HOUSING
FHA--MUTUAL MORTGAGE INSURANCE FUND
2013 Summary Statement and Initiatives
(Dollars in Thousands)

FHA--MUTUAL MORTGAGE & COOPERATIVE MGMT. HOUSING INSURANCE FUND	Enacted/ Request	Carryover	Supplemental/ Rescission	Total Resources	Obligations	Outlays
2011 Appropriation	$207,000[a]	...	-$414	$206,586	$112,962[d]	$91,572[d]
2012 Appropriation/Request	207,000[b]	...	...	207,000	135,500[d]	120,000[d]
2013 Request	215,000[c]	...	...	215,000	142,782[d]	136,000[d]
Program Improvements/Offsets	+8,000	...	...	+8,000	+7,282	+16,000

a/ Includes non-expenditure transfers of $70.7 million to the HUD Working Capital Fund and $1.4 million to HUD's Transformation Initiative account. These amounts are excluded from obligations and outlays.
b/ Includes a non-expenditure transfer of $71.5 million to the HUD Working Capital Fund. This amount is excluded from obligations and outlays.
c/ Includes non-expenditure transfer of $71.5 million to the HUD Working Capital Fund. Also includes an estimated Transformation Initiative (TI) transfer of $717,500 in fiscal year 2013; the TI transfer may be up to 0.5 percent of Budget Authority. These amounts are excluded from obligations and outlays.
d/ Excludes upward re-estimate.

1. What is this request?

The Mutual Mortgage Insurance (MMI) Fund is the largest fund covering activities of the Federal Housing Administration (FHA). Since 1934, mortgage insurance provided by FHA has made financing available in neighborhoods and geographic areas facing economic uncertainty, and to individuals and families not adequately served by the conventional mortgage market. Through MMI, the Department offers several types of single family forward mortgage insurance products and Home Equity Conversion Mortgages (HECMs) for seniors. Activity for the Cooperative Management Housing Insurance (CMHI) Fund – which insures mortgages for multifamily cooperatives – is reported together with MMI.

The fiscal year 2013 Budget request will enable FHA to continue in its mission of providing access to mortgages for low- and moderate-income families, and to play an important countercyclical role in the stabilization and recovery of the nation's housing market. By facilitating the availability of vital liquidity through a variety of HUD-approved lenders, including community and national credit unions and banks, FHA has helped over 2 million families buy a home since President Obama took office – 75 percent of whom were first-time buyers. FHA has also helped nearly 1.5 million existing homeowners refinance into stable, affordable products, with an average monthly savings from their previous mortgage payment exceeding $100. FHA's share of the mortgage market has gone from a low of 3.1 percent of loan originations in 2005, up to a peak of 24 percent in the second quarter of 2010, and more recently down to 17 percent in 2011.

The fiscal year 2013 request for MMI includes four components:

- ***Appropriations for Administrative Contracts.*** The Department requests an appropriation of $215 million for administrative contract expenses for fiscal year 2013; of this amount, up to $71.5 million will be transferred to the Working Capital Fund for FHA systems costs. The amount not transferred supports administrative functions for all of FHA programs, including multifamily and healthcare programs operating under the General and Special Risk Insurance Fund (GI/SRI).
- In fiscal year 2013, the Department renews its request for the Transformation Initiative, which provides the Secretary the flexibility to undertake an integrated and balanced effort to improve program performance and test innovative ideas. Up to 0.5 percent of the funds appropriated for this account may be transferred to the Transformation Initiative Fund account for the following purposes: research, evaluations, and program metrics; program demonstrations; technical assistance and capacity building, and information technology. Departmentwide, no more than $120 million is estimated to be transferred to the Transformation Initiative Fund account in fiscal year 2013, although transfers could potentially total up to $214.8 million. More details on the overall Transformation Initiative and these projects are provided in the justification for the Transformation Initiative Fund account.
- For fiscal year 2013, the increase in funding requested for FHA's administrative contract expenses is necessary to support the following FHA activities:
    - <u>Enhanced Risk Analysis and Management</u>. As part of the Department's credit risk improvements, an Office of Risk Management was established during fiscal year 2010. With this new office and additional staffing, FHA is expanding its capacity to assess financial and operational risk, perform more sophisticated data analysis, and respond to market developments. A portion of the additional administrative contract funds requested in fiscal 2013 will be used to provide additional contract support for this newly created organization. The funds will be used on both the Single Family and Multifamily FHA portfolios.
    - <u>Continue improvements to modeling techniques</u>. The FHA Commissioner and the financial statement auditors have asked FHA to do more in-depth data analyses by product type as well as borrower type to continually improve modeling capabilities for both the single family forward and HECM programs. Beginning with the fiscal year 2013 budget cycle, FHA is incorporating stochastic analysis into its multifamily cash flow projection models and will do for single family models in 2014. This change will enable FHA to offer probabilities and other details for a range of possible outcomes, helping policy makers and program administrators to make more informed decisions and reduce risk in the portfolio.

- ***Commitment authority for up to $400 billion in new loan guarantees.*** The fiscal year 2013 Budget requests $400 billion in loan guarantee limitation which is to remain available until September 30, 2014. This limitation includes sufficient authority for insurance of single family mortgages, mortgages under the HECM program, and the FHA Short Refinance program. Loan volume projected for all MMI programs for fiscal year 2013 is $219.6 billion. Of that total, $149 billion is estimated for standard forward mortgages, $18.7 billion for HECM, and $51.9 billion for FHA Short Refinances. The amount requested above the 2013 projection minimizes the potential for reaching the limitation and having to suspend program activity prior to the end of the year.
- ***Negative Subsidy Receipts.*** The $220 billion in loan volume projected for the entire MMI portfolio is expected to generate $8.2 billion in negative subsidy receipts, which are transferred to the MMI Capital Reserve where they are available to cover any projected cost increases for the MMI portfolio.
- ***Commitment authority for up to $50 million in direct loans to facilitate single family property disposition.*** The loan authority requested is for short-term purchase money mortgages for non-profit and governmental agencies to make HUD-acquired single family properties available for resale to purchasers with household incomes at or below 115 percent of an area's median. This program has been infrequently utilized in recent years, but remains a valuable tool for HUD in managing its property portfolio. The loan program is designed to operate at break-even for the government, so no credit subsidy is involved.

Approval of this request will allow FHA to continue its work in stabilizing the nation's housing market and supporting homeownership, especially for low- and moderate-income borrowers and first-time homebuyers. FHA programs are central to HUD's achievement of its strategic goal to "strengthen the nation's housing market to bolster the economy and protect consumers." More specifically, FHA is making it a priority focus to assist homeowners through early delinquency intervention, loss mitigation programs, and specific joint efforts with the Department of Treasury, including: the Home Affordable Modification Program and the FHA Short Refinance program for underwater borrowers with conventional loans. As of fiscal year-end 2011, 406,234 cases of loss mitigation activity had been reported, which exceeds the goal of assisting 300,000 homeowners by the end of FY 2011. At least 85 percent of those loans participating in loss mitigation are expected to stay current for 6 months or longer.

2. What is this program?

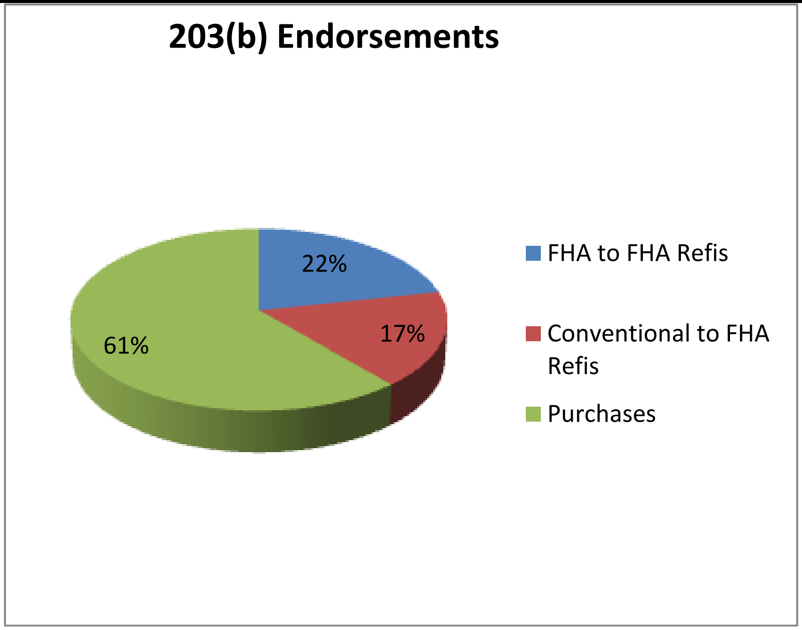
FHA is the largest insurer of mortgages in the world, insuring over 40 million home mortgages since 1934. In exchange for adherence to strict underwriting and application requirements established by HUD and the payment of insurance premiums, HUD-certified lenders are able to file claims with FHA when a borrower defaults. The FHA includes a strong, mandatory loss mitigation program. Mortgage insurance premiums and specific terms for claim payments vary by program. FHA insurance has played a key role in mitigating the effect of economic downturns on the real estate sector, as FHA does not withdraw from local markets during periods of recession. Through program reforms FHA has become a key support for the national mortgage market and is mitigating the foreclosure crisis and the overall economic downturn.

At the end of fiscal year 2011, the MMI insurance portfolio included 7.1 million loans with an unpaid principal balance of just over $1 trillion. FHA mortgage insurance enhances a borrower's credit and provides banks with better access to capital markets, most notably through Ginnie Mae securities. FHA has long been a valuable resource for enabling the purchase of a first home, especially among minority and low-income families. FHA loans are highly attractive to borrowers who are credit-worthy but have difficulty assembling a large down payment or securing conventional financing.

