

FHA
Mortgage

consumer protection
FHA

THE ROLE OF THE FEDERAL HOUSING ADMINISTRATION

by P. N. Brownstein
Commissioner, FHA

In a sense, FHA, like a great many other Government agencies, is entirely devoted to consumer interest, even though it approaches the interest of the consumer about as indirectly as one could imagine. Technically, it does no direct business with consumers at all. Rather, it protects organizations making loans to individual purchasers of homes or persons repairing their homes; and it protects these lenders through a premium paid by the consumer.

But even though technically the relationship is between FHA and the lender, the benefits flow to the consumer; for the insurance permits the lender to make high-ratio long-term loans which he otherwise could not make; the housing must meet certain standards; the mortgage must be in a certain form; and FHA exercises general review of the soundness of the transaction.

The effect of FHA's operation over 28 years has been to transform the Nation from one in which a minority of families owned their own homes to one in which a substantial majority are owners; to greatly improve housing standards; and to reform lending practices in a most salutary manner in favor of the consumer. This is not just true of FHA financing. The influence of FHA has affected the pattern of home financing generally.

You hear a lot of talk from some elements about the lack of wisdom in FHA financing terms which provide protection for lenders to make mortgage loans in a very high ratio of the value of the home. Actually, before FHA was established 100 percent financing on homes was not uncommon. Of course, it was obtained through the home owner's getting some short-term notes on his home, often containing a balloon clause. In those days lenders based their loans on the amount they could expect to recover from the property in the event of foreclosure; thus the property was the main consideration in making a loan.

Under the FHA system the emphasis is on the borrower. In effect, this policy of government says: we have sufficient faith in the borrower to insure the lender against any loss, if the borrower is extended mortgage credit within agreed limits. Our underwriting instructions place the emphasis on the borrower's qualifications.

We of course do assess the property as a consideration in this transaction. In doing so we require that the property meet certain standards that we consider necessary if its value is to be maintained over the life of the mortgage. Thus we have provided a way for the qualified borrower to obtain a property that we consider a good investment for him; and we require that the mortgage be in a certain form that provides for reasonable terms and complete amortization of the loan through monthly payments.

What I have said may be somewhat elementary, but it sets the stage for discussing what the FHA considers important in carrying forward President Kennedy's expressed interest in consumer protection and education.

In the field of home buying right now, the importance of consumer education cannot be over-emphasized. The reason this is of importance at the moment is that many homebuyers are realizing for the first time in their experience that shelter, indeed, does cost money.

For many years the depression and war-born housing shortage and spiraling inflation created an abnormal market situation in which people came to expect that they could unload a property at almost any time, and, in most cases, the property would have gained enough equity through inflation to equal what the owner had put into it, or even provide him with some profit.

In the late 1950's, supply began to catch up with demand in housing in most localities and with this balanced situation inflationary pressures were no longer important. Here people became faced with the realities of life in the home buying field, for it they had over-extended themselves or suffered an economic setback they were likely to lose their homes.

Not a great deal had been done to educate people to these facts or even to their responsibilities as home owners. In the past year and a half FHA has made major efforts to acquaint potential purchasers of homes with what the important considerations are. One of the problems of developing such an information and education program is finding the proper vehicle for transmitting the information to the public.

We have developed the information, but the problem is to get it before the public. How to do this, I presume, is one of the objectives of our meeting here today, and one of the purposes of this council.

We have used our normal channels, and worked through the various clientele of the agency, but a well organized national means of communication is needed -- not just in this field, but in many others.

But even through our somewhat limited means of getting to the public we have been able to make known on a fairly wide scale the availability of the several publications designed to acquaint consumers with FHA programs. The thirst of the public for such information is demonstrated by the quite large numbers of requests we receive when availability of a certain publication becomes known.

