Frequently Asked Questions on FHA Lending

Business Considerations Regarding the Decision to Become an FHA Lender

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FEDERAL RESERVE BANK OF BOSTON™

Frequently Asked Questions – Becoming an FHA Lender

Economic related criteria that a bank might consider in determining whether to offer the FHA loan product.	
What type of customer would an FHA loan service?	• FHA loans are for primary residences. • The product is primarily for customers that can only afford a small down payment and therefore may have difficulty obtaining a conventional mortgage product. • Loan advances can be as high as 97% of LTV. • Can help to stimulate market by allowing first time buyers to enter market. • Possible niche for customers who want to refinance but their home values dropped leaving them with a marginal amount of equity. • May be useful for higher end buyer wishing to leverage with a lower down-payment. • FHA mortgage insurance is traditionally less expensive than private mortgage insurance. • The 'down payment' can be 'borrowed' from permissible second parties. • Underwriting criteria regarding personal credit history can be more lenient when qualifying for an FHA loan compared to conventional credit. This is especially so for the new 'Hope For Homeowners' program.
What are the different ways that an institution can participate in the FHA Lending Program?	• An FHA '*mortgagee'* can originate, underwrite, fund, service and/or own FHA insured loans. Mortgagees are also known as <u>Full-Eagles</u> because they perform any lender function on FHA loans. • An FHA loan '*correspondent*' can only originate loans that are underwritten by their sponsoring mortgagee, and also are known as <u>Mini-Eagles</u>. A correspondent cannot underwrite, own or service FHA insured loans. They must use a mortgagee to sponsor them in an origination. Many banks become a Mini Eagle given expertise and accompanying staffing requirements necessary to become a Full Eagle, that imply minimum volumes to cover increased overhead costs.
What financial opportunities are there in each part of the FHA mortgage process: origination, underwriting, servicing and holding?	• Originators earn money based on the origination fee (max 1%) and discount points (max 2%) charged to the borrower. • Sponsoring mortgagee earns money from underwriting and funding fees. • Servicers receive a fee on an ongoing basis. • Holders of FHA loans will receive principal and interest payments based on the particular loan.
What is the potential for FHA loan volume?	• The FHA does not produce volume data by community on a regular basis. • An attached graph represents the growth of FHA loans originated in the New England region from 10/2007 – 8/2008 period. **Please see Attachment 1.**
Given home prices and household incomes in my community, will I have customers for whom the FHA program is a fit?	• There are no maximum household income requirements as part of the FHA loan program so technically any household can have an FHA mortgage. Additionally, maximum loan amounts have been increased recently by the FHA and consider the average home price in the community. **See Attachment 2 for an applicability analysis for selected New England towns.** This analysis is considered conservative, and therefore further discussion with an underwriter is advised.

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Criteria related to the FHA loan product in comparison to other loan products	
What has been the recent history of the FHA product in comparison to other loan products?	• Securitization channels for FHA 'competitor' products constructed by private markets have been disrupted and do not appear ready to recover in near term. . • Key features of the FHA loan product – lower down payment, mortgage insurance, consideration of personal credit history – distinguish it at this time from private sector, non-agency supported mortgages.
What other 'agency' sponsored programs exist and are there differences relative to the FHA program?	• State housing agencies offer various affordable mortgages and other services targeted at low- and moderate-income individuals. **Please see Attachment 3 for details of New England State program requirements and qualification criteria.**
Criteria related to the underwriting of FHA loans	
What are the loan size limits for FHA loans?	• Loan size is partially dictated by community related limits imposed imposed by the FHA. A 'map' of limits on can be found on the FHA website: http://www.fhaoutreach.com • The Economic Stimulus Act of 2008 permits FHA to insure loans on amounts up to 125 percent of the area median house price, when that amount is between the national minimum ($271,050) and maximum ($729,750).
What are the FHA Underwriting Guidelines with regard to Debt to Income (DTI) ratios?	• The current DTI requirement for manually underwritten loans is 29% of gross monthly income up to 41% of all debt service and related expenses. A ratio exceeding 29% may be acceptable only if significant compensating factors exist and/or FHA's automated underwriting system approve based on the strengths of the borrower. More information on DTI requirements can be found at: http://www.hud.gov/offices/hsg/sfh/ref/sfhp2-12.cfm • Compensating factors include the following: Ability to pay housing expenses for new mortgage over the past 12-24 months; large down payment; accumulate savings and conservative attitude towards debt; and documented substantial cash reserves. • In actual practice, loans with compensating factors can be approved with back end ratios as high as 55%. Typically the highest that get approved are in the 45% range. • The 'Hope For Homeowners' program, effective October 1, 2008, is aimed at borrowers facing difficulty in paying their mortgages will be eligible to refinance into affordable FHA-insured mortgages. . Details of the program, which include write downs of the mortgage and equity sharing with FHA, can be found at: http://portal.hud.gov/portal/page?_pageid=73,7601299&_dad=portal&_schema=PORTAL
Who is eligible for an FHA mortgage?	• Anyone who meets the credit, income, and employment requirements is eligible for a FHA mortgage. The property securing the mortgage must be the purchaser's primary residence. • U.S. citizenship is not required for a FHA mortgage. Proof of legal US residency is required. A social security card is necessary to qualify for a FHA mortgage.