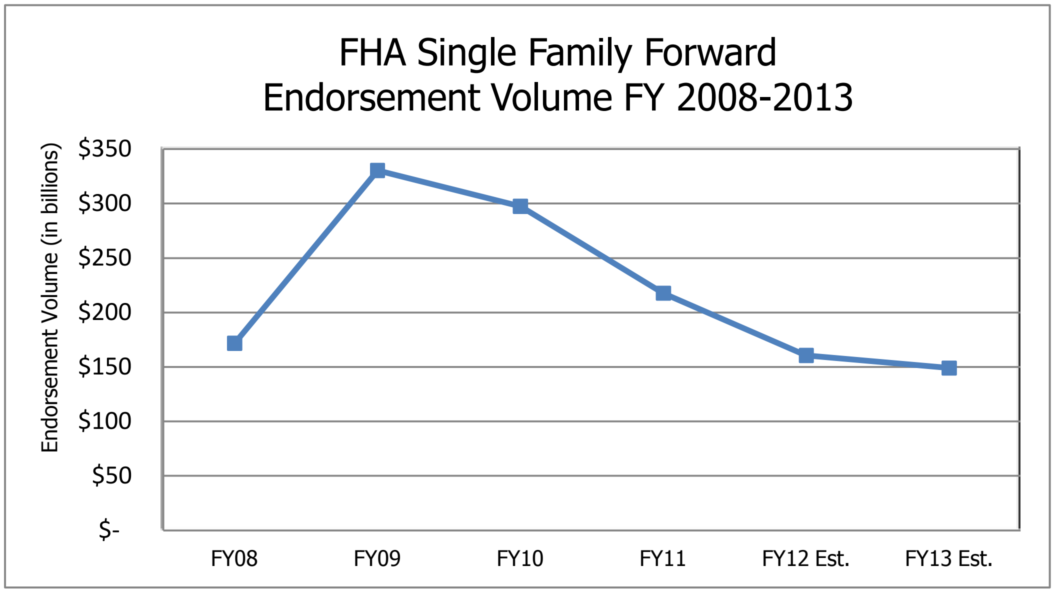
For budgetary purposes, the programs of the MMI Fund are broken into three risk categories, each of which is discussed below: Forward Mortgages, FHA Short Refinances, and HECM.

Fiscal Year 2011 MMI Endorsement Volume by Loan Product

	Loans	*Amount*
203(b) (excluding condos)	1,120,824	$203,125,125,942
Condominiums	54,237	$10,713,171,774
203(k) Rehabilitations	21,296	$3,657,999,372
Other	278	$223,493,703
Forward Total	*1,196,635*	*$217,719,790,791*
HECM	73,131	$18,224,410,152
FHA Short Refi	334	$73,263,044
MMI TOTAL	**1,270,100**	**$236,017,463,987**

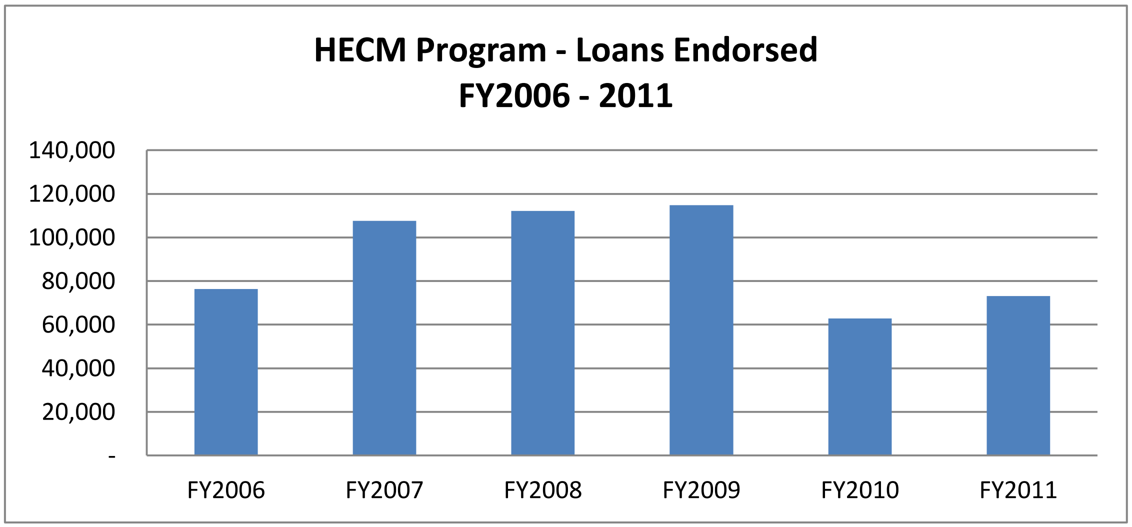


Forward Mortgages. The largest FHA insurance program is the single family program authorized under Section 203(b) of the National Housing Act. In fiscal year 2011, endorsements under 203(b) were $203 billion, out of the MMI Fund's total of $236 billion. Beginning in fiscal year 2009, FHA consolidated a majority of its single family mortgage programs under this risk category including those for condominiums, purchase of homes on Indian and Hawaiian lands, and rehabilitation loans (Section 203(k)). Single family programs provide mortgage insurance for the purchase and refinance on 1-4 unit homes. Maximum mortgage amounts insured by FHA are calculated annually by HUD and are tied to the median house price in each county. In fiscal year 2011, the limits started at $271,050 and went as high as the temporarily expanded mortgage limit ceiling of $729,750 in "high cost" areas. Maximum mortgages in high cost areas were legislatively increased in 2008 (from no more than 87 percent of the conforming loan limit to 175 percent) in order to expand the number of families who would be able to access affordable mortgage financing during the economic downturn. FHA activity peaked in fiscal year 2009, when monthly volume surpassed $25.8 billion, compared to just $4.7 billion in 2007. From this peak, FHA's annual endorsement volume dropped markedly through 2010 and 2011, and is projected to continue at a decreasing pace in fiscal year 2012 before stabilizing in the out years.



FHA Short Refinance. In fiscal year 2010, HUD and the Department of Treasury announced enhancements to FHA's refinance program that give a greater number of responsible borrowers the opportunity to remain in their homes. The enhancements were designed to maintain homeownership by borrowers who owe more on their mortgage than the value of their home with opportunities to refinance into an affordable FHA loan. This program allows a borrower who is current on his mortgage to qualify for an FHA refinance loan, provided that the lender or investor writes off the unpaid principal balance of the original first lien mortgage by at least 10 percent. Under current policy, applications for the negative equity refinance program will be accepted only through December 31, 2012. FHA and Treasury are extending the program through the end of 2014.

HECM. FHA's HECM program allows senior homeowners age 62 and older access to FHA-insured reverse mortgages to convert the equity in their homes into monthly streams of income and/or a line of credit to be repaid when they no longer occupy the homes. In fiscal year 2010, HUD introduced a new product – HECM Saver – that offers lower upfront loan closing costs for mortgagors who want to borrow a smaller amount than that available with the Standard HECM product. Homeowners who select either option are required to receive consumer education and counseling by a HUD-approved counselor so they can be sure this program meets their needs. The amount a borrower is eligible for is based on the borrower's age, the current interest rates, and the lesser of the appraised property value or the FHA mortgage limit for HECM. Unlike forward mortgage borrowers, the HECM borrower has no income or credit qualifications to meet and makes no payments as long as the property securing the HECM loan is his main residence. For fiscal year 2012, it is estimated that over 72,585 loans will be endorsed under HECM programs, with approximately 10 percent of those being for the HECM Saver product. A 2 percent increase in loan volume is projected for fiscal year 2013. From the beginning of the HECM program in fiscal year 1990 through fiscal year 2011, over 723,129 loans have been endorsed under the program. Over 65 percent of these loans were endorsed during fiscal years 2007 through 2011.



Staffing

FTE	2011 Actual	2012 Estimate	2013 Estimate
Headquarters	294	275	275
Field	781	805	805
Total	1,075	1,080	1,080

Descriptions of work to be performed by FTE (Headquarters and Field) allocated to MMI Programs

The primary workload for FHA programs in the MMI fund is carried by HUD's Office of Housing, mainly the Office of Single Family Housing. Critical functions are also supported by financial, procurement, IT, and other administrative organizations.

Within the Office of Single Family Housing, Headquarters staff: develop and update policy related to all aspects of implementing the program; provide oversight of FHA approved-lenders; provide oversight and monitoring of field staff implementation of policy and procedures related to FHA programs; ensure that adequate funding is provided to the field for necessary contract services required to implement the program; provide technical support and assistance to field staff; and review regulatory waiver requests.

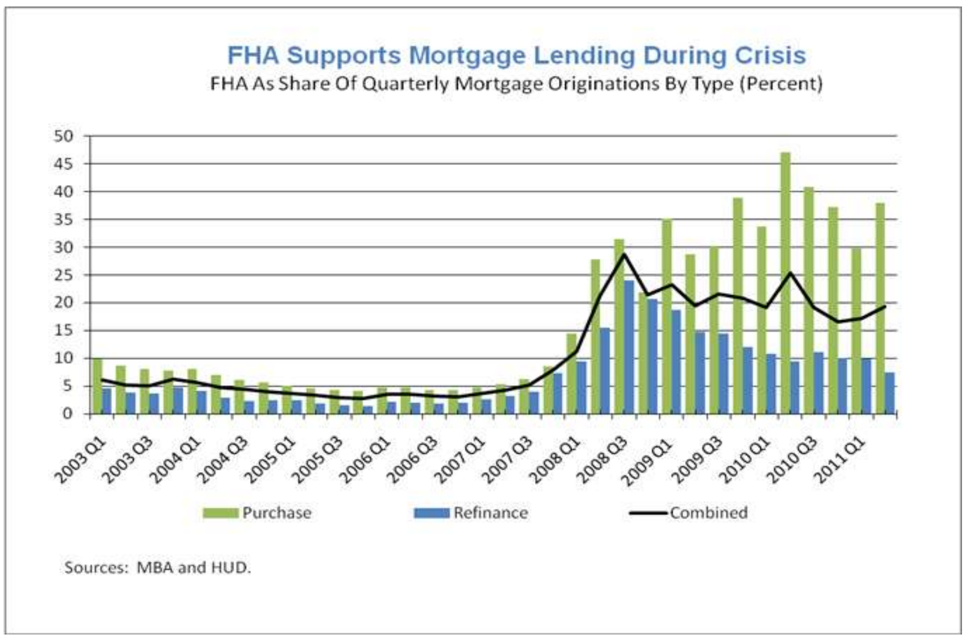
Field Staff perform the following functions in administering FHA Mortgage Insurance Programs: provide oversight of contractors that process case-level endorsement for mortgage insurance; review underwriting and mortgage credit analyses of pre-endorsement files for individual test-phase lenders; provide oversight of contract field appraisers that conduct site reviews; monitor appraisers for compliance with FHA requirements; participate in marketing and outreach of FHA programs; train FHA lenders; provide technical assistance to lenders for facilitation of loan endorsements; provide oversight of condominium approval process; monitor originating lenders and servicing lenders for FHA requirement compliance; provide oversight of field service managing and asset managing contractors that perform property preservation and sales for the HUD-held real estate owned inventory; and provide on-going assistance and support to Field Policy Management staff throughout the nation.

3. Why is this program necessary and what will we get for the funds?

FHA provides mortgage insurance on single family mortgage loans made by FHA-approved lenders throughout the United States and its territories, encouraging the return of private capital to the housing market. FHA's single family mortgage insurance program supports our nation's housing recovery by meeting the needs of borrowers facing difficult economic conditions, such as declining property values and contracting credit markets due to the dearth of lending by private lenders and insurers. FHA remains active and viable in all markets during times of economic disruption, playing an important counter-cyclical role until private capital returns to its natural levels.

