. GNMA is responsible for guaranteeing securities backed by pools of mortgages insured by the federal government. In exchange for a fee charged to lenders or issuers of the securities, GNMA guarantees the timely payments of scheduled principal and interest due on the pooled mortgages that back these securities. Because the value of the fees collected are estimated to exceed the cost of loan defaults in each year, the GNMA MBS program is estimated to have subsidy rate of −0.21 percent in 2007, resulting in the net collection of receipts to the federal government.

Because most FHA-insured loans are eventually included in GNMA's MBS program, CBO estimates that implementing the zero down-payment program would result in additional collections to GNMA. We estimate that about 60 percent of the loan guarantees made under this new program would represent new loan guarantees for FHA that would not otherwise participate in GNMA's MBS program, resulting in the collection of $2 million in 2007 and $8 million over the 2007–2010 period. GNMA collections associated with the remaining 40 percent of the loans made under the pilot program are not included in this savings estimate because CBO estimates these borrowers would use the existing FHA program if the zero down-payment option were not available.

GAO studies

This legislation also would require the Government Accountability Office to prepare a report on loan performance under the zero downpayment program no later than two years following enactment of the bill and annually thereafter. CBO estimates that GAO would require less than $500,000 annually beginning in 2008 for such reports. In addition, GAO would be required to study the financial soundness of the Mutual Mortgage Insurance Fund in the event that authority for the pilot program is expanded to more than 50,000 mortgages or extended beyond its sunset date of September 30, 2010. Because CBO cannot predict whether the pilot program will be expanded or extended, we do not estimate any costs associated with this study.

Intergovernmental and private-sector impact: H.R. 3043 contains no intergovernmental or private-sector mandates as defined in UMRA and would impose no costs on state, local, or tribal governments.

Estimate prepared by: Federal Costs: Susanne S. Mehlman. Impact on State, Local, and Tribal Governments: Sarah Puro. Impact on the Private Sector: Paige Piper/Bach.

Estimate approved by: Peter H. Fontaine, Deputy Assistant Director for Budget Analysis.

Federal Mandates Statement

The Committee adopts as its own the estimate of Federal mandates prepared by the Director of the Congressional Budget Office pursuant to section 423 of the Unfunded Mandates Reform Act.

Advisory Committee Statement

No advisory committees within the meaning of section 5(b) of the Federal Advisory Committee Act were created by this legislation.

Constitutional Authority Statement

Pursuant to clause 3(d)(1) of rule XIII of the Rules of the House of Representatives, the Committee finds that the Constitutional Authority of Congress to enact this legislation is provided by Article 1, section 8, clause 1 (relating to the general welfare of the United States) and clause 3 (relating to the power to regulate interstate commerce).

Applicability to Legislative Branch

The Committee finds that the legislation does not relate to the terms and conditions of employment or access to public services or accommodations within the meaning of section 102(b)(3) of the Congressional Accountability Act.

Section-by-Section Analysis of the Legislation

Sec. 1. Short title

The short title of this act is the "Zero Downpayment Pilot Program Act of 2006."

Sec. 2. Pilot program for insurance for zero-downpayment mortgages

This section permits FHA to insure a limited number of zero-downpayment mortgages for eligible one- to three-family residences.

Mortgage insurance authority

In order for a borrower to qualify for a mortgage created by this pilot program, he or she must be a first-time homebuyer. Also, the borrower will be required to participate in approved, third-party financial counseling prior to the loan application. This section describes the topics that must be covered during this counseling.

This section gives the lender the option of providing notice to a housing counseling agency if the borrower falls more than 60 days behind on his or her payments, so that the borrower may receive foreclosure prevention counseling. The Secretary of HUD may establish penalties for failing to provide this option. Also, the lender will not incur any damages through the failure of the counseling agency to prevent foreclosure and the borrower will have no cause of action.

In order for eligible borrowers to receive an FHA-insured zero-downpayment loan, this section renders the FHA downpayment requirement inapplicable for this class of borrowers.