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What is mortgage insurance, and how does it apply to FHA mortgages?	• Mortgage insurance is required to secure an FHA mortgage. The insurance premium is collected by the lender and paid to the FHA in the form a one time payment as well as an ongoing annual payment. The upfront payment is typically 1.75% of the loan balance, with a monthly charge of 0.55 % per year. • Pricing associated with the 'Hope For Homeowners' program is higher given the greater risk in this program. The upfront mortgage insurance premium is 3% of the outstanding loan balance, in addition to a 1.5% annual premium. See the following disclosure for additional program details: http://portal.hud.gov/pls/portal/docs/PAGE/FHA_HOME/CONSUMERS/H_FOR_H_CONSUMER_FACT-SHEET/H4H%20CONSUMER%20FACT%20SHEET.DOC. • Consideration has been given to adjusting FHA pricing in light of significant increases in volumes, and therefore should be monitored. •
What are the different types of FHA mortgages?	• Like conventional mortgages, there are several different types of FHA mortgages, including both fixed rate and adjustable rate products. A list is provided on the FHA website that can be accessed via the following link: www.fha.gov
If the decision is made not to underwrite, but only to originate, who are the underwriters serving my community?	• Sponsoring lenders (underwriters) come in a range of forms, from national banks to local banks to non-bank mortgage companies. • The FHA has a search tool on its website that will provide list of underwriters in your area. http://locator.fha.gov/
Criteria related to the formal application process by which an institution becomes an originator, underwriter or servicer.	
What is the approval process to become involved in the FHA loan program?	Cover sheet for application: http://portal.hud.gov/fha/sf/lenders/titl2app.pdf For Supervised Loan Correspondent applications, the following must be provided: (1) Application Form – HUD 11701. (2) $1,000 Application fee. (3) Combination Sponsor/Funding letter. (4) Quality control plan. (5) State DBA Approval, if applicable. For Supervised Mortgagee additional bond and insurance are required as stated in HUD Handbook 4060.1, Chapter 3. Send Application Form 11701 and Exhibits to FHA Lender Approval & Recertification Division in Washington DC Mail $1,000 Application Fee and transmittal form to FHA hand lockbox in Atlanta, GA FHA Handbook: http://portal.hud.gov/fha/reference/4060-1.doc