The HECM program fills a special niche in the national mortgage market and offers critical opportunities for the nation's seniors to preserve their quality of life by tapping into their home equity. According to a 2009 study by MetLife's Mature Market Institute, today's issues of increased longevity, rising health care and other costs, fewer defined benefit pension programs, and diminished investment values have put extraordinary pressure on seniors in finding new sources of income and creative ways to stretch out accumulated savings during retirement. To supplement their budgets, older homeowners are increasingly considering the option of tapping their housing wealth. However, options once available to tap home equity, such as selling the home and moving to less costly housing, are also more limited in today's market as homes can languish on the market for extended periods of time, and when they do sell, the price may be 25 percent or more below the homes' pre-crisis value. Reverse mortgages are another viable option. Due to the tightening of conventional credit since the housing crisis, HECM has become nearly 100 percent of the reverse mortgage market. Eventually, conventional reverse mortgages may become available again, but for the immediate future, HECM *is the market* for this much needed loan product. The Budget also proposes to permanently lift the statutory cap on the number of HECM guarantees. Prior appropriations have lifted the cap only for the year in question. This change will help the program operate without disruption.

The fiscal year 2013 Budget request will provide the commitment authority and administrative funding for FHA to continue its important work.



Commitment Authority and Subsidy Projections

Below is a table indicating loan commitment volumes, credit subsidy rates, and subsidy obligations for each MMI risk category in fiscal year 2013. Credit subsidy rates represent the projected net cost (positive credit subsidy) or savings (negative credit subsidy) to the government of operating a loan guarantee program, and take into account projected claims, pre-payments, premium revenue, and recoveries on defaults for a cohort of loans over their lifetime. For more information on credit subsidy calculation please see the Notes section.

MMI COMMITMENT VOLUME BY RISK CATEGORY (in thousands)	FY 2012 Commitments Estimated	FY 2013 Commitments Estimated	FY 2013 Subsidy Rate	FY 2013 Negative Subsidy
MMI Purchase and Refinance	$160,500,000	$149,000,000	-5.38%	($8,016,200)
MMI HECM	18,271,000	18,700,000	-.92%	(172,040)
FHA Short Refi	51,862,000	51,862,000	0.00%	0
Totals	$230,633,000	$219,562,000		($8,188,240)

Administrative Contract Appropriations

The request for fiscal year 2013 will provide funding for contracts necessary in the administration of all FHA programs, including those operating under MMI and GI/SRI. (Beginning in fiscal year 2010, appropriations for FHA administrative contracts were consolidated under MMI to allow for more efficient management of funds.) The request includes $71.5 million that will be transferred to the HUD Working Capital Fund for the maintenance and development of mission critical systems. Funds remaining in the MMI program account will fund activities including, but not limited to: construction inspections on multifamily projects, the required annual FHA actuarial review and financial audit, management and oversight of asset disposition, risk analysis and accounting support, and assistance with claims and premium refund processing.

4. How do we know that this program works?

FHA continuously monitors and evaluates the results of its programs, and updates its policies as necessary to take into consideration product performance as well as market forces. To address current and difficult conditions in the housing market, aid homeowners, and mitigate risk to FHA's insurance fund, FHA develops new programs, modifies existing programs and improves controls. For example, FHA has recently modified its premium structure and tightened underwriting requirements for forward mortgages, steps necessary to raise negative subsidy receipts and restore FHA's capital reserve.

The continued weakness in the housing market and reduction in private lending have increased the demand for loss mitigation actions, and FHA has expanded its tools to meet that need. The Department has provided increased targeted loss mitigation training for lenders, and has increased monitoring of mortgagees and services to assure they are making sincere efforts to curb foreclosures. As part of its annual performance plan, the Department established an agency priority goal to assist homeowners who are at risk of losing their homes due to foreclosure. For FHA, that translates to specific targets and tracking of its early delinquency intervention efforts and loss mitigation program. For fiscal years 2010 and 2011, HUD assisted 496,197 homeowners with early intervention actions such as formal forbearance agreements, surpassing the 2-year target of 400,000 by 24 percent. During the same period, FHA also assisted 406,234 homeowners through its loss mitigation program, exceeding the 2-year goal by over 35 percent. HUD's loss mitigation efforts can be considered successful only if the program has effective solutions for homeowners in both the short and long term. In 2011, HUD set a target of having no more than 20 percent of loans that received loss mitigation assistance experience a re-default within 6 months. That goal was exceeded with an actual re-default rate of only 13.6 percent.

Strengthening FHA Business Practices

The fiscal year 2009 Omnibus Appropriations Act provided FHA with $4 million, in direct appropriations to the HUD Working Capital Fund, to develop a strategic plan for Information Technology. Once completed, this plan became the foundation for FHA Transformation Initiatives with the goal of developing and implementing a modern financial services information technology environment to better manage and mitigate counterparty risk across all of FHA's Insurance Programs. Specifically, FHA Transformation will enable risk detection and fraud prevention by capturing critical data points at the front-end of the loan lifecycle, and leveraging the right set of risk and fraud tools, rules based technology, and transactional controls to minimize exposure to FHA's Insurance Funds. This will protect consumers and support the housing market by ensuring compliance with FHA's underwriting standards.

FHA Transformation will also provide decision-makers with higher quality data and lower data latency to facilitate enhanced business analytics and informed decision-making. This will enable FHA's leadership to analyze portfolio trends and patterns across the lending community, and will help with the identification of fraudulent lenders and reduce risk in the FHA portfolio. Finally, FHA Transformation will allow the business to start the careful process of migrating relevant portions of our legacy applications, most of which were built with a 1970's era programming language, to the modern financial services environment. The use of commercial off-the-shelf products will minimize operational risk as FHA migrates relevant portions of our legacy applications to our new environment. FHA's experience with the Hope for Homeowners program provides a clear illustration of the expected benefits from the FHA Transformation Initiatives. Implementing the Hope for Homeowners program required roughly $20 million of system changes, the modification of over 10 contracts, and 4 months of staff work across multiple HUD offices. In comparison, modern financial services technology will allow rules-based changes to be made more quickly and at much lower cost.

In sum, the FHA Transformation Initiatives will provide FHA with the ability to:

- ✓ Detect and prevent fraud, waste, and abuse by lenders and borrowers;
- ✓ Modernize 40-year-old FHA systems and processes;

- ✓ Manage credit risk prudently at both the portfolio and loan level; and
- ✓ Respond rapidly to changing market conditions.

Strengthening FHA's Capital Reserves

HUD's fiscal year 2011 Report to Congress on the status of the MMI Fund conveyed that the Fund's capital ratio as of the end of fiscal year 2011 was 0.24 percent – below the 2 percent level mandated by statute. Building upon a number of policy changes initiated in 2009 and 2010 to better manage risk to the MMI Fund, FHA is currently exploring and will soon announce a series of steps to further strengthen the MMI Fund. These include:

- Premium increases – The Temporary Payroll Tax Cut Continuation Act of 2011 (H.R. 3630) mandated an increase in FHA's annual insurance premiums. In accordance with this legislation, FHA will soon implement a 10 basis point increase to annual premiums for single family forward mortgages. "Jumbo" loans with an original principal balance above $625,500 will pay an additional 25 basis points, resulting in a total increase of 35 basis points for these loans. FHA continues to evaluate other potential increases to its premiums to protect the fund while balancing the need to do so in a manner that does not impact market recovery.

- Lender enforcement – A final rule is scheduled to be published in the second quarter of fiscal year 2012 which outlines new indemnification requirements for lenders participating in the Lender Insurance (LI) Program, whereby they will be required to indemnify HUD for losses associated with loans that were improperly originated, or for which fraud or misrepresentation were involved. This rule will permit FHA to improve its oversight of LI lenders and better protect its insurance Funds from the adverse effects of non-compliant loans. In addition, a proposed rule regarding potential reductions in seller concessions will also be published in the very near future, which if ultimately enacted, will better reduce risks to FHA associated with inflated appraisals. FHA also continues to evaluate other opportunities to further strengthen its counterparty risk management as well.

- Loss mitigation – FHA is looking at additional mechanisms to assist distressed borrowers to keep them in their homes, or, if necessary, transition to other housing options. This includes exploring additional mechanisms to facilitate refinance activity whereby distressed borrowers can benefit from today's low interest rates, and the execution of a robust and impactful housing counseling strategy that equips homeowners to make smart housing choices and obtain assistance when necessary.

- Borrower qualifications – FHA is constantly evaluating its underwriting criteria to ensure that responsible borrowers can access sustainable homeownership opportunities. Toward that end, FHA is making changes to its TOTAL Mortgage Scorecard to better ensure that borrowers are receiving adequate consideration by lenders, and considering the sufficiency of various other components of its underwriting approach to ensure that qualified borrowers are able to access and sustain mortgages insured by FHA.

- REO and Pre-REO recovery - Through the Mortgage Acquisition and Disposition Initiative (601 Notes Sales) and various pilot opportunities resulting from the Request For Information process initiated in conjunction with FHFA and Treasury, FHA hopes to implement successful strategies to increase REO recovery rates and limit losses to the MMI Fund.

In total, FHA expects that the steps outlined above will protect and strengthen FHA's MMI Fund and assist in returning the Fund's capital ratio to a level of 2 percent. Under current economic and loan performance assumptions, the Budget projects the Capital Reserve will grow significantly starting in 2013 and the capital reserve ratio will reach the target level of 2 percent in 2015.

5. Notes to Justification

Credit Subsidy Calculations and the Annual Re-estimate

Credit subsidy rates represent the projected net cost or savings to the government of operating a loan guarantee program, and take into account projected claims, pre-payments, premium revenue, and recoveries on defaults for a cohort of loans over their lifetime. In accordance with the Credit Reform Act of 1990, administrative costs (excluding property disposition) are not included in credit subsidy calculations. FHA credit subsidy rates reflect historic performance data for similar loans made over the past 40 years, with adjustments made for significant policy shifts as well as changing economic and market conditions. The Department devotes significant efforts to updating and continuously refining the credit subsidy estimates. Each year the extensive statistical base, from which projections of future loan performance are calculated, is updated with an additional year of actual data. The Department and OMB continue to examine the data, assumptions, and calculations that are used to estimate loan program cash flows and subsidy rates in order to eliminate errors and improve the accuracy and reliability of projections.

