FHA Program Adjustments to Support Refinancings for Underwater Homeowners

Today the Administration announced adjustments to Federal Housing Administration (FHA) programs that will permit lenders to provide additional refinancing options to homeowners who owe more than their home is worth because of large falls in home prices in their local markets. These adjustments will provide more opportunities for qualifying mortgage loans to be responsibly restructured and refinanced into FHA loans as long as the borrower is current on the mortgage and the lender reduces the amount owed on the original loan by at least 10 percent. This option should be available by the fall.

The new FHA loan must have a balance less than the current value of the home, and total mortgage debt for the borrower after the refinancing, including both first and any other mortgages, cannot be greater than 115 percent of the current value of the home – giving homeowners a path to regain equity in their homes and an affordable monthly payment. This refinancing will help homeowners by setting monthly payments at affordable levels and decreasing the mortgage burden for families owing significantly more than their homes are worth. Keeping more responsible families in their homes should support the continued recovery of the housing market.

FHA Refinance Option

1. FHA Refinance Option for Underwater Loans –Encouraging Responsible Restructuring and Refinancing

- Voluntary option encourages lenders and borrowers to work together, when appropriate, to restructure underwater mortgages. Because it is voluntary for lenders, not all underwater borrowers who meet criteria below will receive an FHA refinance loan.
- Enables refinancing into more sustainable loans that are no higher compared to the value of the home than the standard FHA refinance loan (97.75 percent).
- Lenders write down principal of the original first mortgage at least 10 percent to reduce the debt burden on borrowers, though we expect the average principal write-down to be significantly more than that.
- Enables refinancing to a reduced monthly payment at current low interest rates to facilitate affordable homeownership.
- Homeowner Eligibility
  - Homeowners must be current on their existing mortgage. They must occupy the home as their primary residence, fully document their income and have a qualifying credit score.
  - As with any loan forgiveness, this short refinancing should be reflected as a negative feature on a borrower's credit score.
  - Option is available to homeowners with mortgages not currently insured by the FHA.

2. Incentives for Principal Write-downs on Second Liens

- All mortgage debt including second liens must be written down to a maximum of 115 percent of the current value of the home to qualify for the refinance.

3. Transparency on Impact of These Refinancings

- FHA will publish data on number of loans, average percentage written down and quantity of principal reduced quarterly.

4. TARP Funded Support to Expand Impact of Refinance Option

- TARP funds will be made available up to a total of $14 billion to provide incentives to support write-downs of second liens and encourage participation by servicers, and to provide additional coverage for a share of potential losses on these loans.

The following information provides a brief overview of the key features of the refinance option. Detailed guidelines will be announced by FHA Mortgagee Letter.

1. FHA Refinance Option for Underwater Homeowners – Encouraging Responsible Refinancings

- Voluntary option for lenders and borrowers
- Encourages lenders and borrowers to work together, when appropriate, to restructure debts
    - Qualifying first lien mortgage loans must have a minimum write-down of at least 10 percent and total mortgage loan to value on the home can be no greater than 115 percent after the refinancing
- Eligible underwater loans are refinanced into new FHA loans on FHA terms for full documentation, income ratios, and complete underwriting
- Terms of FHA refinancing:
    - FHA loan will be equal to no more than 97.75 percent of the value of the home
    - Combined mortgage debt must be written down to a maximum of 115 percent of the current value of the home
    - Standard FHA mortgage insurance premium structure will apply
- Mandatory principal write-down as part of refinance
    - Minimum write-down by lender of 10 percent of the unpaid balance of the original loan
- Affordable monthly mortgage payments to facilitate affordable homeownership
    - New monthly mortgage payment at current low FHA interest rate
    - Total monthly mortgage payment, including for second mortgage, will not be greater than approximately 31 percent of income, and total debt service including all forms of household debt will not be greater than approximately 50 percent except for some borrowers with especially strong credit histories
- Existing lenders can retain second mortgages on the property, but only up to a combined 115 percent of the current value of the home
    - If there is an existing mortgage that is not extinguished, holders must agree to resubordinate and write off any amount over 115 percent of the current value of the home
    - The existing first mortgage is refinanced into a fully documented FHA insured mortgage at no greater than 97.75 percent of the value of the home
- Homeowner Eligibility
    - Homeowners must be current on their existing mortgage payment
    - Homeowner must occupy the home as their primary residence and fully document their income
    - Homeowners must qualify under standard FHA underwriting guidelines
    - Homeowners must have a FICO credit score of at least 500
    - Existing lenders/investors holding the first lien must agree to the principal write-down requirement. Thus, not all homeowners who meet above criteria will receive an FHA refinanced loan.
    - As with any loan forgiveness, the short refinancing should be reflected on borrowers' credit score
- Performance of these refinanced loans will not count against lenders for their Credit Watch scores, if the above parameters are met

2. Incentives for Principal Write-downs on Second Liens

- Incentives for immediate write-down of underwater second liens by lenders will be offered to encourage write-downs in connection with the FHA refinance.
- An extinguishment schedule will be implemented based on the below taking into account the likely distribution of the second lien lenders that will agree to immediate write-downs

Table: Extinguishment Price Schedule: Per Dollar of Unpaid Principal Balance (UPB) in Combined Loan-to-Value (CLTV) Range

	Second Lien CLTV Range		
Combined LTV	**105 to 115**	**115 to 140**	**> 140**
Projected Schedule	0.21	0.15	0.10

3. Transparency on Impact of These Refinancings

- FHA will publish data on numbers of loans refinanced in this way including average percentage written down and quantity of principal reduced quarterly

4. Up to a total of $14 billion in TARP funds to expand impact of refinance option

- TARP funds will be made available for incentives to support write-downs of second liens and encourage participation by servicers as well as the provision of coverage for some share of potential losses on loans. Total support provided through these three mechanisms will not exceed $14 billion.
- TARP funds will be used to provide coverage for a share of losses on loans up to a specified amount. The FHA will provide remaining loss coverage up to the maximum insurance coverage. Thus, the new lender will have a loan that is backed by the United States for up to 97.75 percent of the home value, as with other FHA refinance loans.
- TARP will purchase a letter of credit that will provide this loss coverage.