This section directs the Secretary of HUD to review the zero-downpayment pilot program and make adjustments, if needed, so that the Mutual Mortgage Insurance Fund (MMIF) continues to generate a negative credit subsidy.

This section also establishes the mortgage insurance underwriting standards for loans provided by this pilot program. The borrower's credit and ability to make monthly mortgage payments will be evaluated using the Federal Housing Administration's Technology Open Scorecard (TOTAL) or a similar program. In the case that the mortgage involves multi-unit properties, the Secretary of HUD may establish underwriting standards.

For a mortgage to be eligible as a "zero-downpayment mortgage," as defined by this legislation, it must meet standards set forth by the Secretary.

This section requires a disclosure of incremental costs to the borrower of securing a zero-downpayment FHA-insured loan, as opposed to securing an FHA-insured loan requiring a downpayment.

The lender will be required to engage in loss mitigation upon the default of any mortgage insured under this legislation by FHA, in order to provide an alternative to foreclosure. The Secretary of HUD will be required to provide a report that compares the rates of default and foreclosure during the year for mortgages under this Act to mortgages for homes purchased using downpayment assistance provided under section 271 of the Cranston-Gonzalez-National Affordable Housing Act.

This section also gives the Secretary of HUD the authority, as it relates to mortgage insurance authority, to establish additional requirements as necessary or appropriate.

Because this is a pilot program that will provide an opportunity to study the effects of an FHA-insured zero-downpayment product, this section includes limitations on the ability of FHA to insure zero-downpayment mortgages. In any fiscal year, the total number of FHA-insured zero-downpayment mortgages may not exceed 50,000, nor may these products comprise more than 10 percent of the FHA portfolio.

Further, this pilot program will end if, at any time, the claim rate exceeds 3.5 percent, and will remain suspended until the claim rate is 3.5 percent or less. These measures will allow many families access to an FHA-insured zero-downpayment product and will provide data for use in determining the long-term fate of the FHA zero-downpayment program, all while protecting the FHA portfolio.

This pilot program will sunset on September 10, 2010 unless reauthorized.

The Government Accountability Office (GAO) will submit a report to Congress two years after the enactment of this Act regarding the performance of FHA-insured zero-downpayment mortgages authorized by this legislation.

The Secretary will have the authority to implement this program on an interim basis by issuing an interim rule and will solicit public comments before issuing a final rule.

Mortgage insurance premiums

Currently, under statute, a first-time homebuyer may not be charged an up-front FHA premium above 2 percent. This section amends current law so that FHA will have the ability to charge an up-front premium in excess of 2 percent.

General insurance fund

This section states that the General Insurance Fund may be used to carry out the FHA-insured zero-downpayment pilot program.

GAO study of expanded or extended program

This section requires that a GAO study of the FHA zero-downpayment program be conducted if the program is expanded to more than 50,000 mortgages or is extended past the sunset date of September 10, 2010. This study will examine the financial soundness of the MMIF and the effects of the expansion or extension on the MMIF.

CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

In compliance with clause 3(e) of rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italic, existing law in which no change is proposed is shown in roman):

NATIONAL HOUSING ACT

* * * * * * *

TITLE II—MORTGAGE INSURANCE

* * * * * * *

INSURANCE OF MORTGAGES

SEC. 203. (a) * * *

* * * * * * *

(c)(1) * * *

(2) Notwithstanding any other provision of this section, each mortgage secured by a 1- to 4-family dwelling that is an obligation of the Mutual Mortgage Insurance Fund or of the General Insurance Fund pursuant to subsection (v) and each mortgage that is insured under subsection (k) or section 234(c),, shall be subject to the following requirements:

(A) The Secretary shall establish and collect, at the time of insurance, a single premium payment in an amount not exceeding 2.25 percent of the amount of the original insured principal obligation of the mortgage. ⟦In⟧ *Except with respect to a mortgage insured under subsection (l), in* the case of a mortgage for which the mortgagor is a first-time homebuyer who completes a program of counseling with respect to the responsibilities and financial management involved in homeownership that is approved by the Secretary, the premium payment under this subparagraph shall not exceed 2.0 percent of the amount of the original insured principal obligation of the mortgage. Upon payment in full of the principal obligation of a mortgage prior to the maturity date of the mortgage, the Secretary shall refund all of the unearned premium charges paid on the mortgage pursuant to this subparagraph, provided that the mortgagor refinances the unpaid principal obligation under title II of this Act.

