April 17, 2023

The Honorable Julia Gordon
Assistant Secretary for Housing and Federal Housing Commissioner
Federal Housing Administration
U.S. Department of Housing and Urban Development
451 7th Street, S.W., Washington, DC 20410

Dear Commissioner Gordon:

The Community Mortgage Lenders of America (CHLA) submits this feedback to the questions asked in your request for information regarding the Federal Housing Administration's (FHA) key 203(k) loan program (Docket number FR-6366-N-01), a program that serves a very valuable niche, especially in select low- and moderate-income neighborhoods with inventory needing substantial renovations and repairs. Please see our responses below.

1. What information can you provide regarding ways in which the FHA 203(k) Program does or does not meet the needs of borrowers seeking to renovate or rehabilitate their homes?

This program is a great option for borrowers to purchase or refinance a home to make it the home they want at generally a *much more* affordable price. But as detailed below, the program does need some modernizing.

2. What policies or processes governing the 203(k) Program could be streamlined, modified, or eliminated to enhance your experience with the 203(k) Program?

FHA should consider less-restrictive advances to the contractor at closing on the Standard 203(k) program, as is allowed on the Streamlined program. For the Standard 203(k), borrowers must have significant cash to prepay advances, which is a key impediment to renovation in the most-needed neighborhoods. Simply put, much of this borrower population does not have extra cash, and contractors will not forward theirs to fill the gap. Both FNMA and FHLMC allow advances up to 50% of the total estimated material costs at closing; even on a Standard construction loan, lenders may advance some estimated costs to the builder/contractor at the initial closing. A reform here would be a game changer for FHA.

3. How could FHA increase participation in the 203(k) Program?

For borrowers, we need to reduce the cost of financing. In an increasing-interest-rate environment, reducing monthly MI would help borrowers qualify by keeping their debt ratio down. Currently the conventional renovation loans have been a better fit for borrowers that qualify (even with a slightly higher interest rate) due to (a) the lower monthly MI costs; (b) the fact that there is no up-front mortgage insurance added to the loan amount; and (c) the ability to remove MI from the loan once 78% LTV has been reached.

Our experience is that a borrower will always opt for a FNMA/FHLMC renovation loan vs. FHA if they qualify. We do understand that the FHA may not agree to lower premiums here, but failure to do so will prove a major cap on program demand.

4. The Standard 203(k) Program relies on a 203(k) Consultant to determine if a property meets the requirements of the program. What changes would you recommend to FHA's 203(k) Consultant requirements to enhance the program while ensuring a subject property would, after improvements, meet FHA's Minimum Property Requirements (MPR) or Minimum Property Standards (MPS)?

We are seeing consultants in our market area retire or drop from the program – we don't believe the quality of the consultant should be compromised, as they serve a critical role in protecting the borrower, but there needs to be some solution to increase the number of consultants, as they absolutely make the program run smoother for the mortgagees. We would like to consult with HUD on how we might work together to boost the numbers of qualified consultants.

5. What methods would you recommend HUD use to increase stakeholders' awareness about FHA's 203(k) Program?

HUD could use social media channels and other media venues to bring awareness to the program. CHLA believes we are fighting an old, preconceived notion that 203(k) loans are difficult and arduous to complete. Providing education and product information to the public--well as agents and loan officers--regarding how the program actually works would help greatly in this area.

6. Supporting local authorities' efforts to preserve and expand single-family housing is an important goal of HUD's strategic plan. Please describe how HUD could better support local authorities' efforts to increase the stock of available and affordable single-family housing using the 203(k) Program, especially in underserved communities. What role could the program play in improving the supply of available housing in underserved communities?

Many HFAs do not allow their grant programs to be used for renovation lending. In addition, many community-grant organizations do not allow their grants to be used for renovations. Largely, this is because 203(k)s, and other renovation programs, lend on “future value” and there may be presumed risk due to lack of understanding of the program. CHLA recommends HUD educate community foundations and HFAs about the benefits of renovating homes in declining neighborhoods. Often property ‘flippers’ buy these properties, make minimal renovations to the home, and sell the property to the same buyer who COULD HAVE obtained their own financing and made possibly more quality renovations at a lesser cost.