Each year, FHA completes a required re-estimate of liabilities and subsidy costs associated with the existing insurance portfolio. Revised liability estimates take into account another year of actual loan portfolio performance and the latest economic assumptions. Vacancy rates, Treasury interest rates, and house price appreciation are among the key variables that shape MMI projected cash flows. Multivariate statistical models generate the claim and prepayment rates that drive the fund's financial worth. To determine the amount of the re-estimate, the revised liabilities (net of projected loan default recoveries) are compared to the current assets on hand. When assets exceed projected liabilities, a downward re-estimate occurs with the difference being transferred to the MMI Capital Reserve account. When projected liabilities exceed assets, an upward re-estimate occurs and the fund must transfer cash from its Capital Reserve account to bring the assets and liabilities in balance. For example, if the portfolio of loans made in a given year has a net liability of $250 million and cash on hand of $300 million, then the cohort would require a downward re-estimate in which $50 million would be moved from the fund's financing account (which handles all loan guarantee cash flows) to the MMI Capital Reserve account. Re-estimates are calculated each year for each cohort of loans (from 1992 onward). Three MMI cohorts have net lifetime downward re-estimates, meaning costs to the government for that group of loans are now projected to be less than the original subsidy calculation. Seventeen cohorts have a lifetime upward re-estimate, meaning the original subsidy calculation is now believed to have underestimated the costs.

HOUSING
FHA – MUTUAL MORTGAGE INSURANCE FUND
Summary of Resources by Program
(Dollars in Thousands)

Budget Activity	2011 Budget Authority	2010 Carryover Into 2011	2011 Total Resources	2011 Obligations	2012 Budget Authority/ Request	2011 Carryover Into 2012	2012 Total Resources	2013 Request
Administrative Contract Expense	$134,575	...	$134,575	$112,962	$135,500	...	$135,500	$143,500
Working Capital Fund transfer	70,652	...	70,652	...	71,500	...	71,500	71,500
Transformation Initiatives transfer .	1,359	...	1,359	...	...	...	...	...
Total	206,586	...	206,586	112,962	207,000	...	207,000	215,000

NOTE: The 2011 Budget Authority for Administrative Contract Expenses includes $414,000 of the governmentwide rescission.

HOUSING
FHA--MUTUAL MORTGAGE INSURANCE FUND
Appropriations Language

The fiscal year 2013 President's Budget include proposed changes in the appropriation language listed and explained below. New language is italicized and underlined, and language proposed for deletion is bracketed.

New commitments to guarantee single family loans insured under the Mutual Mortgage Insurance Fund shall not exceed $400,000,000,000, to remain available until September 30, [2013] *2014: Provided, That during fiscal year* [2012] *2013, obligations to make direct loans to carry out the purposes of section 204(g) of the National Housing Act, as amended, shall not exceed $50,000,000: Provided further, That the foregoing amount in the previous proviso shall be for loans to nonprofit and governmental entities in connection with sales of single family real properties owned by the Secretary and formerly insured under the Mutual Mortgage Insurance Fund. For administrative contract expenses of the Federal Housing Administration,* [$207,000,000] *$215,000,000, to remain available until September 30,* [2013] *2014, of which up to $71,500,000 may be transferred to and merged with the Working Capital Fund: Provided further, That to the extent guaranteed loan commitments exceed $200,000,000,000 on or before April 1, 2012, an additional $1,400 for administrative contract expenses shall be available for each $1,000,000 in additional guaranteed loan commitments (including a pro rata amount for any amount below $1,000,000), but in no case shall funds made available by this proviso exceed $30,000,000. (Department of Housing and Urban Development Appropriations Act, 2012.)*

<u>Changes from 2012 Appropriations</u>

The 2013 request for administrative contract expenses is $215 million; $8 million more than that requested in 2012.

HOUSING
GENERAL AND SPECIAL RISK INSURANCE FUND
2013 Summary Statement and Initiatives
(Dollars in Thousands)

FHA--GENERAL AND SPECIAL RISK INSURANCE FUND	Enacted/ Request	Carryover	Supplemental/ Rescission	Total Resources	Obligations	Outlays
2011 Appropriation	$8,600	$9,724	-$17	$18,307	$1,765	$7,801
2012 Appropriation/Request	...	16,542	...	16,542	5,739	13,864
2013 Request	...	10,803	...	10,803	...	8,500
Program Improvements/Offsets	...	-5,739	...	-5,739	-5,739	-5,364

1. What is this request?

Loan guarantee programs operating under the Federal Housing Administration's (FHA) General Insurance and Special Risk Insurance (GI/SRI) Fund encourage critical mortgage financing opportunities that strengthen communities across the country. GI/SRI houses a wide range of mortgage insurance products to address specialized financing needs, including insurance for loans to develop, rehabilitate, and refinance multifamily rental housing, nursing home facilities, and hospitals. GI/SRI programs also include loan guarantees for Title I manufactured housing and for property improvement loans.

FHA mortgage commitment issuances for multifamily housing and healthcare rose from $4.3 billion in fiscal year 2008 to $7.7 billion in 2009 to $17.5 billion in 2011. As of September 2011, GI/SRI's multifamily/healthcare portfolio had an unpaid principal balance (UPB) of $76 billion on 12,600 loans. FHA's multifamily programs have helped private lenders fill the gap left with the shrinkage of conventional financing resources. High levels of mortgage insurance activity are anticipated to continue in fiscal years 2012 and 2013, peaking in fiscal year 2012.

The fiscal year 2013 request for GI/SRI includes four components:

- **Commitment authority for up to $25 billion in new loan guarantees.** New insurance commitments are projected to exceed $19.3 billion in fiscal year 2012, then decline to $16.4 billion in 2013. The amount requested above the 2013 projection minimizes the potential for reaching the limitation and having to suspend program activity prior to the end of the year. Of the total commitments projected for fiscal year 2013, it is estimated that $10.1 billion will be issued for FHA's multifamily housing programs. Another $6.2 billion is estimated for hospitals, nursing homes, and assisted living facility mortgages. Title I Property Improvements and Manufactured Housing commitments – which represent the only new single family activity for fiscal year 2013 – are projected at $121 million.

- **Offsetting receipt estimates from negative credit subsidy.** No new appropriations for positive credit subsidy are requested for fiscal year 2013, while offsetting negative subsidy receipts are projected to be $661 million. FHA is proposing to terminate or suspend new activity for three GI/SRI programs that have not been self-supporting and will realign certain supplemental loans to the risk categories of the primary FHA mortgage for which they enhance or maintain performance.
- In fiscal year 2013 new insurance will not be issued for Section 221(d)(3) loans to non-profit housing developers, Section 223(d) operating loss loans to multifamily housing projects with a HUD-insured primary mortgage, and Section 238(c) single family loans in military impact areas. Beginning in 2013, section 241(a) supplemental loans to FHA-financed multifamily housing projects and Section 223(d) Operating Loss loans to heath care facilities with a primary Section 232 mortgage will be reported in the budget risk category of the primary FHA mortgage.
- Credit subsidy rates for fiscal year 2013 assume implementation of targeted mortgage insurance premium (MIP) increases for market-rate multifamily housing and healthcare loans. Proposed increases for market rate activity range from 5 basis points for 223(a)(7) refinancing to 20 basis points for 221(d)(4) new construction or rehabilitation activity. MIPs for market rate deals in all other multifamily and healthcare programs will increase by 15 basis points. MIPs for affordable housing projects (such as those with HUD rental subsidies and low-income housing tax credits, as well as those insured under FHA risk-sharing programs) will not be increased. These changes are discussed in greater detail in section 4 of this justification.
- **Commitment authority for up to $20 million in direct loans to facilitate single family property disposition**. The loan authority requested is for short-term purchase money mortgages for non-profit and governmental agencies to make HUD-acquired single family properties available for resale to purchasers with household incomes at or below 115 percent of an area's median. This program has been infrequently utilized in recent years, but remains a valuable tool for HUD in managing its property portfolio. The loan program is designed to operate at break-even for the government, so no credit subsidy is involved.
- **Flexible Authority for risk Sharing and GNMA Securitization of Insurance for Small Property Loan**. The General Provisions in the 2013 request include legislative language that will expand on the Department's demonstration authority to make Section 542(b) Risk Share loans available to small multifamily properties (5 to 49 units). These small properties are underserved by the conventional market, and are traditionally underserved by FHA as well. This request focuses on the particular needs of very small (20 units and under), unsubsidized properties. These small properties comprise a significant share of rental housing in certain urban areas. Small multifamily properties are an important focus for the Department to meet its affordable housing and community development goals. These properties are more likely to be owned by small entities or individuals, tend to be concentrated in lower income neighborhoods, and often offer rents affordable to households below median income. The impact of the amendments is discussed in greater detail under Section 2 of this justification.

- Funding for administrative contracts associated with GI/SRI programs was realigned to the Mutual Mortgage Insurance (MMI) Fund beginning in fiscal year 2010 to enable more efficient management of FHA resources.

The fiscal 2013 request supports mortgage insurance programs that are essential in achieving the Department's mission of strong, sustainable, inclusive communities and quality affordable homes for all. More specifically:

- At a time when credit availability is low, FHA mortgage insurance encourages private lenders to make loans for important projects that might otherwise not be possible. New workforce housing in high demand markets, innovative "green" technology renovations, nursing homes serving aging senior citizens, and critical access hospitals are among the types of projects that FHA makes possible. In fiscal year 2011, HUD endorsed a total of 1,694 multifamily and healthcare loans in GI/SRI in 50 states and Puerto Rico, covering 245,255 units of housing and healthcare facility beds.
- In addition to new development, FHA supports refinance lending that preserves financially healthy housing and healthcare projects that are endangered due to their current debt obligations. FHA's major refinancing programs for housing and nursing home facilities offer long-term amortization periods and are a critical option for many conventionally financed projects facing large balloon payments. FHA refinancing may also enable properties to undertake needed renovation and rehabilitation. New loan insurance commitments in 2011 included 1,550 refinances of existing properties that include more than 160,000 apartment homes and 55,000 nursing home/assisted living beds.
- FHA mortgage insurance has a strong secondary effect of creating and preserving jobs. HUD estimates that Multifamily housing loans endorsed in fiscal year 2011 are supporting 54,525 private sector jobs in construction, property management, service and administrative fields. In addition, FHA's internal forecast estimates that the 17 loans made to hospitals in fiscal year 2010 are creating an economic benefit of $3.9 billion and nearly 15,500 jobs during the construction period alone. Following construction, the completed hospital projects will generate $1.4 billion in economic activity per year, and support an additional 8,500 jobs in the community.