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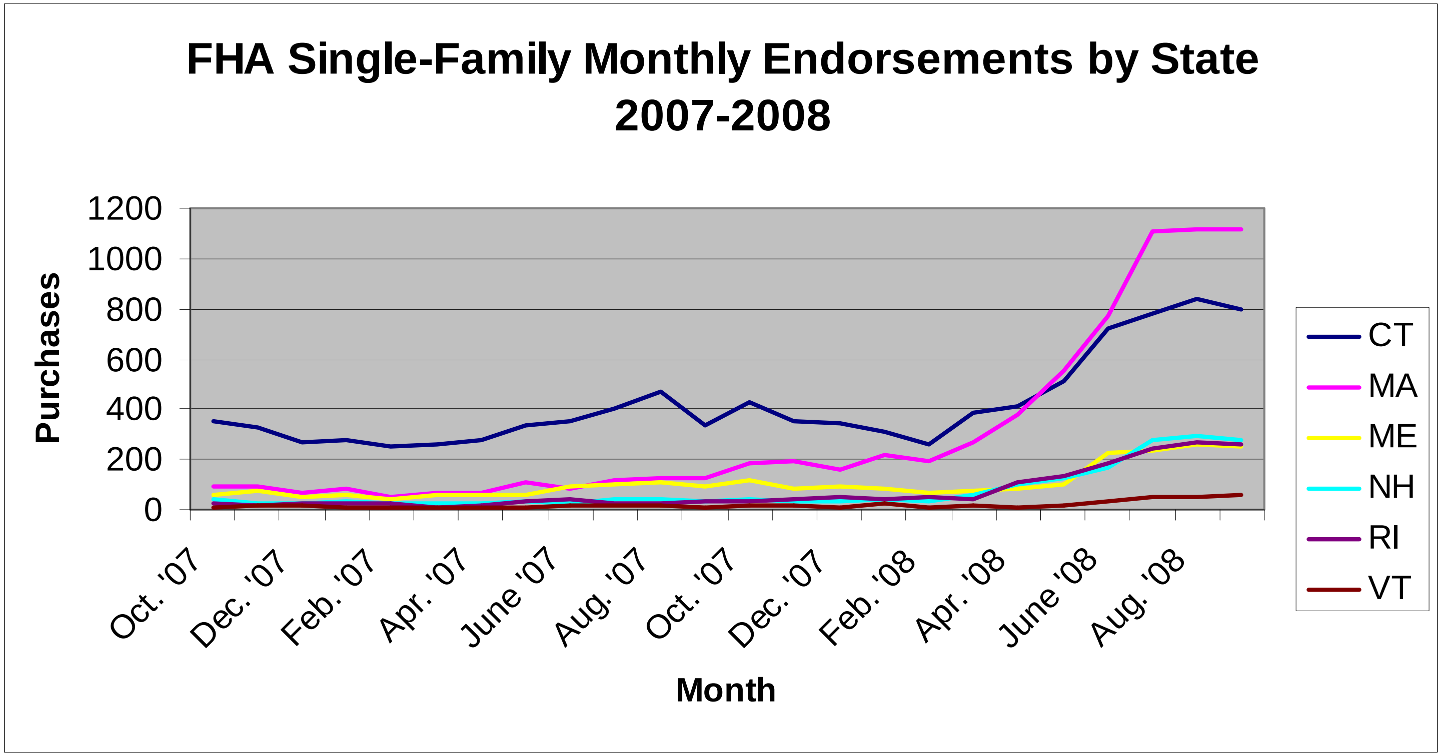
Are there eligibility requirements to become an originator (Correspondent or Mini-Eagle)?	Yes, the FHA does have eligibility requirements to become an originator. (1) You must be a Corporation, LLC or partnership. (2) Must be a licensed Lender. (3) Maintain a permanent office with at least two staff. (4) Must have one officer with three years experience. (5) No debarments or suspensions. (6) A quality control Plan. (7) Net worth and liquid assets requirements - $63M to be a loan correspondent (plus $25M per branch). Please reference HUD Handbook 4060.1 for complete details on above requirements
Are there eligibility requirements to become an underwriter (Mortgagee, Sponsor, or Full Eagle)?	Yes, the FHA does have underwriter eligibility requirements. (1) The form of business must be a corporation, partnership, or other chartered institution. (2) The company must have the required business licenses. (3) The company must have State approval for their legal name and d/b/a. (4) Supervised mortgagees must have a net worth of at least $250M. (5) Supervised mortgagees must have liquidity assets equal to 20% of net worth or $100M, whichever is lesser. Please reference HUD Handbook 4060.1 for complete details on above requirements
Are there eligibility requirements to become a servicer?	• A **mortgagee** can originate, underwrite, fund, service and/or own FHA insured loans. Mortgagees are also known as Full-Eagles because they can do any lender function on FHA loans. • Generally, only mortgagees (Full Eagles) can retain servicing rights. However, the FHA does allow correspondents to retain servicing rights. When banks apply for correspondent status simultaneously the bank also applies for servicing rights from the FHA.
What causes FHA loans to be returned?	• FHA loans can be denied insurance from the FHA if they determine that there is false documentation, misleading information, or any form of fraud or misrepresentation on the part of any of the parties involved. If the mortgagee fails to meet a statutory or regulatory requirement, the FHA also has the ability to reject insurance. • Credit Watch Termination Initiative holds single family mortgagees accountable for poorly performing loans that they originated or underwrote. This process is administered by the Quality Assurance Division (QAD) in FHA Headquarters (see 24 CFR 202.2 and 202.3(c)(2)). • QAD compares the proportion of a mortgagee's loans that became 90 days delinquent early in their term to the proportion of early defaults and claims on all insured loans. A mortgagee (or branch) with default and claim rates that are two or more times the average for a HUD Field Office jurisdiction may become ineligible to originate or underwrite further single family insured mortgages in that area. Before any restriction takes effect, a mortgagee will have an opportunity to present its analysis of the early defaults and claims, and conclusions about its accountability to FHA officials in Washington, DC.