* * * * * * *

(l) ZERO-DOWNPAYMENT MORTGAGES PILOT PROGRAM.—

(1) INSURANCE AUTHORITY.—The Secretary may insure, and commit to insure, under this subsection any mortgage that meets the requirements of this subsection and, except as otherwise specifically provided in this subsection, of subsection (b).

(2) ELIGIBLE SINGLE FAMILY PROPERTY.—To be eligible for insurance under this subsection, a mortgage shall involve a property upon which there is located a dwelling that is designed principally for a 1- to 3-family residence and that, notwithstanding subsection (g), is to be occupied by the mortgagor as his or her principal residence, which shall include—

(A) a 1-family dwelling unit in a multifamily project and an undivided interest in the common areas and facilities which serve the project;

(B) a 1-family dwelling unit of a cooperative housing corporation the permanent occupancy of the dwelling units of which is restricted to members of such corporation and in which the purchase of such stock or membership entitles the purchaser to the permanent occupancy of such dwelling unit; and

(C) a manufactured home that meets such standards as the Secretary has established for purposes of subsection (b).

(3) MAXIMUM PRINCIPAL OBLIGATION.—

(A) LIMITATION.—To be eligible for insurance under this subsection, a mortgage shall involve a principal obligation in an amount not in excess of 100 percent of the appraised value of the property plus any initial service charges, appraisal, inspection and other fees in connection with the mortgage as approved by the Secretary.

(B) INAPPLICABILITY OF OTHER LOAN-TO-VALUE REQUIREMENTS.—A mortgage insured under this subsection shall not be subject to subparagraph (B) of paragraph (2) of subsection (b) or to the matter in such paragraph that follows such subparagraph.

(4) ELIGIBLE MORTGAGORS.—The mortgagor under a mortgage insured under this subsection shall meet the following requirements:

(A) FIRST-TIME HOMEBUYER.—The mortgagor shall be a first-time homebuyer. The program for mortgage insurance under this subsection shall be considered a Federal program to assist first-time homebuyers for purposes of section 956 of the Cranston-Gonzalez National Affordable Housing Act (42 U.S.C. 12713).

(B) COUNSELING.—

(i) REQUIREMENT.—The mortgagor shall have received counseling, prior to application for the loan involved in the mortgage, by a third party (other than the mortgagee) who is approved by the Secretary, with respect to the responsibilities and financial management involved in homeownership. Such counseling shall be provided to the mortgagor on an individual basis by a representative of the approved third party counseling

entity, and shall be provided in person to the maximum extent practicable.

(ii) TOPICS.—Such counseling shall include providing to, and discussing with, the mortgagor—

(I) information regarding homeownership options other than a mortgage insured under this subsection, other zero- or low-downpayment mortgage options that are or may become available to the mortgagor, the financial implications of entering into a mortgage (including a mortgage insured under this subsection), and any other information that the Secretary may require; and

(II) a document that sets forth the amount and the percentage by which a property subject to a mortgage insured under this subsection must appreciate for the mortgagor to recover the principal amount of the mortgage, the costs financed under the mortgage, and the estimated costs involved in selling the property, if the mortgagor were to sell the property on each of the second, fifth, and tenth anniversaries of the mortgage.

(iii) 2- AND 3-FAMILY RESIDENCES.—In the case of a mortgage involving a 2- or 3-family residence, such counseling shall include (in addition to the information required under clause (ii)) information regarding real estate property management.

(5) OPTION FOR NOTICE OF FORECLOSURE PREVENTION COUNSELING AVAILABILITY.—

(A) OPTION.—To be eligible for insurance under this subsection, the mortgagee shall provide mortgagor, at the time of the execution of the mortgage, an optional written agreement which, if signed by the mortgagor, allows, but does not require, the mortgagee to provide notice described in subparagraph (B) to a housing counseling entity that has agreed to provide the notice and counseling required under subparagraph (C) and is approved by the Secretary.