One of our basic publications devoted entirely to guiding potential home buyers into proper assessment of their financial considerations is, "FHA Financing for Home Purchases and Home Improvements." In the less than one year since its first printing, more than 100 thousand copies have been distributed -- mostly on individual requests. The publication provides a brief explanation of how FHA financing works and a guide to the answering of such questions as: How much do I

need to borrow to buy a particular home; how long should I take to repay the loan; and how much is the loan going to cost? Typical transactions are outlined and it is pointed out that a 30-year loan, which may be necessary to reduce payments sufficiently to make the purchase, costs about 60 percent more in total interest than a 20-year loan would cost, while the monthly payments on a 20-year loan are only about 20 percent higher than a 30-year loan. In a case such as this, you really pay your money and take your choice -- but it should be an educated choice.

The publication also provides a guide to calculating home buying ability and explains how FHA assesses a family's ability to make a given purchase. Some further information is provided about such generally unrealized facts as the necessity for obtaining a release of liability in an assumption of the mortgage by another party or the original mortgagor may still be liable if the other party defaults. Additional information is included about home improvements loans.

The availability of this and other FHA publications is made known through press releases and radio and television public service announcements. These media generally cooperate well, but their efforts naturally cannot fulfill the entire need.

FHA also has published a Home Owner's Guide, which is given to every buyer of a new home built under FHA inspection and financed with an insured mortgage. The purpose of the Home Owner's Guide is to explain the respective responsibilities of the FHA, the owner, and the builder, in the transaction. Many FHA buyers are undertaking home ownership for the first time and are not clear about where their own responsibility begins and that of the others in the transaction leaves off.

These publications and the others printed for consumer education by FHA all are important in today's home buying market and they tend to assist the buyer in realizing his obligations, thereby guiding him in making a sound financial transaction. But the agency is not content with this approach alone, and we try to be constantly alert to the possibility of perfecting the law to the maximum that we can, not only to broaden home ownership as much as we possibly can, but to protect home owners from circumstances beyond their control which may cause them to lose their homes.

In this balanced, noninflationary market, mortgages are more fragile, and recovery more difficult if an economic setback occurs. In 1959 an amendment to the National Housing Act provided for forbearance agreements between the borrower and the lender when an FHA loan is in temporary difficulty. A review of that provision in 1961 showed it to be procedurally unworkable, and the procedures were overhauled. Attempts were made to make the existing statute as flexible and easy to work as possible, but, even so, recent reviews of the effectiveness of the provisions have indicated legislative correction probably is needed, since the existing legislation sometimes makes foreclosure an easier and less costly way out for a lender when a borrower is in

trouble. Further, even at the best, forbearance arrangements are difficult to make under existing statutory authority. This particular problem is under agency study at the moment.

There are many ways in which FHA directly or indirectly serves the consumer -- through its minimum property standards, construction inspection, borrower's credit analysis, objective property appraisals, builder's warranty requirements compliance procedures, limitations of charges to buyers, market analyses, land planning services, technical studies, and so on.

The Kennedy Administration's 1961 Housing Act greatly broadened the possibilities for home ownership through its expansion and further liberalization of home mortgage insurance and its provisions for rental and cooperative housing to meet special needs of the elderly and of low-income persons.

This landmark legislation -- except for some small corrective needs which have emerged -- gave FHA a comprehensive set of programs.

Additionally, the FHA under this Administration has been brought into much closer coordination with the other constituent agencies of the Housing and Home Finance Agency. HHFA Administrator Robert C. Weaver has effected a degree of teamwork never before known in the HHFA complex. All this works to the public interest through better and more comprehensive community and housing development.

The income gaps between public housing and the regular housing market are being met through the channelling of private mortgage monies and special assistance funds into areas previously unserved. The major needs now in serving the requirements of home buyers and home owners are to protect as best we can against loss of a home by persons having temporary difficulties which they cannot control; continually to improve the risk analysis processes of the agency, in order to guard against miscalculations in the market which adversely affect the equities of property owners; and to continue to develop our credit and market evaluation processes in order to spread home ownership as widely as possible.

It is the spirit of this Administration to attempt in so far as possible to make a given program responsive to the needs of the people.

I certainly intend to see that this spirit is infused in that most basic area of public and social need -- housing.