Frequently Asked Questions – Becoming an FHA Lender

Does the underwriter (mortgagee) have an ability to return loans to the originator (correspondent)?	• No, the underwriter (mortgagee) is responsible for the actions of each of its loan originators (correspondents) in originating FHA-insured mortgages.
Does the FHA perform reviews of servicers? If so, how often is this done and what are the penalties for less than satisfactory reviews?	• The FHA, at any time, may require a Title II mortgagee to report on any matter related to its FHA operations. This may include the inspection of a mortgagee's mortgage loan files, reports, records, books, or accounts. Representatives of the Office of Inspector General and/or Quality Assurance Division (QAD) may periodically visit a mortgagee's office to review its origination and servicing procedures. • HUD may take an administrative action against individuals, companies and lenders for actions or omissions in connection with FHA mortgage insurance programs. Depending on the nature of the incident, HUD can take a number of actions, such as: **(1)** Limited Denial of Participation **(2)** Debarment or Suspension **(3)** Civil Money Penalties
As the servicer, is there reporting required by the FHA?	• The only specific reporting required by the FHA is if there are any findings related to the quality control program. A mortgagee's Quality Control Program must ensure that findings discovered by employees during the normal course of business and by quality control staff during reviews/audits of FHA loans are reported to HUD within 60 days of the initial discovery. • Findings of fraud or other serious violations must be immediately referred, in writing to the Director of the Quality Assurance Division in the HUD Homeownership Center (HOC) having jurisdiction (determined by the State where the property is located).
Is there a minimum loan volume required by the FHA to be an underwriter (Full-Eagle)?	• No, there is no minimum volume to be an underwriter. However, before obtaining Direct Endorsement authority, the mortgagee must submit a number of FHA mortgage loans to HUD for review.

Attachment 1



Source: HUD Website http://www.hud.gov/offices/hsg/comp/rpts/sfend/sfend.xls

Attachment 2
Estimated FHA Loan Affordability for Selected Towns

City & State	Trulia Median Sales Price	FHA Mortgage Maximum	2008 Estimated Median Family Income (EMFI)	FHA Maximum Loan $ for 2008 EMFI	FHA Maximum Loan $ Amount for EMFI as a % of Median Sales Price
Manchester, CT	$248,000	$440,000	$81,000	$249,139	101%
Milford, CT	$307,000	$387,500	$74,900	$230,377	75%
Brockton, MA	$179,676	$523,750	$79,500	$244,526	124%
Danvers, MA	$312,000	$523,750	$78,800	$242,373	78%
Nantucket, MA	$315,500	$729,750	$74,000	$227,609	72%
Hooksett, NH	$219,000	$302,500	$66,200	$203,618	67%
Salem, NH	$265,500	$523,750	$82,300	$225,138	85%
Warwick, RI	$175,400	$475,000	$68,300	$210,077	120%
Woonsocket, RI	$162,000	$475,000	$68,300	$210,077	130%

Notes: Trulia Median Sales Prices as of August 27, 2008 (Trulia.com).
FHA Mortgage Maximum (HUD.gov).
EMFI = 2008 HUD Estimated Median Family Income (HUD data).
FHA Maximum calculated with GNMA online qualification tool (Ginniemae.gov).
FHA Maximum Loan for EMFI calculated by dividing FHA Maximum Loan by Trulia Median Sales Price.

