

Washington Report: FHA Tightening Standards

by Kenneth R. Harney

FHA is tightening up its standards for home buyers - but the changes are not as tough as some analysts had feared - especially on downpayments.

FHA commissioner David Stevens outlined the agency's new underwriting policies last week, including an increase in the "upfront" mortgage insurance premium charged all borrowers, and a decrease in the amount of financial inducements a home seller can provide a buyer.

The tightening of the rules come in the wake of findings by an independent auditor last Fall that FHA's insurance fund capital reserves have fallen far below the congressionally-required minimums.

HUD Secretary Shaun Donovan promised in response that FHA would take steps early this year to begin building up its reserves with higher premium revenues and ratchet up its credit standards for some borrowers.

Under the new plan, which will take effect shortly, FHA applicants will be charged a higher entry fee on insurance: An upfront premium of two and a quarter percent (2.25%) of the loan amount, instead of the current one and three quarters (1.75%) percent premium.

On a \$200,000 home purchase with a \$193,000 loan amount, the new premium will add about \$965 to an FHA borrower's costs.

There will be no immediate increase to FHA's current annual insurance premiums of zero point fifty five percent (0.55). But Stevens said the agency plans to ask Congress for a higher limit on annual premiums, which get tacked onto borrowers' monthly mortgage bills.

Once FHA gets Congress's okay, Stevens said he expects to boost the annual premiums and reduce the upfront premiums. That, in turn, will lower the cash borrowers need to bring to the table, and stretch out the higher premium charges over multiple years.

Stevens also announced that applicants with FICO credit scores below 580 will now have to make downpayments of at least 10 percent, up from three and a half percent currently.

That change shouldn't have much of an impact, however, since most of the largest lenders offering FHA mortgages already require a minimum credit score of 620 for all applicants.

Now for the good news on downpayments: Though mortgage industry analysts had expected FHA to raise its minimum cash down requirement to five percent, Stevens said 3.5 percent will remain the standard.

On the other hand, Stevens also announced that the agency is lowering its "seller concessions" ceiling from six percent to three percent, effective immediately. Concessions include contributions at settlement from the seller to the buyer to help cover loan fees and closing costs. Critics say the concessions often get lumped onto the house price -- thereby raising FHA's loss exposure.