(B) NOTICE TO COUNSELING AGENCY.—The notice described in this subparagraph, with respect to a mortgage, is notice, provided at the earliest time practicable after the mortgagor becomes 60 days delinquent with respect to any payment due under the mortgage, that the mortgagor is so delinquent and of how to contact the mortgagor. Such notice may only be provided once with respect to each delinquency period for a mortgage.

(C) NOTICE TO MORTGAGOR.—Upon notice from a mortgagee that a mortgagor is 60 days delinquent with respect to payments due under the mortgage, the housing counseling entity shall at the earliest time practicable notify the mortgagor of such delinquency, that the entity makes available foreclosure prevention counseling that may assist the mortgagor in resolving the delinquency, and of how to contact the entity to arrange for such counseling.

(D) ABILITY TO CURE.—Failure to provide the optional written agreement required under subparagraph (A) may be corrected by sending such agreement to the mortgagor

not later than the earliest time practicable after the mortgagor first becomes 60 days delinquent with respect to payments due under the mortgage. Insurance provided under this subsection may not be terminated and penalties for such failure may not be prospectively or retroactively imposed if such failure is corrected in accordance with this subparagraph.

(E) PENALTIES FOR FAILURE TO PROVIDE AGREEMENT.—The Secretary may establish and impose appropriate penalties for failure of a mortgagee to provide the optional written agreement required under subparagraph (A).

(F) LIMITATION ON LIABILITY OF MORTGAGEE.—A mortgagee shall not incur any liability or penalties for any failure of a housing counseling entity to provide notice under subparagraph (C).

(G) NO PRIVATE RIGHT OF ACTION.—This paragraph shall not create any private right of action on behalf of the mortgagor.

(H) DELINQUENCY PERIOD.—For purposes of this paragraph, the term "delinquency period" means, with respect to a mortgage, a period that begins upon the mortgagor becoming delinquent with respect to payments due under the mortgage and ends upon the first subsequent occurrence of such payments under the mortgage becoming current or the property subject to the mortgage being foreclosed or otherwise disposed of.

(6) INAPPLICABILITY OF DOWNPAYMENT REQUIREMENT.—A mortgage insured under this subsection shall not be subject to paragraph (9) of subsection (b) or any other requirement to pay on account of the property, in cash or its equivalent, any amount of the cost of acquisition.

(7) MMIF MONITORING.—In conjunction with the credit subsidy estimation calculated each year pursuant to the Federal Credit Reform Act of 1990 (2 U.S.C. 661 et seq.), the Secretary shall review the program performance for mortgages insured under this subsection and make any necessary adjustments, which may include altering mortgage insurance premiums subject to subsection (c)(2), adjusting underwriting standards, and limiting the availability of mortgage insurance under this subsection, to ensure that the Mutual Mortgage Insurance Fund shall continue to generate a negative credit subsidy.

(8) UNDERWRITING.—For a mortgage to be eligible for insurance under this subsection:

(A) IN GENERAL.—The mortgagor's credit and ability to pay the monthly mortgage payments shall have been evaluated using the Federal Housing Administration's Technology Open To Approved Lenders (TOTAL) Mortgage Scorecard, or a similar standardized credit scoring system approved by the Secretary, and in accordance with procedures established by the Secretary.

(B) MULTI-UNIT PROPERTIES.—In the case of a mortgage involving a property upon which there is located a dwelling that is designed principally for a 2- or 3-family residence, the mortgagor meets such additional underwriting standards as the Secretary may establish.

(9) APPROVAL OF MORTGAGEES.—To be eligible for insurance under this subsection, a mortgage shall have been made to a mortgagee that meets such criteria as the Secretary shall establish to ensure that mortgagees meet appropriate standards for participation in the program authorized under this subsection.