2. What is this program?

FHA has insured mortgages on over 34 million single family and multifamily properties since its inception in 1934 (under both MMI and GI/SRI Funds). At the end of fiscal year 2011, the GI/SRI insurance portfolio included 497,000 loans with an unpaid principal balance of $136 billion. These active loans cover more than two million apartments, healthcare facility beds, and single family homes across the nation. FHA mortgage insurance enhances a borrower's credit and provides banks with better access to capital markets, most notably through Ginnie Mae securities. In exchange for adherence to strict underwriting and application requirements established by HUD and the payment of annual insurance premiums, HUD-certified lenders are able to file claims with FHA when a borrower defaults. Mortgage insurance premiums and specific terms for claim payments vary by program.

Mortgage and Loan Insurance Programs – GI/SRI Account

FHA mortgage works in part by helping private lender access liquidity otherwise not available to borrowers developing or maintaining rental housing for low- and moderate-income families. The credit enhancement provided by an FHA loan guarantee (typically 100 percent) enables borrowers to obtain long-term, fully amortizing financing (up to 40 years in the case of new construction/substantial rehabilitation) which can result in substantial cost savings that can be passed on to residents. FHA mortgage insurance provides long-term amortization not found with conventional lending sources. The fact that FHA loans are fully amortizing protects properties from interest rate and liquidity risk in that project owners don't have to refinance with unattractive terms. The long-term amortization period and guarantee of payment in the event of claim stabilizes interest rates and allows monthly mortgage payments to be less than payments required under non-insured financing. These savings in turn can also reduce the overall costs of developing and maintaining housing, stabilizing housing markets and benefiting low- and moderate-income residents. In a similar relationship, FHA financing of healthcare facilities contributes to lower healthcare costs for taxpayers and consumers.

Multifamily and healthcare loans – which now constitute 99 percent of new insurance commitments in GI/SRI – are much larger and substantially more complex than their FHA single family counterparts. Prior to receiving a mortgage guarantee for any multifamily or healthcare loan, lenders and borrowers must complete a rigorous application process in which HUD staff review borrower credit worthiness, project cash flow projections, property appraisals, architectural design, environmental impact, requested loan size, quality of the property management, and other information that establishes a loan as an acceptable credit risk to HUD. Large multifamily housing projects and all healthcare facility loans receive secondary review and approval by a national loan committee of senior HUD officials. Once insurance has been approved, progress on any new construction or renovations is closely monitored by HUD inspectors. HUD asset managers monitor project financial statements on an on-going basis and periodic physical inspections are conducted by HUD's Real Estate Assessment Center. (Note that GI/SRI does not include funding for administrative contracts and program staffing, which are covered by appropriations under MMI and Housing Personnel and Benefits, respectively.) Loss mitigation measures – including a partial payment of claim policy approved in 2010 – are undertaken before a default and full claim on the loan occurs. When a borrower does default and a claim is filed, HUD will take possession of the mortgage note or property and seek to recover losses.

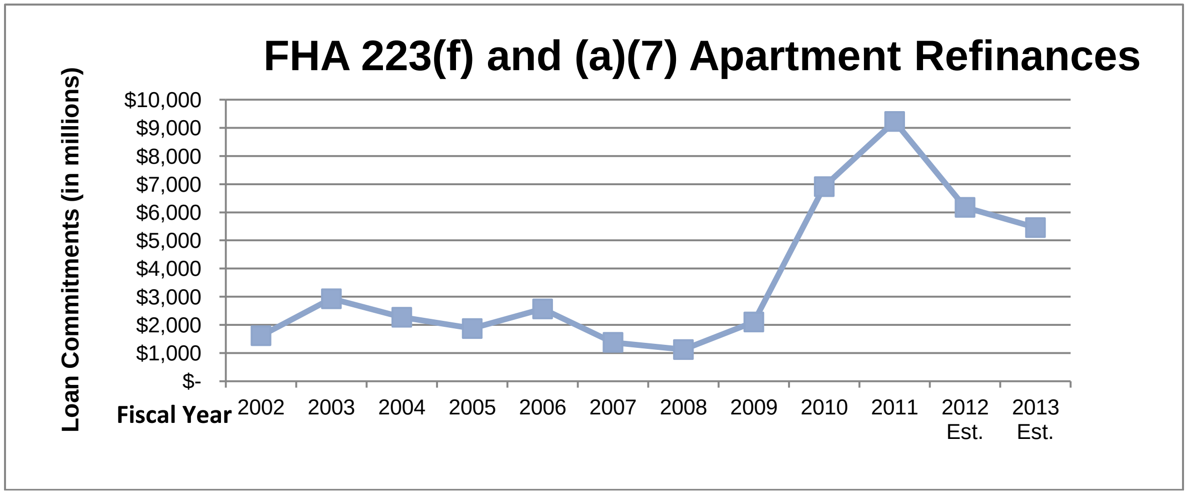
Active programs included under GI/SRI are authorized under Sections 220, 221(d)(3) and (4), 223(a)(7), 223(f), 223(d), 231, 241, 232, 207,and 242 of the National Housing Act and Sections 542(c) and 542(b) of the Housing and Community Development Act. In addition, GI/SRI includes single family property improvement and manufactured housing programs authorized by Title 1 of the National Housing Act. Sections of the act citations are commonly used to identify the programs, both within HUD and the housing industry. In the Federal Budget, programs are identified and discussed according to their risk category. Risk categories are groupings of loans with similar terms and/or credit risks. A credit subsidy rate and loan volume projection is prepared annually for each risk category. For fiscal year 2013, there will be 11 risk categories within GI/SRI – 6 covering multifamily housing programs, 3 for healthcare facilities, and 2 for Title 1 programs. Each risk category is briefly described below.

Multifamily Housing Risk Categories

Section 221(d)(4) Mortgage Insurance for Rental and Cooperative Housing. The Section 221(d)(4) program is FHA's largest new construction/substantial rehabilitation for multifamily housing. In 2011, new Section 221(d)(4) loans averaged a little over $16 million and included an average of 160 units. The program insures loans made primarily to profit-motivated sponsors, with financing allowed for up to 90 percent of the project replacement cost (as limited by debt service coverage and per-unit cost requirements). The program covers long-term mortgages of up to 40 years and, like all FHA new construction loan programs, provides for both construction and permanent financing. In 2010, HUD implemented tighter underwriting requirements for 221(d)(4) – with the largest adjustments coming for market-rate projects – to ensure deals in the rapidly increasing portfolio remain financially sound. Volume has increased rapidly, but is expected to level off in fiscal years 2012 and 2013 as the conventional market rebounds.

Section 221(d)(3) Mortgage Insurance for Rental and Cooperative Housing . This is one of three positive subsidy risk categories for which HUD does not plan to issue new commitments in fiscal year 2013. This program operates similarly to Section 221(d)(4), but provides financing for up to 100 percent of the project replacement cost. Only projects with non-profit sponsors can be considered for insurance under this program. Activity in the risk category has been very limited in recent years, with no new projects receiving insurance commitments in fiscal year 2011. Non-profit sponsored projects that are able to meet requirements for financing under 221(d)(4) are encouraged to apply under that program, which has lower maximum mortgage limits but also lower mortgage insurance premiums and a negative credit subsidy rate.

Section 223(f) Mortgage Insurance for Refinancing or Purchase of Existing Multifamily Rental Housing. Section 223(f) is currently the highest volume program operating under GI/SRI. It allows for long-term mortgages of up to 35 years for refinance or purchase of existing multifamily rental housing. Refinances of current FHA-insured multifamily loans are also offered under Section 223(a)(7), but are grouped together with Section 223(f) for budgetary purposes. Unless waived by a special provision for projects built prior to the 2008 economic crisis that are now unable to obtain permanent financing, properties must have been completed or substantially rehabilitated for at least 3 years prior to the date of the application for mortgage insurance. The maximum mortgage limitation for a market-rate refinance transaction is up to 83.3 percent of the HUD appraised value. Commitments under these programs totaled $9.2 billion in fiscal year 2011, 34 percent more than fiscal year 2010.



Section 241(a) Mortgage Insurance for Supplemental Loans for Multifamily Housing Projects. Section 241(a) provides mortgage insurance for supplemental loans for multifamily housing projects already insured or held by HUD. In fiscal year 2011, FHA made four loan commitments totaling $19.5 million. This program is intended to keep projects competitive, extend their economic life, and finance the replacement of obsolete equipment. Section 241(a) mortgages finance repairs, additions, and other improvements. These loans take second position to the primary mortgage. Beginning in fiscal year 2013, each 241(a) loan will be assigned to the risk category of the associated primary FHA mortgage.

Section 542(b) Risk Sharing with Qualified Participating Entities (QPEs). This is one of two multifamily programs under which FHA insures only a portion of the losses by sharing the risk with Fannie Mae, Freddie Mac, and other qualified Federal, State, and local public financial and housing institutions. If a loan insured under Section 542(b) defaults, the QPE will pay all costs associated with loan disposition and will seek reimbursement from HUD for 50 percent of the losses. A variation of Section 542(b), called "Green Risk Sharing," – introduced in 2011 – permits QPEs to offer loans to both preserve older affordable properties and provide the means to install energy-saving features. Also known as "Green Refinance" or "Risk Sharing Plus," the variation allows for expansion of the QPE's Debt Service coverage and Loan-To-Value lending limits for qualified properties in return for the use of at least 5 percent of the loan proceeds to be applied to energy retrofits identified by a Green Physical Condition Needs Assessment. With terms of 10, 15, or 30 years (all with 30-year amortization), "Green Risk Sharing" loans require an MIP higher than under the standard Section 542(b) program.

Proposed amendments to Section 542(b) authorizing statute will facilitate lending to small multifamily properties, which are an important provider of affordable, but unsubsidized, housing for low- and moderate-income families. According to the 2010 American Community Survey, nearly one-third of all renters live in 5 to 50 unit buildings. The 2001 Residential Finance Survey also demonstrates that these small multifamily properties have lower median rents than do larger properties: $400 per month for 5-49 unit properties, as compared to the $549 monthly rent for properties with 50 or more units. While 62 percent of unsubsidized 5-49 unit properties charge rent below $500 per month, just 38.5 percent of larger unsubsidized properties charge rent below $500 per month. At a time when Federal budgets are shrinking and the need for affordable housing is growing, the amendments will allow us to preserve this vital asset without significant cost to the Federal Government, by drawing in state, local and community resources to these rental properties.

The amendments would allow HUD to enter into Risk Share agreements with qualified lenders, such as well-capitalized Housing Finance Agencies or Community Development Financial Institutions, with demonstrated experience making loans for affordable housing. HUD could then work with these approved lenders to endorse loans to refinance and recapitalize small multifamily rental properties. If the approved lenders meet Ginnie Mae servicer requirements, they would have authority to then securitize these loans with Ginnie Mae. The proposed language provides more flexibility to use the Risk Share program to target small multifamily properties. It also enables lenders to securitize these loans on the secondary market, increasing the availability of capital for more multifamily lending.

