

FEDERAL HOUSING ADMINISTRATION
WASHINGTON, D. C.

OFFICE OF THE
FINANCIAL ADVISER

August 7, 1937

Dear Mr. Eccles:

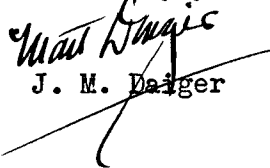
Enclosed are five copies of the revised and shortened memorandum to which I referred in my note of last evening. I am also enclosing five copies of the proposed amendments.

My personal view of this matter is that the White House is the place where a clear understanding of these proposals to stimulate the building of rental housing will be needed next week. I therefore think that if you are still inclined, as you were a week or so ago, to talk directly with the President (or with his son James) and explain the bearing of these proposals on the large economic aspects of the construction industry, you would do far more to insure the adoption of the amendments than if the President were left to obtain his impressions of them from someone much less informed and experienced in the matter than you are.

It is virtually certain that, after a bill is reported by the House committee and passed by the House, and before any meeting of the Senate and House conferees takes place, Senator Wagner and Congressman Steagall will have separate and joint meetings with the President. It is in advance of these talks that the President will need to understand the significance of the proposed amendments, for both Wagner and Steagall will be looking for explicit instructions as to what the President wishes and what the party leaders in the Senate and House will be asked by the President to support.

As the House committee, according to my information, is planning to hold an executive session on Tuesday, I should think it likely that Steagall would be seeing the President on Monday.

Sincerely yours,


J. M. Dainger

Honorable Marriner S. Eccles
Hotel Shoreham
Washington, D. C.

NATIONAL MORTGAGE ASSOCIATION DEBENTURES

(Housing Bonds)

Congress has authorized the purchase of National Mortgage Association debentures by national banks, and has also authorized the Comptroller of the Currency to classify these debentures as investment securities rather than as real-estate loans. In addition, the purchase of National Mortgage Association debentures has been authorized under State enabling legislation as follows:

By commercial banks in 47 States

By savings banks in 37 States

By trust companies in 46 States

By building and loan associations in 34 States

By life insurance companies in 42 States

By trustees in 41 States.

In somewhat the same proportion as to the number of States, these several classes of institutions have been authorized to purchase the capital stock of National Mortgage Associations.

Memorandum on Amendments to Existing Housing Legislation

Suggested for Inclusion in the Wagner-Steagall Housing Bill

In view of the importance of encouraging the private financing and construction of rental housing for families of moderate income, simultaneously with the program of public housing contemplated in the Wagner-Steagall bill, it is suggested that the attached amendments to the National Housing Act be included in the bill.

The first two amendments are to Sections 201 and 203 respectively and extend the principle of mutual mortgage insurance to the very common but important type of small walk-up apartment properties. These properties are now excluded from the mutual mortgage insurance principle because they are not insurable under Section 203, under which insurance is limited to mortgages not in excess of \$16,000 and covering dwellings for not more than four families. On the other hand, they are not practicable for insurance under Section 207, the limited-dividend housing section, because of its restrictive provisions. A great impetus to sound residential construction all over the country would be given by the adoption of these amendments.

An equally great impetus to sound rental projects would be given by the other three amendments. These relate to the financing by private capital of mortgages insured under Section 207 on limited-dividend housing projects, such as the Colonial Village, Buckingham, and Falkland developments in the suburbs of Washington. However, operations under this section of the National Housing Act have been seriously impeded by the unsatisfactory language of this section and Sections 301 and 302.

The third of the suggested amendments makes several changes in Section 207 that are intended to meet legal objections to the language of the section as it now stands. In the first place, the amendment expressly states that separate units of a limited-dividend housing project may be sold off under proper regulation protecting the buyer and the lender. In the second place, the section as it now stands authorizes mortgage insurance on housing "for persons of low income". It has been found impossible as a practical matter to define this clause and it has therefore given rise to many legal questions. It is replaced in the amendment by a definite limit of \$1,300 per room on the amount of mortgage that may be insured. This limitation follows in principle the limitation of \$16,000 which is placed on the amount of mortgage per house which may be insured under Section 203.

The fourth and fifth amendments are to Sections 301 and 302 of the National Housing Act and are intended to facilitate the financing of these limited-dividend projects. The amendment to Section 301 permits the national mortgage associations provided for in the Act to make loans on limited-dividend housing projects, if the loans are secured by mortgages insured under Section 207. This amendment applies only to loans made on large-scale housing projects and does not permit a national mortgage association to compete with banks, building and loan associations, etc., in making individual small-house loans such as are insured under Section 203.

The Amendment to Section 302 increases the ratio of debentures which a national mortgage association may issue from 12 times its capital stock to 20 times. This amendment is necessary because of the small spread between the interest paid and income received on which a national mortgage association must operate. In no instance to date has an insured mortgage loan on a limited-dividend project carried an interest rate in excess of $4\frac{1}{2}$ per cent. The associations that would hold a large amount of these mortgages in their portfolios will have to sell their debentures at a very narrow spread and it is therefore necessary to allow them a reasonably large turnover of business if they are to be permitted to cover their expenses and make a fair profit. As the associations can issue debentures only against insured mortgages, Government securities, and cash, the increase in the ratio of debentures to capital which is provided for in the amendment is neither excessive nor unsound. On the contrary, the quality of these three limited classes of assets behind the debentures, in addition to the capital of the associations, assures investors in the debentures all the protection that is required.