Attatchment 3

FHA Loan Product: Business Decision Criteria for Consideration
New England Housing Agency Programs

	FHA		MassHousing		Connecticut	Maine	New Hampshire	Vermont	Rhode Island
	FHA	**FHA Secure**	**My Community**	**Home Saver**	**CT FAMILIES PROGRAM**	**Maine State Housing Authority**	**New Hampshire Banking Department**	**Vermont Housing Finance Agency (VHFA)**	**Rhode Island Housing**
Sources of Data	http://www.fha.com	http://www.fha.com	www.masshousing.com/homeownership	www.masshousing.com/homeownership	www.chfa.org/firsthome/ctfamilies.htm	http://www.mainehousing.org/Documents/Brochures/Brochure-Foreclosure.pdf	http://www.nh.gov/banking/outreach.html	http://www.vhfa.org/homeownership/consumer_assistance.php	http://www.rhodeislandhousing.org/sp.cfm?pageid=2089
Primary Purpose	Gennerally first time homebuyer	Refi from ARM	Refi - out of high cost	Foreclosure Prevention	Refi from ARM	If the loan was through Maine Housing, then the borrower is offered servicer workouts like informal payment plans, formal payment plans, term modification orforbearance. In addition, borrowers may be eligible for a property tax exemption or a property tax refund. Maine also encourages borrowers to apply for the mortgage relief fund.	There is no refinance program. The state will review loan docs, explain them to borrowers, and offer credit counseling.	If the loan was through VHFA, then the borrower is offered servicer workouts like loan modification, extended repayment or forbearance.	There is no refinance program. The Rhode Island Housing Help Center provides advice to borrowers and helps them to negotiate with their lender. This counsel is available to all borrowers in Rhode Island.
Counseling Requirement	No	No	No	Yes	No				
Typical Term	30 year	There are different product types	30 yr and less	30 yrs	30 yrs for both 1st and 2nd mortgages				
Type	Fixed - 1yr ARM - 3 /1 ARM	Fixed - 1yr ARM - 3 /1 ARM	Fixed	Fixed	Fixed				
Points	Yes	Yes	Borrower's Choice	No Points	Yes				
Closing costs	Some can be rolled	Some can be rolled	Yes - can be rolled	Can be reduced	Yes- up to one point as an origination fee. The cost can be financed through a 2nd mortgage				
Requires Escrow	Yes	Yes	Yes	Yes	Yes				
Loan Limit (single fam)	Up to $739,000* http://www.fha.com/lending_limits.cfm	Up to $739,000* http://www.fha.com/lending_limits.cfm	$417,000	$417,000	differs by county and \www.chfa.org/FirstHome/CT-FAMLIES-Brochure.pdf	Because these programs only provide advice to borrowers they are grouped together, and they do not contain further information.			
Mortgage Insurance	Yes	Yes	Yes - discounted for LMI	No MI	Yes				
Credit decisionmaker?	Bank	Bank	Bank	Bank	Bank				
Who is Servicer	Depends	Depends	MassHousing	MassHousing	Depends				
Salable?	Yes	Yes	Yes - MassHousing	Yes - MassHousing	Yes				
Primary Residence only?	Yes	Yes	Yes	Yes	Yes- includes owner occupied one through four families				
Max DTI	31/43	31/43 but compensatiing factors may be considered	50% (back end)	50% (back end)	31/43				
Max LTV	98%	see mortgagee letter 2007-11	Up to 100%	105%	see mortgagee letter 2007-11				
Cash Out Availabilty?	Yes	Yes ($500 max)	No	No	No				
Income Restrictions	No	No	Yes - by town	Yes - by town	Yes, by town				
Other:	No min credit score, however some wholesalers are imposing their own credit score restrictions. Streamlined refi available.	Can be delinquent on current mortgage- but NOT a requirement (Two types of FHA Secure)		Minimum credit score- 560; risk based pricing.	Can be delinquent only if the delinquency is a result of the interest rate and/or payment increase. CT Families program uses the underwriting standards from FHASecure.				
Pros	Flexible downpayment sources		LMI product	Foreclosure rescue product	Uses underwriting standards from FHASecure				
	Government insured		Flexible	Allows for High LTV	Borrowers with high LTVs will need to get a 2nd mortgage				
	High LTV		High LTV	Low credit score	Can have low credit score due to rate reset only.				
Cons	Must be an approved FHA lender		Income limits may exclude higher income folks in a bad loan	Income restrictions: up to $110,700 depending on the location	Income Restrictions: www.chfa.org/FirstHome/CT-FAMLIES-Brochure.pdf				
	More dsifficult to underwrite, ususally act as broker		Loan limit restricting in some markets	Loan limit restricting in some markets					
	High loan limits can misleading in practice - actually based on property location								