Section 542(c) Risk Sharing with Housing Finance Agencies (HFAs). Section 542(c) provides mortgage insurance of multifamily housing projects whose loans are underwritten, processed, serviced, and disposed of by state and local HFAs. FHA insurance enhances HFA bonds to investment grade and provides capital for affordable housing construction. HFAs may elect to share from 10 to 90 percent of the loss on a loan with HUD. Section 542(c) insured projects often include low income housing tax-credits, in which case they are reported under GI/SRI's risk category for Tax Credit Projects.

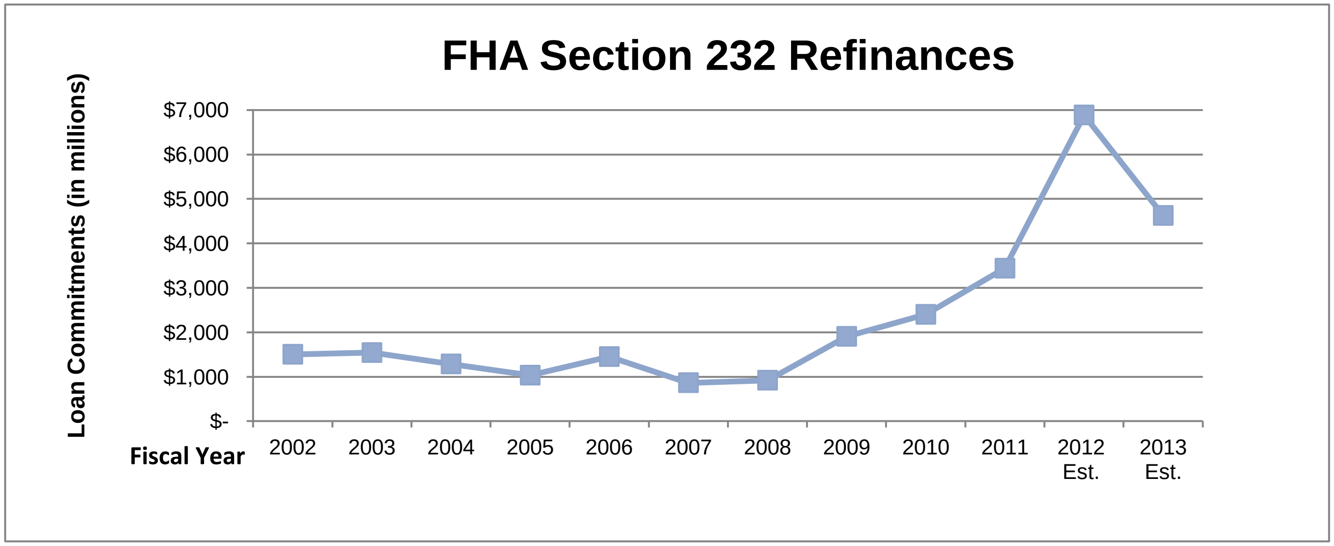
Other Rental Programs. This risk category includes several relatively low-volume programs that have been grouped together for budgetary purposes, including: Section 220 loans in urban areas, Section 231 loans for elderly housing, and Section 207 loans for mobile home park development. Section 220 is a new construction program, distinct from 221(d)(4) in that it insures loans for multifamily housing projects in urban renewal areas, code enforcement areas, and other areas where local governments have undertaken designated revitalization activities. The program offers special underwriting allowances for greater mixed-use development. Section 231 is also a new construction/substantial rehabilitation program, but for projects specifically designed for senior citizens. For Section 231 projects with 90 percent or greater rental assistance, the maximum loan amount is 90 percent of the estimated replacement cost. For market-rate projects, the maximum loan is 83.3 percent of the replacement cost.

Tax Credit Projects. Projects assisted with Low-Income Housing Tax Credits may be insured under a number of FHA multifamily programs, but are grouped together in a single budget risk category. These loans have a lower risk of default than similar projects without tax credits and pay lower FHA mortgage insurance premiums.

Healthcare Risk Categories

Section 232 New Construction/Substantial Rehabilitation of Skilled Nursing, Assisted Living, and Board and Care Facilities. Section 232 programs are split into two budget risk categories, the first of which includes new construction and substantial renovation projects. The program enables access to capital that may not otherwise be available for many quality providers in underserved areas, thereby providing access to needed healthcare and residences for seniors. These loans are offered for terms of up to 40 years, and provide both construction and permanent financing. This risk category also includes Section 241(a) supplemental loans made to projects with a primary FHA Section 232 mortgage.

Section 232/223(f) Refinancing and Purchase of Existing Skilled Nursing, Assisted Living, and Board and Care Facilities. The Section 232/223(f) refinancing program has grown to be one of the highest volume insurance programs in GI/SRI, second only to the apartment refinance program in fiscal year 2011. This program offers loan terms of up to 35 years. For a refinance, maximum mortgage amounts are up to 85 percent of appraised value (90 percent if Borrower is a non-profit). For acquisitions, mortgages are insured up to 85 percent of the acquisition price plus transaction costs (90 percent of acquisition price if Borrower is a non-profit). Equity cash-out transactions are prohibited under this program. Section 223(a)(7)refinances of existing Section 232 loans are also reported under this risk category. In fiscal year 2011, new loan commitments for Section 232/223(f) and (a)(7) surpassed $3.4 billion and are projected to reach $6.9 billion in fiscal year 2012 and $4.6 billion in fiscal year 2013.



Section 242 Hospitals. The Section 242 program provides mortgage insurance for loans made for the construction, renovation, and/or equipping of acute care hospitals. An FHA guarantee allows hospitals to lock in low interest rates and *reduce borrowing costs for major renovation, expansion, replacement, and refinancing projects that help improve healthcare access and quality. Loans are up to 25 years in length, plus a construction period. The risk category also includes the following types of loans when made to hospitals: Section 241(a) supplemental loans; Section 223(a)(7) loans for refinancing current FHA-insured projects; and Section 223(e) loans for hospitals in older, economically declining urban areas. HUD has published a proposed rule that, when finalized, will enable HUD to resume offering Section 242/223(f) refinance loans. Under the current program, refinances are offered only for existing FHA loans, and standard Section 242 loans have to be at least 20 percent new construction. New loan commitments for all Hospital programs were $392 million in fiscal year 2011.*

Section 223(d) Mortgage Insurance for 2-year Operating Loss Loans. Section 223(d) insures short term loans that cover operating losses during the first 2 years after a project's completion (or any other 2-year period within the first 10 years after completion) for projects with a HUD-insured first mortgage. In 2012 and beyond, HUD plans to offer this type of mortgage insurance only to healthcare facilities with a primary mortgage under Section 232. Mortgage insurance on this type of loan has previously been offered (though infrequently utilized) for multifamily housing, but it is no longer viewed as a cost- effective means for preventing future losses on the associated primary FHA mortgages. The program remains a valuable option for Section 232 projects, which are more likely to benefit from the early infusion of working capital and thus avoid default on the primary mortgage. Beginning in fiscal year 2013, each 223(d) loan will be assigned to the risk category of the associated primary FHA mortgage.

Single Family Risk Categories

Title 1 Property Improvement. The Title I Property Improvement program insures loans for repairs and other improvements to residential and non- residential structures, as well as new construction of non-residential buildings. Property Improvement endorsements were $79 million in fiscal year 2011, and are projected to grow to $90 million in 2012 due to the recent addition to the program of a new lender and the implementation of the 2-year FHA "PowerSaver" pilot program (begun in the spring of 2011). Operating under Title 1 authority and regulatory framework, PowerSaver provides single family homeowners loans of up to $25,000 for proven energy improvements. Program lenders will receive incentive grants from the HUD Energy Innovation Fund to help lower the cost of loans to consumers.

Title 1, Manufactured Housing. Under Title I, HUD provides mortgage insurance for individuals to purchase manufactured homes. In fiscal year 2011, $42 million in manufactured housing loans were endorsed, with $28 million and $24 million projected for fiscal years 2012 and 2013 respectively. Projections are based on industry trends and actual activity in early 2012.

Mortgage and Loan Insurance Programs – GI/SRI Account

Staffing

FTE	2011 Actual	2012 Estimate	2013 Estimate
Headquarters	341	365	365
Field	806	805	822
Total	1,147	1,170	1,187

The primary workload for FHA programs in the GI/SRI Fund is borne by two organizations within HUD's Office of Housing: the Office of Multifamily Housing Programs and the Office of HealthCare Programs (OHP). In addition, critical functions are supported by financial, procurement, IT, and other administrative support staff. The workload of all organizations involved has been greatly impacted by large increases in loan volume experienced over the last 4 years. Key activities are as follows:

- Multifamily Housing: Field Staff process applications for mortgage insurance; review plans and specifications and cost estimates; conduct site reviews; perform mortgage credit analyses; participate in marketing and outreach of FHA programs; train FHA lenders; facilitate loan endorsements; process requisitions for release of mortgage proceeds; ensure compliance with Davis-Bacon wage rate requirements; conduct cost certification reviews; remit application and inspection fees to Headquarters in addition to asset management functions that include servicing loans, releasing reserves, managing properties, reviewing financial statements, processing and reviewing transactions such as prepayment requests, transferring physical assets and processing the disposition of assets.

