Regulators Mull Easing Of Rules on FHA Refis

Haircuts to market value, currently 13%, could drop below 5%

■ BY STACY KAPER

WASHINGTON — Regulators are considering easing standards to increase participation in Hope for Homeowners, a government program that began Oct. 1 but has sparked little interest from lenders or servicers, sources said Monday.

Lenders currently must agree to write down a mortgage to 13% below its market value to be eligible for the Federal Housing Administration program, which lets borrowers refinance loans worth less than their home's value. But regulators are thinking of reducing the required writedown to between 3% to 5% below market value, several sources said.

Whether that would be enough to make the struggling program more attractive to the private sector is unclear. Though the banking industry has long pressed for a reduction in the required writedown, many lenders are waiting for details on another Treasury Department plan to reduce foreclosures. That plan, which would guarantee lenders against losses if they agree to systematic modifications, could be announced by the Treasury and the Federal Deposit Insurance Corp. as soon as this week.

Industry representatives said that the Hope for Homeowners program has had little impact because few lenders have applied to take part, and that changing

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Regulators May Revamp Little-Used FHA Program

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the eligibility criteria could give it a boost.

"This hasn't been a gangbuster success," said Robert Davis, the American Bankers Association's executive vice president for government relations. "It's ramping up. ... Nothing's been approved. You have 50 or so loans in the queue; that's not going to change the landscape of America, so if that is the case, I'm not surprised that they might be looking at the range of changes they have discretion to make to make the program more attractive."

As late as July lawmakers and some regulators were touting the Hope for Homeowners program as a way to stabilize home prices. But expectations have dwindled, because few lenders appear willing to take the necessary writedown and securitized loans are difficult to refinance.

The recently enacted rescue bill gave a regulatory oversight board the power to revamp eligibility requirements to make the program more attractive. Regulators declined to offer specifics, while a spokesman for HUD said, "We have been reviewing a number of proposals for some time to help homeowners and no decisions have been made on any of them."

Many lenders also appear to be waiting to see if the Treasury-FDIC loan guarantee plan will offer them a better alternative. Under that program, lenders would keep the loan but agree to a modification program that could include principal writedowns, interest rate reductions, or maturity extensions. In return, the lenders would be covered for part of the losses if the modified loans do not perform.

Details on the plan have not been made public, but sources said the government is contemplating offering guarantees on roughly 2 million loans with a combined value of between $700 billion and $800 billion. Because the government expects many modifications to take hold, it expects to take losses of less than $50 billion over a two-year period, sources said.

Mr. Davis said that plan may be more attractive to lenders, since

Barr: The writedowns are not the sole reason for bankers' resistance.

know the details yet."

One industry lobbyist agreed, arguing that principal writedowns — even small ones — "are the least desirable option." Furthermore, the FHA, despite recently enacted modernization measures, is still seen as a cumbersome alternative, the lobbyist said.

But others disagreed. Another industry lobbyist said reducing the required writedown for the Hope for Homeowners program would have a beneficial impact.

"There will be significantly more takeup with a writedown to only 96% or 97%," the lobbyist said. "There are still challenges to the program. Applying for a new loan is still more complicated than a loan mod. It doesn't solve all the problems, but it's better."

Jaret Seiberg, an analyst with Stanford Group Co., said any effort to increase lenders' options would be welcomed. "From the market's perspective, any change that can put that $300 billion [the FHA refinancing program's capacity] to work is a good change," Mr. Seiberg said. "So lowering the haircut requirement could boost the use of the program and thus reduce foreclosures."

However, he also said doing that would not be sufficient by itself.

"The question is 'Is there more that can and should be done?' And the market clearly wants to see more steps taken," he said. "They want the FDIC proposal, they want an expansion of the FHA Secure to include fixed-rate loans, and they want steps that are going

the Center for American Progress, said servicers have been sluggish in preventing foreclosures using the available options, though diminishing the writedown could have a "small positive effect."

Regulators "may act reasonably quickly," he said. "I think that the change is likely to add some needed flexibility to the program."

But Mr. Barr cited persistent weaknesses inherent with the FHA program. Applications in the works are "infinitesimally small," he said, and not all the reasons relate to the writedown amount.

"The program didn't start until Oct 1. It took a long time" for the Department of Housing and Urban Development "to get regulations out and to get the program up and running," he said. "It wasn't really a priority for the administration, and then you build on top of that the fact it is somewhat restrictive, and I think that tells you a lot about why it hasn't been working. We really do need a broader program. The FDIC's ideas for a loan guarantee are positive."

The FHA refinancing changes and the FDIC-initiated loan modification plan are "complementary," Mr. Barr said, but the FDIC plan holds more potential.

"The FDIC guarantee program is likely to be easier to use and will more rapidly make a difference in the rate of restructuring, and so I think the guarantee proposal is likely to have a positive effect that is noticeable in the near term if they are able to succeed in getting the White House to sign off," he said.

Regulators could also seek to ease borrower eligibility requirements. Under the current program, the borrower's payment-to-income ratio cannot exceed 31%, and the debt-to-income ratio cannot exceed 43% for the FHA to insure a new mortgage immediately. Borrowers with higher ratios — up to 38% for payments and 50% for debt — may still participate, but the FHA would require a three-month trial.

Other ideas floating around that would require legislation include reducing or restructuring the premium rates, perhaps by cutting annual premiums in half, to 75 basis points, or even letting