No additional State enabling legislation, nor Federal legislation applicable to national banks, is now required to permit the national mortgage associations to enjoy a wide market for their debentures among commercial and savings banks, trust companies, building and loan associations, life insurance companies, and other financial institutions. The debentures also furnish a desirable investment for individual investors, endowment funds, and individual trusts. Without these associations the principal outlet for large loans on limited-dividend projects is the large insurance companies, which necessarily limits the market for them. With one or more of these associations in active operation, however, the debentures would be readily salable to all types of investors and a larger supply of moderate-priced rental housing thereby assured.

AMENDMENTS

Section 201 (a) of Title II of the National Housing Act is amended by striking out the words "not more than four" and inserting in lieu thereof the words "one or more".

Section 203 (b) subsection (2) of Title II of the National Housing Act is amended by striking out the work "executed" and the period at the end of said subsection and inserting in lieu thereof the following: "insured, or cover a multi-family dwelling and involve a principal obligation in excess of \$16,000 but not in excess of \$200,000 and not to exceed 80 per centum of the appraised value of the property as of the date the mortgage is insured: Provided, that such part thereof as may be attributable to dwelling use shall not exceed \$1,000 per room; and provided further, that the application for insurance in respect of such mortgage shall be submitted prior to the beginning of the construction of such multi-family dwelling."

The first sentence of Section 207 of Title II of the National Housing Act is amended by striking out the words "persons of low income" and inserting in lieu thereof the words "rent or sale", and by inserting after the word "rents" the words "conditions of sale,". The second sentence of said section is amended by striking out the period after the figures "203" and inserting in lieu thereof a comma and adding the following: "and such part thereof as may be attributable to dwelling use shall not exceed \$1,300 per room."

Section 301 (a) of Title III of the National Housing Act is amended by striking out the semicolon after the word "purchased" in

said section and inserting in lieu thereof a comma and adding the following: "and to make loans and advances upon real estate secured by mortgages and other first liens which are insured under section 207 of this Act and to purchase and sell such mortgages or partial interests therein;".

Section 302 of Title III of the National Housing Act as amended, is further amended by striking out the word "twelve" in the first sentence of said section and inserting in lieu thereof the word "twenty".

EXCERPTS FROM THE ADDRESS OF SENATOR ROBERT F.
WAGNER BEFORE THE NEW YORK BUILDING CONGRESS, IN
NEW YORK, THURSDAY AFTERNOON, JANUARY 30, 1956.

But priming can not go on forever. The ideal situation exists when labor and idle private capital are brought together in a mutual enterprise. Our major economic task in the United States is to find that enterprise and set it in motion.

It is a grievous mistake to entertain fears that a low rent program would encroach upon private industry. In the first place, it would by very definition be confined to that section of the population which individual enterprise alone can not serve. Its tenants would be limited to those whose incomes would not permit them to seek similar quarters elsewhere.

In either event, purely private housing will have a larger market than it can supply. It seems clear that at least 75 per cent in number of the 10,000,000 family units to be built during the next ten years, or 7,500,000 of them, will be built by private industry alone. This includes, of course, apartments and small homes. At an average capitalized cost of \$4,000 for each family, the private building program involves investment opportunities of \$30,000,000,000 or about \$3,000,000,000 per year.

Despite the accelerated tone of residential construction, the Federal Government should continue to add pace to a lagging development. One of the barriers to home buying today, is that the average prospective owner of a \$4,000 or \$5,000 home can not afford to make the down payment of about twenty per cent that is required before the government will protect the mortgage loan. The government might obviate this difficulty by encouraging private mortgage institutions to bear a larger portion of the initial cost of this type of home building. Let me give a concrete example. It is reasonable to believe that the purchaser will be able and willing to make a down payment of approximately 10 per cent. Today 80 per cent can be supplied by private first mortgage loans, amortized over a twenty-year period, and secured by government insurance. I think that the wheel of the construction industry would be set in rapid motion if the government would extend its insurance of mortgages up to 90 per cent. Thus if the government were willing to increase its protective undertaking by only one eighth, it would provide the final incentive for private investment of \$3,000,000,000 per year, and of \$30,000,000,000 within a decade. This proposal should be coupled with the British practice of requiring the builder to guarantee the payment of the mortgage down to 75 per cent. In this way, the British have generated a tremendous home building program that has put decent quarters within the reach of millions.

In conjunction with this action, the Federal Government should assist in other ways. It should continue the work of the Federal Housing Administration in reducing mortgage costs by eliminating multiple-financing and sharp practices. It should lend its influence toward keeping private first mortgage interest rates at a level that will not prove onerous to borrowers. The Government might also guide improvements in the relevant laws of the states and municipalities.

In addition, the Government should widen the areas of eligibility for Federal protection. Under the present law, while mortgages issued prior to July 1937 are ultimately guaranteed by the government itself, those issued subsequently are to be protected only to the extent of the insurance fund. While we all have just confidence in the adequacy of this fund, the more complete security should be afforded in both types of cases. Amendment to the existing law should raise from \$1,000,000,000 to two or three times that sum the limitation upon the public protection of mortgages upon new construction.

Yet another change suggests itself. Today, insurance of large-scale mortgages is confined to rental projects. It should be extended to cover the large-scale development of small individual homes.

There is little reason why the powers of the National Mortgage Associations, which are private institutions, should not be expanded. They ought to be allowed, not merely to purchase the insured mortgages of other institutions, as now provided, but also to make mortgage loans on large-scale projects that are insured by the Federal Housing Administration. Their debentures against insured mortgages, instead of being limited by a law to twelve times the amount of their capital funds, should be allowed a margin at least twice as large. With these improvements in law and practice, the full possibilities of the Federal Housing Act will come closer to realization.