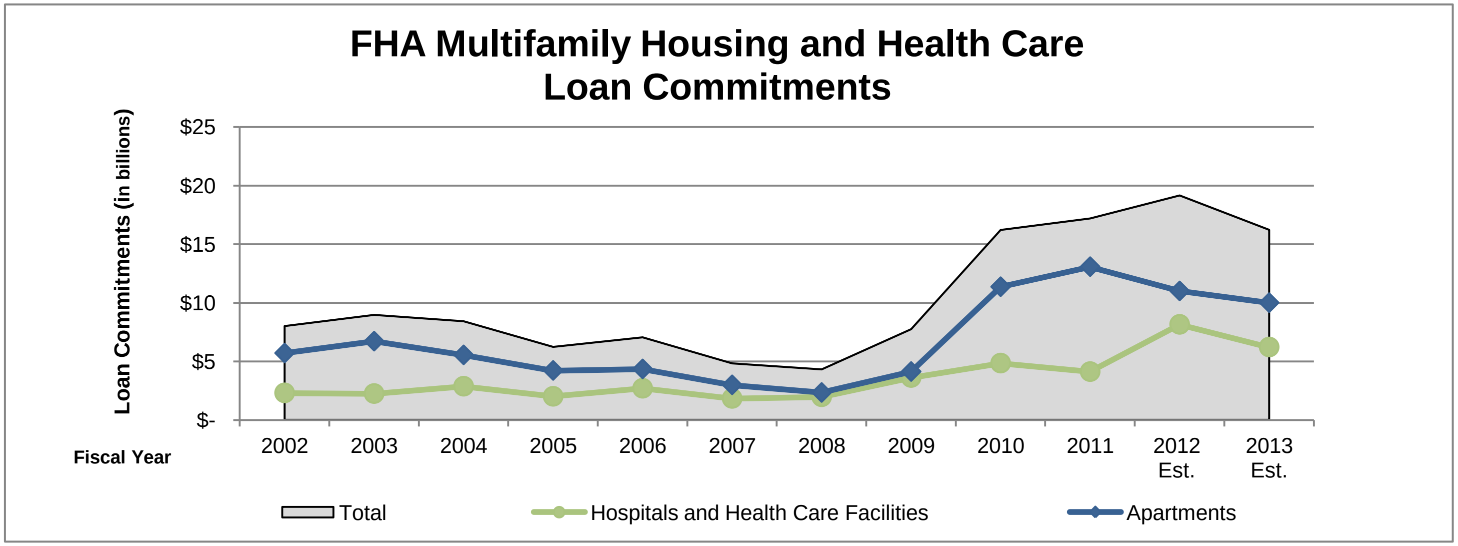
  Headquarters staff develop and update policy related to all aspects of implementing the program; provide oversight of FHA-approved lenders; provide oversight and monitoring implementation of FHA program policy and procedures; conduct training for FHA lenders and field staff; ensure that adequate funding is provided to the field for contract services such as inspections and other review functions required to implement the program; provide technical support and assistance to field staff; manage the operation of a National Loan Committee; and review regulatory waiver requests.

- Healthcare: OHP Staff hold similar responsibilities as described above, though the organizational structure and distribution of work between field and headquarters staff differ.

The increase in FTE in fiscal year 2013 will be dedicated to Multifamily Field staff. FHA continues to be a primary insurer of multifamily mortgages. Multifamily production, both the number of loans and units, has increased five-fold over the last 4 years with an escalated level of business expected to continue through fiscal year 2013. The heightened loan volume not only strains staff resources with the initial processing of applications, but also with the asset management and compliance responsibilities that follow in subsequent years.

3. Why is this program necessary and what will we get for the funds?

FHA's multifamily and healthcare programs are a critical component of the Department's efforts to meet the Nation's need for decent, safe and affordable housing. At a time, in particular, when there is unprecedented stress in the financial markets, FHA Multifamily programs provide the necessary liquidity so that communities can continue to provide quality affordable housing and assisted living/nursing home opportunities. Driven by low interest rates, more constrained lending in the conventional mortgage market, and improvements in HUD business operations, demand for FHA loan insurance for multifamily and healthcare programs has increased dramatically in the last 3 years. In fiscal year 2013, FHA is projected to issue loan insurance commitments providing financing for approximately 900 apartment projects with more than 150,000 units and for 656 healthcare facilities with more than 80,600 beds.



Approval of the requested GI/SRI commitment limitation of $25 billion for fiscal year 2013 will allow FHA to respond to the continuing high level of need for FHA programs and contribute to the nation's economic recovery. Loan volume projections for fiscal year 2013 are the product of several factors, including:

- Pace of recovery and re-engagement by the conventional market;
- Interest rates, which may significantly impact refinance activity;
- Changes in HUD policy to improve risk position;

- HUD capacity to process high volumes of applications; and
- Proposed mortgage insurance premium increases.

The following table indicates projected loan commitment volumes, credit subsidy rates, and subsidy obligations for each risk category in fiscal year 2013. Credit subsidy rates represent the projected net present value cost or savings to the government of operating a loan guarantee program, and take into account projected claims, pre-payments, premium revenue, and recoveries on defaults for a cohort of loans over their lifetime. For more information on credit subsidy calculation please see the Notes section of this justification.

Mortgage and Loan Insurance Programs – GI/SRI Account

GI/SRI PROGRAMS	Commitment Estimates FY2012	Commitment Estimates FY2013	Subsidy Rate FY2013	Negative Subsidy BA FY2013
Multifamily				
221(d)(4) Apartments New Construction/Sub. Rehab	$2,500,000,000	$2,525,080,000	-2.45%	($61,864,460)
221(d)(3) Non-profit Apartments	$35,000,000	N/A	N/A	
Tax Credit Projects	$1,264,000,000	$1,322,000,000	-3.15%	($41,693,864)
223(f)/223(a)(7) Apartments Refinance/Purchase	$6,176,000,000	$5,457,000,000	-4.66%	($254,296,200)
241(a) Supplemental Loans for Apartments	$18,000,000	N/A	N/A	
223(d) Operating Loss Loans	$2,000,000	N/A	N/A	
HFA Risksharing	$233,000,000	$233,000,000	-3.41%	($7,942,847)
GSE Risksharing	$100,000,000	$100,000,000	-2.15%	($2,150,000)
Other Rental (Sections 220,231,207)	$626,000,000	$462,000,000	-0.37%	($1,709,400)
MULTIFAMILY HOUSING SUBTOTAL	$10,954,000,000	$10,099,080,000		($369,656,771)
Section 242 - Hospitals (includes Refinances & Supplemental Loans)	$500,000,000	$1,078,000,000	-6.56%	($70,760,949)
Section 232 - Nursing Homes/Assisted Living				
Full Insurance for Health Care Facilities	$763,000,000	$512,000,000	-2.51%	($12,851,200)
Health Care Refinance Facility Refinance	$6,885,000,000	$4,625,000,000	-4.45%	($205,812,500)
Section 232 Subtotal	$7,648,000,000	$5,137,000,000		($218,663,700)
Title I				
Title I Property Improvements	$90,000,000	$97,000,000	0.00%	
Title I Manufactured Housing	$28,000,000	$24,000,000	-2.58%	($619,200)
Title I Subtotal	$118,000,000	$121,000,000		($619,200)
GI/SRI TOTAL	19,220,000,000	16,435,080,000		($659,700,620)
Stand-by Authority	$5,780,000,000	$8,564,920,000		
Total New Commitment Authority	$25,000,000,000	$25,000,000,000		

N/A=Not Applicable

Shining Examples – New FHA Projects

FHA's multifamily programs have encouraged the development of housing with important, positive benefits beyond just the permanent shelter of families. Many projects feature supporting energy conservation and sustainability efforts, and all new construction and rehabilitation projects stimulate job creation and preservation. One specific example is the Northfield Commons Apartments in Murfreesboro, Tennessee, a "Green" retrofit project with new energy-saving roofing installed throughout the 100-unit complex from an FHA-insured loan endorsed in January 2011. The following are more examples.

Houston House is a $43 million mortgage for the substantial rehabilitation of a 396-unit high-rise property in downtown Houston. It is a mixed use building incorporating "green" construction design features. It is located one block away from the rail line connecting downtown with the Medical Center, and within walking distance of all downtown attractions. The rehabilitation is 78 percent complete.

One Santa Fe is a Section 220 insured mortgage for the new construction of 438 units of market-rate and affordable housing near a major transit station located in the Arts district on the eastern edge of downtown Los Angeles. The project combines a $86.2 million FHA-insured loan with tax-credit and local funding sources to enhance resident affordability.

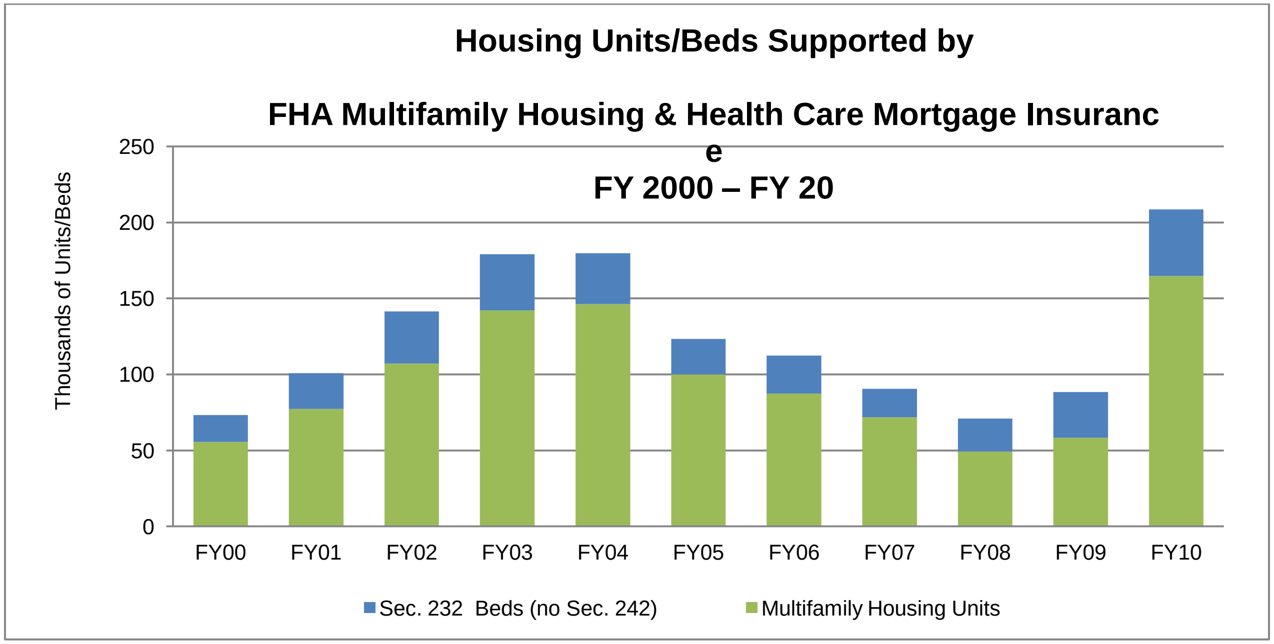
The Village at Odenton Station is a 235-unit apartment complex located adjacent to a Maryland Area Rail Commuter (MARC) stop halfway between Baltimore and Washington DC. Now under construction, the Village at Odenton Station will provide ready access for residents to employment opportunities at nearby Fort Meade, a facility affected by the Base Realignment And Closure (BRAC) commission, which will experience an increase of 9,000-16,000 military and civilian jobs in the next several years. An FHA-insured Section 220 loan of $61.4 million supports this development.

The principles of sustainable development also extend to Section 232 healthcare facility projects. The Elizabeth Seton Pediatric Center received $100 million in FHA-insured financing in 2010 for the construction of a skilled nursing facility to better serve Medically Fragile Pediatric Patients in Yonkers, NY, a designated underserved area. The new facility will include 137 beds to serve children from birth to 21 years of age. The Pediatric Center is committed to creating and sustaining a healthful, healing environment for its resident building users and community and has taken great efforts to design a green, sustainable building. The new building is expected to attain a LEED Silver certification. The grand opening is scheduled for February 2012.

