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"POSSIBLE RESPONSES TO RISING MORTGAGE FORECLOSURES"

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Good morning Chairman Frank, Ranking Member Bachus, and distinguished members of the Committee. I want to thank you for the opportunity to speak today first about the reasons for the surge in mortgage foreclosures, specifically in the subprime arena, and then on potential ways that FHA can work to curtail a number of potential future foreclosures.

As you know FHA's purpose is to serve low to moderate income homebuyers, including those who have less-than-perfect credit and little savings for a downpayment. We do this by offering mortgage insurance to qualifying borrowers that can illustrate the ability to repay the loan as well as insurance premiums in a timely manner. Knowing that the loan is backed by the full faith and credit of the U.S. government, lenders are able to offer homebuyers a loan at a prime interest rate.

I would like to clarify for the record that FHA does not insure subprime loans. FHA requires borrowers to meet strict underwriting criteria, including that they must document income, not just state it. Also, unlike most subprime mortgages, FHA does not offer teaser rates or prepayment penalties. And if borrowers do get in over their heads, if they lose their job, or become ill, or have other life events that prevent them from keeping current on their mortgage, we have one of the best loss mitigation programs. Last year we assisted 75,000 FHA-insured families by preventing foreclosure through our loss mitigation program.

FHA goes the extra yard to keep homeowners in their homes. We not only want to get them into a home but we also want them to fulfill the American dream by remaining in their homes. We fully recognize the crippling effect foreclosure has on homeowners, communities, lending institutions and real estate investors.

It is best for everyone involved that the borrower never be threatened by foreclosure in the first place. This brings me to the importance of another consumer protection tool we support, housing counseling. HUD's Housing Counseling Program supports a nationwide network of approximately 2,300 housing counseling agencies. In Fiscal Year 2006, these agencies provided critical advice and guidance to over 1.6 million households.

An increase in funding for the Program, for which $41.58 million was appropriated for Fiscal Year 2007, allows us to deliver quality housing counseling to thousands of households facing mortgage delinquency and foreclosure, making available to them aggressive loss mitigation, lender advocacy, and other tools and strategies to help them modify their loans, refinance, or otherwise escape the high interest rates, hidden costs, and prepayment penalties to name a few.

The rise in subprime foreclosures is far from a surprise to most people in this room. At my confirmation hearing before the Senate Committee on Banking, Housing and Urban Affairs in May of 2005, I mentioned that I thought many subprime borrowers would have been, and could be, better served by FHA.

I do not mean to infer that all subprime lending is harmful. The subprime market served many borrowers very well, and in many cases this option was the only way for them to achieve homeownership. I remember reading a great quote on this subject by Alan Greenspan from a 1997 speech: “So while we should applaud the "democratization" of our credit markets over the years, we must be vigilant to the risks of excess, both by lenders and by consumers.”

There have been excesses by both lenders and consumers. While I recognize that even one foreclosure still hurts families, the number of borrowers that were not well served by subprime lenders is not at catastrophic levels. MBA estimates that subprime borrowers make up only fourteen percent of all home mortgages, and of those mortgages only thirteen percent are experiencing delinquencies.

Still with the Center for Responsible Lending estimating that by the end of 2006, 2.2 million households in the subprime market will have lost their homes to foreclosure or hold subprime mortgages that will fail over the next several years; we recognize the need to reach out to subprime borrowers.

My single-family team proposed procedural and process improvements that were well received by our industry partners, but they were not enough. That is when we decided to push for real change – to modernize the FHA.

In recent years, as the subprime industry grew significantly, this Committee was well ahead of the curve in understanding the role a modernized FHA could play in offering those same homebuyers a safer, more affordable financing option than subprime loans. Your leadership on this issue was well received when H.R. 5121, the FHA Modernization Act, passed the House 415 – 7.

