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HECMs in the Regulatory and Congressional Spotlight

October 8, 2019
Consumer Financial Services Alert

Home Equity Conversion Mortgage (HECM) loans have attracted significant scrutiny from federal agencies and Congress in recent weeks. The Department of Treasury (the "Treasury") and Department of Housing and Urban Development (HUD) both released Housing Finance Reform plans that recommend structural changes to the HECM Program. On September 5, 2019, Treasury Secretary Mnuchin and HUD Secretary Ben Carson appeared before a Senate hearing entitled "Housing Finance Reform: Next Steps" to discuss their proposals.

On September 25, 2019, the House Subcommittee on Housing, Community Development, and Insurance convened a hearing entitled "Protecting Seniors: A Review of the FHA's Home Equity Conversion Mortgage Program." In advance of the hearing, the Subcommittee released two draft bills proposing various changes to the HECM Program. These bills and other HECM servicing issues were the focus of the hearing.

The Government Accountability Office (GAO) recently issued the findings of a study it conducted to determine if the HECM Program is accomplishing its purpose of providing financial and housing support to seniors. The GAO found that terminations increased significantly between 2014 – 2016, but that HUD failed to collect sufficient data for it to determine the root cause in approximately 30% of cases. The GAO called for HUD to collect more data concerning the reason for HECM terminations.

Housing Finance Reform

In March 2019, President Trump issued a Memorandum on Federal Housing Finance Reform, directing Treasury and HUD to develop proposals to reform the federal housing finance system, including the HECM program. The FHA's 2018 Report to Congress revealed that the HECM Program caused significant losses to the Mutual Mortgage Insurance Fund (MMIF). For fiscal year 2018, the HECM Program had a negative capital ratio of 18.83% and a negative economic net worth of $13.63 billion. Given these losses, the President tasked HUD Secretary Carson with addressing the financial viability of the HECM Program.

Treasury's Housing Finance Reform plan focuses on removing the government-sponsored enterprises Fannie Mae and Freddie Mac from conservatorship and establishing a new competitive secondary housing finance market. With respect

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to HECMs, Treasury called for eliminating HECM-to-HECM refinancing, creating geographically-based loan limit values that track those for FHA-insured forward mortgages, and developing new HECM servicing standards. Treasury recommended that Congress set a separate HECM capital reserve ratio for HECMs, remove HECMs from the MMIF and implement a "tiered pricing" framework.

HUD's financial reform plan criticized the HECM Program for its impact on the MMIF and urged FHA to "continue to develop policies that ensure its reverse mortgage product—HECM, which has cost the MMIF billions of dollars in claims in recent years—is fiscally sustainable." "To ensure that HUD and taxpayers are properly compensated for riskier loans, FHA should implement a 'tiered pricing' framework to protect the MMIF." The plan also proposed staffing increases for FHA and the Government National Mortgage Association.

Combined, the Treasury and HUD reform plans include 116 different proposed policy changes (49 from Treasury, 67 from HUD) to FHA programs. Many of the plans' more substantial provisions would have to be enacted by Congress, which appears unlikely this Congress. While there are many noteworthy changes the Administration believes could be enacted administratively by either FHA or the Federal Housing Finance Agency, the plan does not specify if and when these agencies intend to carry out these proposals.

On the heels of Treasury's submission of its reform plan to the President, Secretary Mnuchin, HUD Secretary Dr. Ben Carson, and Dr. Mark A. Calabria, director of the Federal Housing Finance Agency testified before the Senate Banking Committee as part of a hearing entitled "Housing Finance Reform: Next Steps." While the panelists did not discuss HECMs during the hearing, Secretary Carson's written statement submitted in connection with the hearing represented that HUD would "continue [to shore] up the HECM Program [to] best ensure these mortgage products remain a viable option for America's seniors" by pursuing the following recommendations:

- First, HUD recommends that Congress reform the loan limit structure in the HECM Program to reflect variations in local housing markets and regional economies across the U.S. instead of the current national loan limit set to the level of high-cost markets in the forward program ($726,525 for 2019);
- Second, HUD proposes that Congress set a separate HECM capital reserve ratio and remove HECMs as obligations to the MMIF—reforms that would provide for a more transparent accounting of the program costs and decrease the cross-subsidization that occurs with mission borrowers in the forward mortgage portfolio; and
- Third, HUD proposes that FHA eliminate HECM-to-HECM refinances as these loan transactions result in greater appraisal inflation, increase program costs, and negatively impact GNMA guaranteed HECM MBS due to quick 'churn' in pool participations.

The witnesses' prepared statements and testimony can be found here: Housing Finance Reform: Next Steps.