(10) DISCLOSURE OF INCREMENTAL COSTS.—

(A) REQUIRED DISCLOSURE.—For a mortgage to be eligible for insurance under this subsection, the mortgagee shall provide to the mortgagor, at the time of the application for the loan involved in the mortgage, a written disclosure, as the Secretary shall require, that specifies the effective cost to a mortgagor of borrowing the amount by which the maximum amount that could be borrowed under a mortgage insured under this subsection exceeds the maximum amount that could be borrowed under a mortgage insured under subsection (b), based on average closing costs with respect to such amount, as determined by the Secretary. Such cost shall be expressed as an annual interest rate over the first 5 years of a mortgage.

(B) COORDINATION.—The disclosure required under this paragraph may be provided in conjunction with the notice required under subsection (f).

(11) LOSS MITIGATION.—

(A) IN GENERAL.—Upon the default of any mortgage insured under this subsection, the mortgagee shall engage in loss mitigation actions for the purpose of providing an alternative to foreclosure to the same extent as is required of other mortgages insured under this title pursuant to the regulations issued under section 230(a).

(B) ANNUAL REPORTING.—Not later than 90 days after the end of each fiscal year, the Secretary shall submit a report to the Congress that compares the rates of default and foreclosure during such fiscal year for mortgages insured under this subsection, for single-family mortgages insured under this title (other than under this subsection), and for mortgages for housing purchased with assistance provided under the downpayment assistance initiative under section 271 of the Cranston-Gonzalez National Affordable Housing Act (42 U.S.C. 12821).

(12) ADDITIONAL REQUIREMENTS.—The Secretary may establish any additional requirements for mortgage insurance under this subsection as may be necessary or appropriate.

(13) PILOT PROGRAM LIMITATIONS.—

(A) ANNUAL.—In any fiscal year, the aggregate number of mortgages insured under this subsection may not exceed 10 percent of the aggregate number of mortgages and loans insured by the Secretary under this title during the preceding fiscal year.

(B) TERM OF PROGRAM.—The aggregate number or mortgages insured under this subsection may not exceed 50,000.

(14) PROGRAM SUSPENSION.—

(A) IN GENERAL.—Subject to subparagraph (C), the authority under paragraph (1) to insure mortgages shall be suspended if at any time the claim rate described in subparagraph (B) exceeds 3.5 percent. A suspension under this

subparagraph shall remain in effect until such time as such claim rate is 3.5 percent or less.

(B) FHA TOTAL SINGLE-FAMILY ANNUAL CLAIM RATE.—The claim rate described in this subparagraph, for any particular time, is the ratio of the number of claims during the 12 months preceding such time on mortgages on 1- to 4-family residences insured pursuant to this title to the number of mortgages on such residences having such insurance in force at that time.

(C) APPLICABILITY.—A suspension under subparagraph (A) shall not preclude the Secretary from endorsing or insuring any mortgage that was duly executed before the date of such suspension.

(15) SUNSET.—No mortgage may be insured under this subsection after September 30, 2010, except that the Secretary may endorse or insure any mortgage that was duly executed before such date.

(16) GAO REPORTS.—The Comptroller General of the United States shall submit a report to the Congress not later than 2 years after the date of the enactment of this subsection, and annually thereafter, regarding the performance of mortgages insured under this subsection.

(17) IMPLEMENTATION.—The Secretary may implement this subsection on an interim basis by issuing an interim rule, except that the Secretary shall solicit public comments upon publication of such interim rule and shall issue a final rule implementing this subsection after consideration of the comments submitted.

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TITLE V—MISCELLANEOUS

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ESTABLISHMENT OF GENERAL INSURANCE FUND

SEC. 519. (a) * * *

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(e) The General Insurance Fund shall not be used for carrying out the provisions of sections 203(b) (except as provided in section 203(v)), 203(h) [and 203(i)]*, 203(i), and 203(l)*, or the provisions of section 213 to the extent that they involve mortgages the insurance for which is the obligation of the Cooperative Management Housing Insurance Fund created by section 213(k), or the provisions of sections 223(e), 233(a)(2), 235, 236 and 237; and nothing in this section shall apply to or affect mortgages, loans, commitments, or insurance under such provisions.