Under the modernization proposal FHA would be given the expanded authority, to charge insurance premiums commensurate with risk, and to increase maximum loan amounts. This would allow us to “dive deeper” into the pool of homeowners who could benefit from a refinancing of their subprime loan. Modernizing FHA is the most practical and immediate way to address the needs of a large number of troubled subprime borrowers. FHA modernization legislation has already been filed in both the House and in the Senate.

With expanded authority to set insurance premiums commensurate with risk, FHA could potentially assist tens of thousands more borrowers who need an exit strategy from their subprime mortgages. Under today's restricted premium limits and maximum loan amounts, FHA simply cannot reach these borrowers who need the safety that FHA can provide. The broadest group of subprime borrowers needing to refinance is beyond FHA’s ability to serve in a sound manner.

Subprime borrowers are paying interest rates up to 10 percent or more. Refinancing into an FHA-insured mortgage can, on a $200,000 mortgage, save a qualifying borrower $3,000 to $4,000 in the first year. Thus, FHA could save borrowers substantial money and do so in a financially sound manner.

I am pleased to report that there are actually an increasing number of conventional borrowers who are currently refinancing into FHA. In today's market environment, it is safe to say that a significant portion of these loans are subprime. For the first five months of FY2007, conventional-to-FHA refinancings were up 94 percent from the same period in FY 2006. If this current trend continues, FHA will endorse over 100,000 conventional-to-FHA refinancings in FY2007. That compares with a previous peak of 64,474 in FY2002.

In efforts to assist more subprime to FHA refinances, we have been working hard on outreach. We began this type of outreach as early as October of last year. We have conducted hundreds of meetings nationwide with groups of housing counseling agencies, lenders and realtors to promote the refinancing through FHA of subprime and other high cost loans, particularly loans which are due to reset.

We have reached out to State agencies in Ohio, Pennsylvania, West Virginia and Maryland, as well as county agencies and local coalitions to create partnerships in outreach and to secure funding to "fill the gap" that exists in some instances between maximum FHA eligible mortgages and the costs to refinance a subprime loan. Our efforts at reaching out to our industry partners and ultimately to borrowers continues and remains strong.

While FHA as it stands today is witnessing an upward trend of refinances by likely subprime borrowers, and our outreach efforts are moving forward, we are still considering some programmatic changes to assist more subprime borrowers in trouble.

FHA recognizes that many subprime borrowers have mortgage debt that far exceeds the value of their homes. Being financially "upside down" in their homes can result from factors such as their inability to make the increased monthly payments after the mortgage interest resets or depreciation in the value of their home.

In addition, one factor that may prohibit many of these borrowers from refinancing out of their subprime mortgage is the cost of the prepayment penalty, a common feature of subprime loans.

Staff has been analyzing our ability to restructure our underwriting guidelines to serve more of the troubled subprime borrower pool. Keep in mind that while we would like to stabilize the mortgages of as many homeowners as possible, I have to protect the solvency of the FHA Insurance Fund, so there will be a limit to what we can accomplish.

FHA can help those who:

1.) Can afford payments on a fixed-rate loan at a market rate of interest, with FHA insurance premiums;

2.) Have a property with sufficient equity to qualify for FHA financing;

3.) Can meet other standard underwriting criteria that balance the overall risk of the mortgage; and

4.) Are owner-occupiers.

FHA more than likely cannot and should not try to help those subprime borrowers who:

1.) Took out subprime loans because of an inability to document income and assets;

2.) Are involved in speculative investments;

3.) Who have accumulated other debts that make it impossible to sustain their current property with a new fixed-rate loan with current income, or who lack sufficient positive equity in their homes.

I want to restate, we would like to help as many subprime borrowers as possible. I am very proud of the efforts HUD staff across the country have made to get the word out that FHA can help and is helping.

In closing, I would again like to thank this Committee for inviting me here today. I would also like to thank you for your leadership, and understanding of the need for FHA to be modernized to help low and moderate income families achieve the dream of homeownership – and to stay in it. Thank you.