8. What state or local regulations impact the use of FHA’s 203(k) Program?

At present, CHLA is unaware of any state or local regulations that would adversely impact the use of FHA’s 203(k) program.

9. The 203(k) Program parameters limit the types of eligible properties and improvements. Please describe any rehabilitation needs not served or underserved due to the existing program requirements and how could the 203(k) Program be enhanced to address those needs.

CHLA has not found property parameters to be an issue with these loans. CHLA DOES SUPPORT increasing the renovation amount on the Limited 203(k) program from $35,000 to at least $50,000. A revision of this limitation would expand access in underserved communities and improve participation in the program.

10. The 203(k) Program is currently underutilized by nonprofits and governmental entities. What type of changes would encourage more nonprofits and governmental entities to increase their participation in the program?

While lenders try to educate the HFAs and nonprofits on the value of renovation loans, HUD’s direct communication will garner more attention and possibly hasten more change. Downpayment and closing costs are the single-largest obstacle in purchasing a home. The grant and assistance programs offered by HFAs and nonprofits would be a huge benefit to potential borrowers. It will take HUD’s education to move the needle on this subject. (Also, please see our answer to Question 6 above for additional input relative to Question 10.)

11. What are the benefits or drawbacks to re-opening the 203(k) Program to other parties that acquire and rehabilitate distressed single-family properties in underserved communities?

The risk is property 'flippers' will put some lipstick on the property and a borrower may overpay for less-than-qualify work. The 203(k) consultant must provide strong oversight so investors and other third parties don't slide on guidelines & quality. There is a reason HUD eliminated the 203(k) investor option.

12. What technology solutions could improve the availability of, or facilitate, the 203(k) Program?

There are several technology solutions that could improve the availability and efficiency of the 203(k) Program. One potential solution is to create an online portal that provides borrowers, lenders, contractors, and consultants with easy access to information about the program. The portal could include information about eligibility requirements, program guidelines, and loan limits, as well as tools for calculating renovation costs, tracking project progress, and submitting loan applications. Another potential technology solution is the use of mobile applications that enable borrowers and contractors to communicate and share project updates in real-time.

13. Currently, HUD-approved housing counseling agencies provide advice about FHA-insured loans to potential and current homeowners. Should housing counseling agencies play a more significant role in educating consumers about the FHA 203(k) program?

Yes, as it would at least let potential homeowners know about program and how it works. Additionally, if nonprofits were ever to offer down payment or closing cost assistance, they would have the assurance of knowing that the homeowners had been educated on the 203(k) program and how it works.

14. What are the advantages and disadvantages of the 203(k) Program compared to other sources of rehabilitation financing? Are there changes to the program you recommend in light of these?

Disadvantages:

1. The cost of financing, pertaining specifically to mortgage insurance. If, for example, MI could be dropped from the payment when the loan to value equals 78% or less, as with conventional financing, the 203(k) loan would be much more attractive to borrowers in general.
2. Offering a percentage of estimated up-front material costs (at closing) to the contractor would entice more of them to take on renovation loans. Most contractors scoff at having to carry the costs themselves until enough work has been done to warrant a draw request.

Advantages:

1. The FHA 203(k) program to be a great option for potential homeowners. The lower credit score and down payment requirements make it a great option for borrowers with limited cash.
2. The renovations that are allowed under the program meet and/or exceed most borrower's needs.

15. Are there any requirements of the 203(k) program that might restrict utilization by any underserved groups of borrowers and what changes could HUD make to the program to encourage more utilization by these groups

FHA's credit standards are more forgiving than conventional, which is FHA's significant advantage.   However, this advantage comes at a cost to the borrower. FHA's high-cost mortgage insurance drives out higher-quality borrowers from this program. HUD should consider lowering the MI/tiering the MI based on credit score levels.

We appreciate your consideration of our comments and recommendations.

Sincerely,

COMMUNITY HOME LENDERS of AMERICA