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DISSENTING VIEWS OF RON PAUL

The Zero Downpayment Act of 2006 (H.R. 3043) establishes a pilot program waiving the requirement that a homebuyer make a downpayment in order to be eligible for a Federal Home Administration (FHA) insured mortgage. This bill distorts the housing market, and thus weakens the general economy. Repealing the downpayment requirement could also increase the default rate of FHA insured mortgages and thus increase the costs of the FHA insured mortgage program to the taxpayer. These concerns alone would justify rejecting this bill. However, my main objection to this legislation is that it furthers the something-for-nothing mentality that is incompatible with a free society.

The requirement that homebuyers make a downpayment ensures that a prospective homebuyer is a worthy credit risk and reduces the likelihood of default. After all, people are less likely to abandon property if they have invested substantial savings in the property in the form of a downpayment. The sponsors of H.R. 3043 claim that modern methods of evaluating whether someone poses a good credit risk eliminates the need for the downpayment requirement. However, while modern techniques to measure credit worthiness can measure one's income and credit history, they cannot measure a person's willingness and ability to delay current consumption to ensure one can make monthly mortgage payments. Eliminating the downpayment requirement makes it more likely that people unwilling to save to insure they can make their monthly mortgage payments will receive FHA insured home loans. Therefore, this program increases the rate of default on FHA loans, and thus increases the costs to taxpayers of the FHA program. HUD claims it can recoup the loss of a mortgage by increasing premium payments. However, if the zero mortgage policy raises the default rate, the higher premium will be useless in recouping revenue lost from eliminating the downpayment requirement.

A friend of mine was informed by a mortgage broker that his business was experiencing an increase in defaults. According to this mortgage broker, one reason for this was the failure to require downpayments; private industry has excessively relied on credit history information instead of a downpayment to entice more people into the home market. H.R. 3043 authorizes the federal government to repeat this folly. Does anyone really believe the federal government will succeed where the private sector has failed? Before answering that question, my colleagues should consider that FHA foreclosure rates are already at record levels! Of course, if default rates rise, Congress can pass a new program making the taxpayers responsible for the monthly mortgage payments of holders of FHA insured loans.

H.R. 3043 will harm the economy by artificially increasing the demand for housing, causing resources to be diverted from other uses into housing to meet this government-created demand. Allocating resources based on market-distorting government programs insures that those resources will not be devoted to their highest-valued use. Thus, government interference in the economy results in a loss of economic efficiency and, more importantly, a lower standard of living for all citizens. The only policy guaranteed to maximize economic growth and the well being of citizens is to allow the actions of private individuals in a free-market to determine the allocation of resources.

Government polices have already artificially inflated the demand for housing, creating a housing bubble. While the temporary effect of this bubble may appear beneficial to homebuyers and homebuilders, eventually they will suffer when the housing bubble bursts. Encouraging more people to enter an already-inflated market will only increase the economic damage and human suffering the bursting of the housing bubble will cause.

By increasing the demand for housing, H.R. 3043 will also increase the price of housing. Those unable to qualify for an FHA insured mortgage might find themselves priced out of the housing market. Thus, an unintended consequence of this bill could be to reduce some people's ability to obtain affordable housing!

Finally, the most important reason to reject this bill is that it undermines liberty. It is bad enough that this committee has expanded the handout state with legislation like the misnamed "America Dream Downpayment Act." This bill would now relieve those already receiving help from the taxpayers through the FHA program of the modest requirement that they save for a downpayment. Every time Congress makes it easier for people to receive handouts from the government, we erode people's willingness and ability to care for themselves. Eventually, the recipients of this government largesse stop thinking of themselves as independent citizens and begin viewing themselves as wards of the state. It is impossible to maintain a free society when a large number of people look to the state to meet every one of their needs.

By creating a pilot program relieving some participants in the Federal Home Administration program of the requirement that they pay a downpayment, H.R. 3043 increases the risk of default, thus increasing the program's cost to the taxpayer. H.R. 3043 also encourages the something for nothing mentality that is inconsistent with a free society. Therefore, the Financial Services Committee should reject this bill.

RON PAUL.

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