GAO Report: "Reverse Mortgages: FHA Needs to Improve Monitoring and Oversight of Loan Outcomes and Servicing"

The GAO recently issued a 106-page report of its findings of a study of 272,155 HECMs terminated between 2014 and 2018. The GAO observed a steep increase in borrower default rates from about 24,000 in 2014 to roughly 82,000 in 2016, before a decline to about 60,000 in 2018. The GAO found that the death of the borrower was the most commonly reported reason why HECMs terminated, but that the percentage of terminations due to defaults increased from 2 % in 2014 to 18 % in 2018. Most of these defaults were due to the borrowers' failure to meet occupancy requirements or pay property charges. The GAO disclosed that it was unable to determine the reason for termination in about 30% of cases. The GAO also noted that, based on the data it had access to, only 22 % of borrowers who went into default were placed into repayment plans but observed that this option.

The report criticized HUD's monitoring, performance assessment, and reporting on HECM performance and default servicing, finding that the HECM Program lacks comprehensive loan performance indicators and fails to track key performance metrics. The GAO recommended that HUD collect more comprehensive data, implement procedures for conducting on-site reviews of HECM servicers, and develop a risk-rating system for prioritizing and determining the frequency of reviews.

House Sub-Committee Hearing: Protecting Seniors: A Review of the FHA's Home Equity Conversion Mortgage Program

On September 25th, the House Financial Services Subcommittee on Housing, Community Development, and Insurance convened a panel entitled "Protecting Seniors: A Review of the FHA's Home Equity Conversion Mortgage Program." The hearing featured four panelists: Sarah Bolling Mancini, Staff Attorney, National Consumer Law Center; Alicia Puente Cackley, Director, Financial Markets and Community Investment of the Government Accountability Office ("GAO"); Laurie Goodman, Vice President, Housing Financial Policy, Urban Institute, and Mr. Bell. The hearing covered tax and insurance defaults, loss mitigation, and separating the HECM Program from the MMIF, among others.

In advance of the hearing, the Subcommittee unveiled two draft bills concerning the HECM Program. The first, "Preventing Foreclosures of Seniors Act of 2019," is sponsored by Financial Services Committee Chairwoman Maxine Waters (D-Calif.) and Rep. Denny Heck (D-Wash). The purpose of the bill is to help borrowers, and non-borrowing spouses avoid foreclosure. It requires mortgagees to defer placing a loan into due and payable status following the death of the borrower until the death of the non-borrowing spouse or other default, notify non-borrowing spouses of their rights and options for remaining in their home, offer repayment plans for delinquent property charges, and connect at-risk borrowers with HUD-approved counselors. The bill also requires HUD to provide Congress with an annual report of default volumes and the reasons for defaults. The bill is still in draft form. During the hearing, the bill sponsor, Rep. Heck, stated that the next draft would incorporate the GAO's recommendations.

The second bill, sponsored by Rep. Clay, codifies Treasury's recommendation to align maximum HECM loan limits with area maximum loan limits for FHA-insured forward mortgages. The key provision of the draft states:

In no case may the benefits of insurance under this section for a mortgage exceed the maximum dollar amount limitation […] for a residence of the applicable size for the area in which the residence subject to the mortgage is located, as such limitations may be increased for properties located in Alaska, Guam, Hawaii, or the Virgin Islands.

In his written statement to the House Financial Services Subcommittee on Housing, Community Development, National Reverse Mortgage Lenders Association President and CEO Peter Bell expressed skepticism with the proposal, noting that the idea of applying "area limits" to HECMs was discussed and rejected when the FHA adopted the single national limit in 2007-2008. "'Area-by-area' loan limits penalize homeowners who have improved and maintained their homes over the years and have accumulated more equity as a result of higher home values. Applying the forward mortgage concept of 'area limits' to a financial resource (HECMs) created for a completely different population at a completely different time of their life would be ill-advised."

The panelists uniformly praised the HECM Program for providing critical financial assistance to many seniors while allowing them to age in their homes. Both the panelists and members of Congress acknowledged that over the past few years, HUD had addressed most of the problems that had long plagued HECM loans by adding ability-to-pay requirements and non-borrowing spouse protections.

Despite these improvements, several panelists recommended additional changes to the Program. Ms. Mancini from the Consumer Law Center suggested that HUD should extend foreclosure deadlines and make loss mitigation mandatory for insurance and tax defaults. She also suggested streamlining non-borrowing spouses to obtain a deferral of due-and-payable status and improve communications with borrowers and non-borrowing spouses. She also suggested that escrowing for taxes and insurance should be the default position unless a borrower can demonstrate the ability to pay these items for the life of the loan.

The Urban Institute's Laurie Goodman likewise suggested that HUD should simplify reverse mortgage product design, lower costs for safer products, and redesign programs to reduce foreclosure frequency and loss severity. Ms. Cackley addressed the results of the GAO report, including the lack of data concerning the reason for approximately one-third of HECM foreclosures. She reiterated the GAO's recommendation that HUD should collect additional data concerning the causes of defaults and loss mitigation.

Based on this heightened Congressional and federal agency scrutiny, HECM industry participants can anticipate further program changes, whether through statutory updates or further rulemaking. We will keep you updated, as developments warrant.

Copies of the panelist's written statements, testimony, and draft legislation can be found here: Protecting Seniors: A Review of the FHA's Home Equity Conversion Mortgage Program.

About the Author

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