In Chicago, a safety net hospital (Mercy Hospital and Medical Center) serving a socio-economically disadvantaged neighborhood obtained a $66 million mortgage as a result of FHA insurance. This mortgage allowed improved patient care through the renovation of a birthing center, improvement in a 10-bed Cardiac Care Unit, and updates to meet local building codes and improve patient safety. In addition, the resulting project generated 277 construction-related jobs and an economic stimulus of $83.9 million in the local community.

4. How do we know that this program works?

The greatest testament to FHA's effectiveness is the tangible result of its programs. Quality housing and healthcare facilities are made possible and/or more affordable throughout the country due to an FHA mortgage guarantee. For example, FHA recently approved mortgage insurance for a loan supporting the preservation of 312 units of affordable housing at Inwood on the Park in Dallas, Texas. The loan was endorsed in April 2011 and ensures the continued availability of housing for residents whose income is at or below 40 percent or 60 percent of area median income. This is just one example from the 1.1 million multifamily housing units that GI/SRI insurance has supported over the last 10 years.



In addition to the direct impact of production and preservation of needed multifamily housing units and healthcare facilities, FHA projects can be significant contributors to the economic health of a community. HUD has conducted economic impact analysis on both its Section 232 and Section 242 loans, which demonstrate significant economic stimulus during and after construction. For Section 232 projects, every $1 spent on construction generates an additional $2.83 in economic activity. For the 51 loans closed in fiscal year 2010, that means $1.56 billion in new economic activity. Post construction, those same loans will result in more than 5,000 new healthcare jobs. Section 242 hospital projects approved in fiscal year 2011 created 3,662 construction-related jobs and provided $726 million in economic benefit to local communities.

GI/SRI by the Numbers – FY 2011
Insurance in Force: $136 billion
New Commitments: $17.2 billion
- Average Multifamily Housing Loan: $9.8 million/150 units
- Average Section 232 Loan: $8.1 million/124 units
- Average Hospital Loan: $50 million/150 beds

Negative Subsidy Offsetting Receipts: $492 million
Premiums Collected: $774 million
Claims Paid - Single Family/HECM: $1.46 billion
Claims Paid - Multifamily/Healthcare: $338 million
Recoveries on Defaults: $531 million
Interest Earned on Cash Reserves: $540 million

With each mortgage it insures, FHA carefully considers the benefits to the community along with financial risks to the government. Cognizant of the increased risk associated with FHA's expanding role in the multifamily housing market, the Department has launched several new initiatives aimed at appropriately managing the risk involved with multifamily and healthcare loans. In fiscal year 2010, FHA made a number of updates to underwriting requirements for multifamily housing loans.

These updated requirements are part of a broader strategy that features a national loan committee process for all large projects, new initiatives (under development) to improve lender oversight, and a revised partial payment of claim policy that will generate savings by reducing the number of full claims. FHA also adopted a more balanced approach to loan-to-value and debt service coverage requirements and increased scrutiny of borrowers' other real estate obligations which could jeopardize their financial positions and make it more difficult for them to assist projects with financial or operational challenges. FHA is taking steps such as these to ensure its policies and practices do not contribute to any unanticipated losses.

As a companion to risk management efforts, FHA is proposing modest increases to mortgage insurance premiums (MIP) in fiscal year 2013 for market-rate projects. MIPs for Section 221(d)(4) loans are proposed to increase by 20 basis points and 223(a)(7) loans by 5 basis points, with a 15-basis point increase for all other multifamily housing and healthcare loans. As stated previously, the increases will not apply to affordable housing projects and those under FHA risk sharing programs. These MIP increases will not only better protect the government from losses and increase receipts to the Treasury, but will also encourage private lending to return to the market by ensuring FHA is not underpricing its risk.

In addition to strengthening performance in the portfolio, FHA has also taken steps to improve program administration through business process improvements. For the Section 232 program, a Lean Process has been adopted for both new construction and refinance applications. Lean Processing employs standardized work product and processes to obtain a consistent, timely result. The following are some of the specific changes implemented with Lean Processing: standardized checklists, statements of work for third party work, certifications, and templates for the lenders to use in their assembly of the application package; development of standardized punchlists for HUD staff to use in their underwriting of submitted applications; initiation of HUD legal review immediately when the Firm Application is submitted in order to cut down the time between Firm Commitment issuance and closing; and removal of portions of the application process/requirements for submittal that were duplicative or not necessary.

For the multifamily housing insurance programs, FHA has launched the “Breaking ground” initiative that focuses on optimizing processes, strengthening risk management, developing specialized skills of the staff and strengthening the way the organization manages this workload. The Office of Multifamily Housing is employing standardization of processes to achieve consistent and timely results. It has created a standardized loan underwriting review template, adopted an early warning system, created application staging areas, and standardized work products. It has established timeframes for which staff must strive to meet regarding the review and approval/rejection of applications. In addition, it has created a dashboard which tracks and reports the number of concept meetings, applications in processing, the number of decisions made and the length of time that applications are in processing as well as how many decisions are overdue for each multifamily processing office. The dashboard is reviewed monthly by Headquarters with each office to discuss the successes and issues/challenges that the office may be facing as it meets the targeted timeframes.

5. Notes to Justification

GI/SRI Single Family Portfolio

In addition to new insurance commitments for the multifamily, healthcare and Title 1 programs, the GI/SRI fund also houses activity on mortgage insurance and HUD-held notes for a number of large single family programs. Prior to fiscal year 2009, the GI/SRI Fund housed new insurance for a number of significant single family insurance programs, such as the Home Equity Conversion Mortgage (HECM) reverse mortgage guarantees and condominium unit financing. With the enactment of the Housing and Economic Recovery Act of 2008 (HERA), financial responsibility for almost all single family programs was transferred to the Mutual Mortgage Insurance (MMI) Fund. However, obligations made prior to 2009 (and the associated cash flows) remain in GI/SRI. Eighty-five percent of the current liabilities for loans guaranteed in the fund are associated with the HECM reverse mortgage program.

Credit Subsidy Calculations and the Annual Re-estimate

Credit subsidy rates represent the projected net cost or savings to the government of operating a loan guarantee program, and take into account the present value of projected claims, pre-payments, premium revenue, and recoveries on defaults for a cohort of loans over their lifetime. In accordance with the Credit Reform Act of 1990, administrative costs (excluding property disposition) are not included in credit subsidy calculations. FHA credit subsidy rates reflect historic performance data for similar loans made over the past 40 years, with adjustments made for significant policy shifts as well as changing economic and market conditions. The Department devotes significant efforts to updating and continuously refining the credit subsidy estimates. Each year the extensive statistical base from which projections of future loan performance are calculated is updated with an additional year of actual data. The Department and OMB continue to examine the data, assumptions, and calculations that are used to estimate loan program cash flows and subsidy rates in order to eliminate errors and improve the accuracy and reliability of projections.

Each year, FHA completes a required re-estimate of liabilities and subsidy costs associated with the existing insurance portfolio. Revised liability estimates take into account another year of actual performance and the latest economic assumptions. Vacancy rates, Treasury interest rates, individual property's past financial performance, and house price appreciation are among the key variables that shape GI/SRI's projected cash flows. Multivariate statistical models generate the claim and prepayment rates that drive calculations of the Fund's financial worth. To determine the re-estimate, the revised liabilities (net of projected loan default recoveries) are compared to the current assets on hand. When assets exceed projected liabilities, a downward reestimate occurs with the difference being transferred to the Treasury general fund as mandatory receipts. When projected liabilities exceed assets, an upward re-estimate occurs and the fund receives a mandatory appropriation to bring assets and liabilities into balance. For example, if the portfolio of loans made in a given year has a net liability of $250 million and cash on hand of $300 million, then the cohort would require a downward re-estimate in which $50 million would be paid from the Fund's financing account (which handles all loan guarantee cash flows) to the Treasury. Re-estimates are calculated each year for each cohort of loans. Twelve GI/SRI cohorts have net lifetime downward re-estimates, meaning costs to the government for that group of loans are now projected to be less than the original subsidy calculation. Eight cohorts have a lifetime upward re-estimate, meaning the original subsidy calculation is now believed to have underestimated costs. While GI/SRI's newer books of business consist primarily of multifamily and healthcare loans, it is important to keep in mind that GI/SRI re-estimates for all cohorts prior to 2009 include assets and liabilities for a large portfolio of single family loans (programs subsequently transferred to MMI).

HOUSING
GENERAL AND SPECIAL RISK INSURANCE FUND
Summary of Resources by Program
(Dollars in Thousands)

Budget Activity	2011 Budget Authority	2010 Carryover Into 2011	2011 Total Resources	2011 Obligations	2012 Budget Authority/ Request	2011 Carryover Into 2012	2012 Total Resources	2013 Request
Positive Subsidy Appropriation	$8,583	$9,724	$18,307	$1,765	...	$16,542	$16,542	...

NOTE: The fiscal year 2011 Budget Authority reflects $8.6 million appropriation net of the 0.2 percent governmentwide rescission, pursuant to the Department of Defense and Full-Year Continuing Appropriations Act, 2011, P.L. 112-10.

HOUSING
FHA-- GENERAL AND SPECIAL RISK INSURANCE FUND
Appropriations Language

The fiscal year 2013 President's Budget includes proposed changes in the appropriation language listed and explained below. New language is italicized and underlined, and language proposed for deletion is bracketed.

[During fiscal year 2012,] *New commitments to guarantee loans [incurred] insured under the General and Special Risk Insurance Funds, as authorized by sections 238 and 519 of the National Housing Act (12 U.S.C. 1715z-3 and 1735c), shall not exceed $25,000,000,000 in total loan principal, any part of which is to be guaranteed, to remain available until September 30, 2014: Provided, That during fiscal year 2013,*[.Gross] *gross obligations for the principal amount of direct loans, as authorized by sections 204(g), 207(l), 238, and 519(a) of the National Housing Act, shall not exceed $20,000,000, which shall be for loans to nonprofit and governmental entities in connection with the sale of single family real properties owned by the Secretary and formerly insured under such Act.* (Department of Housing and Urban Development Appropriations Act, 2012.)

<u>Changes from 2012 Appropriations</u>
In order to avoid any disruption in FHA's multifamily and healthcare mortgage insurance operation during a continuing resolution and eliminate the need for anomaly provisions, the Department requests that the $25 billion requested for loan guarantee commitment authority remains available for 2 years, rather than the 1-year authority requested in prior years.