FHA Increases Upfront MIP Fee; Raises Credit Score Requirement; Reduces Seller Concessions

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As promised in December, the Federal Housing Administration has announced the details of changes intended to strengthen its capital reserves which were reported to be headed into dangerously low territory late last year. The changes are designed to increase the FHA's income from customers while reducing its portfolio's risk.

FHA Commissioner David Stevens comments:

"Striking the right balance between managing the FHA's risk, continuing to provide access to underserved communities, and supporting the nation's economic recovery is critically important,"

"When combined with the risk management measures announced in September of last year, these changes are among the most significant steps to address risk in the agency's history. Additionally, by continuing to provide affordable, responsible mortgage products, FHA will support the housing market's recovery. Importantly, FHA will remain the largest source of home purchase financing for underserved communities."

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Announced FHA Policy Changes:

Mortgage insurance premium (MIP) will be increased to build up capital reserves and bring back private lending

- The first step will be to raise the up-front MIP by 50 bps to 2.25% and request legislative authority to increase the maximum annual MIP that the FHA can charge.
- If this authority is granted, then the second step will be to shift some of the premium increase from the up-front MIP to the annual MIP.
- This shift will allow for the capital reserves to increase with less impact to the consumer, because the annual MIP is paid over the life of the loan instead of at the time of closing
- The initial up-front increase is included in a Mortgagee Letter to be released tomorrow, January 21st, and will go into effect in the spring.

Update the combination of FICO scores and down payments for new borrowers.

- New borrowers will now be required to have a minimum FICO score of 580 to qualify for FHA's 3.5% down payment program. New borrowers with less than a 580 FICO score will be required to put down at least 10%.
- This allows the FHA to better balance its risk and continue to provide access for those borrowers who have historically performed well.
- This change will be posted in the Federal Register in February and, after a notice and comment period, would go into effect in the early summer.

Reduce allowable seller concessions from 6% to 3%

- The current level exposes the FHA to excess risk by creating incentives to inflate appraised value. This change will bring FHA into conformity with industry standards on seller concessions.
- This change will be posted in the Federal Register in February, and after a notice and comment period, would go into effect in the early summer.

Increase enforcement on FHA lenders

- Publicly report lender performance rankings to complement currently available Neighborhood Watch data – Will be available on the HUD website on February 1.

  o This is an operational change to make information more user-friendly and hold lenders more accountable; it does not require new regulatory action as Neighborhood Watch data is currently publicly available.

- Enhance monitoring of lender performance and compliance with FHA guidelines and standards.

o Implement Credit Watch termination through lender underwriting ID in addition to originating ID.
o This change is included in a Mortgagee Letter to be released tomorrow, January 21st, and is effective immediately.

- Implement statutory authority through regulation of section 256 of the National Housing Act to enforce indemnification provisions for lenders using delegated insuring process

o Specifications of this change will be posted in March, and after a notice and comment period, would go into effect in early summer.

- HUD is pursuing legislative authority to increase enforcement on FHA lenders. Specific authority includes:

o Amendment of section 256 of the National Housing Act to apply indemnification provisions to all Direct Endorsement lenders.This would require all approved mortgagees to assume liability for all of the loans that they originate and underwrite
o Legislative authority permitting HUD maximum flexibility to establish separate "areas" for purposes of review and termination under the Credit Watch initiative. This would provide authority to withdraw originating and underwriting approval for a lender nationwide on the basis of the performance of its regional branches

In addition to the changes proposed today, the FHA is continuing to review its overall response to housing market conditions, and continuing to evaluate its mortgage insurance underwriting standards and its measures to help distressed and underwater borrowers through FHA/HAMP and other FHA initiatives going forward.

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