

August 9, 1937.

MEMORANDUM:

TO - Mr. Steagall
FROM - Chairman Eccles

Attached herewith are the amendments to the Housing Bill about which I talked to you over the telephone and which I hope can be incorporated in the Wagner Bill. I am also attaching a brief memorandum which explains the amendments.

Attachments.

ET:b

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MEMORANDUM:

TO - Mr. Goldsborough
FROM - Chairman Eccles

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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 housing for rent to families of moderate income, simultaneously with the program of public housing contemplated in the Wagner-Steagall Housing Bill, it is suggested that certain additional provisions be included in this bill that will in effect be amendments to the National Housing Act.

These amendments are based on the fact that construction in 1937 appears likely to provide fewer than 400,000 dwelling units, whereas approximately 3,000,000 houses or apartments will be needed within the next four years to avert a serious housing shortage. Substantial increases in construction are imperative both to prevent rents from rising rapidly and to increase industrial activity and employment and thereby increase the national income.

The loan and subsidy provisions of the Wagner-Steagall Housing Bill will meet part of this need, but even if the facilities of the bill should be availed of to the maximum, they would lead to the construction of fewer than 300,000 family units over the next three years, or approximately 10 per cent of the total requirements for that period. The bulk of the required housing, therefore, must in any event be provided by private capital and private enterprise.

The Federal Government already has a workable and working plan to assist the private financing and construction of housing for rent, as well as housing for sale, to families of moderate income, under a program which involves no lending or other investment of Government funds, but which does impose certain minimum standards of sound financing and sound construction in return for the granting of mutual mortgage insurance that is paid for by the borrower in return for exceptionally favorable terms of financing.

The utmost possible development of this program is needed in order to promote the further expansion of residential construction and yet to keep a speculative boom from developing with all the after-consequences which that would involve. The amendments suggested are the minimum necessary to allow this development to go ahead.

The first two amendments (to Section 201 and Section 203, respectively) provide for the extension of mutual mortgage insurance to the very common but important type of small, walk-up apartment

properties. Such properties are now excluded from mortgage insurance by the limitation of insurable mortgages under Section 201 to four-family dwellings and under Section 203 to \$16,000. A great impetus to sound residential construction would be given by the adoption of these amendments.

An equally great impetus to sound residential construction would be given by the other three amendments. These relate to the financing, by private investors under mutual mortgage insurance, of limited-dividend housing projects similar to the Colonial Village, Buckingham, and Falkland developments in the suburbs of Washington. Equity capital for such developments is available in abundance; mortgage funds are potentially available in much greater abundance; but counsel for large institutional investors have found certain flaws, from a legal point of view, in the wording of the legislation under which mutual mortgage insurance on limited-dividend projects is granted.

The third of the suggested amendments (that to Section 207) meets the principal objections from this source. In the first place, it is explicitly stated that units of a limited-dividend housing project may be sold, under proper regulation protecting the buyer and the mortgage lender, as well as rented. Heretofore this has only been implied in the law. In the second place, the vague provision contained in existing law, that the projects insured must be for "persons of low income", is replaced by a definite limit on the amount of mortgage per room that may be insured, just as under Section 203 a definite limit of \$16,000 is placed on the amount of mortgage per house that may be insured.

It will be noted that a similar limitation is contained in the second amendment, but that the amount of the limit is different. The reason for the limitation of the mortgage to \$1,300 per room in the case of limited-dividend housing projects (which is equivalent to a limitation of total costs to about \$1,600 per room) is not because the cost of such developments is any higher ordinarily than the cost of the small, walk-up apartment houses, but only because it is necessary to allow for the exceptional case of construction in those large cities where high land costs and the greater cost of fireproof and elevator construction must be met. The actual average to date of mortgages on insured limited-dividend projects is less than \$1,000 per room.

The last two amendments (those to Section 301 and Section 302) will facilitate in another way the financing of limited-dividend housing projects. The funds of large institutional lenders which are available for making these large loans in single blocks are necessarily limited. On the other hand, almost unlimited funds are

potentially available from individual investors and from financial institutions generally if it were made possible for them to invest on a smaller scale. Existing law authorizes the establishment of a special type of institution, known as national mortgage associations, which may hold insured mortgages and in turn sell debentures or "housing bonds" against them. No additional State enabling legislation, nor legislation affecting national banks, is now required to permit national mortgage associations to enjoy a very wide market for their debentures among commercial and savings banks, trust companies, building and loan associations, life insurance companies, and other financial institutions. Nevertheless, the formation of the first national mortgage association still awaits two essential enlargements of the powers permitted to it.

The first of these would permit a national mortgage association to make loans on limited-dividend housing projects on the security of insured mortgages. This amendment applies only to limited dividend or public-housing projects and does not permit a national mortgage association to compete with banks, building and loan associations, etc., in making the ordinary insured mortgage loan.

The last amendment is necessary because of the small spread between interest paid and interest received on which a national mortgage association must operate. In no instance to date has an insured mortgage loan to a limited-dividend project carried an interest rate higher than $4\frac{1}{2}$ percent. The association will be able to float its own debentures at somewhat lower interest rates, but not at a very much lower rate on the average. It is therefore necessary to allow the association a reasonably large turnover of business if it is to cover its expenses and make a fair profit.

The 12-to-1 ratio of debentures to capital permitted under existing law is insufficient to make the business of an association reasonably profitable. The association must hold cash, Government securities, and mortgages insured by the Federal Housing Administration up to the full amount of its outstanding debentures, and the 20-to-1 ratio provided for in this amendment is neither excessive nor unsound in view of the quality of these assets.

MEMORANDUM ON PROPOSED AMENDMENTS TO THE WAGNER HOUSING BILL

It is proposed to submit certain amendments to the Wagner Housing Bill which in effect will be amendments to the National Housing Act.

Because of the present wording of the National Housing Act, there has been some hesitancy for large loaning organizations, such as insurance companies, to lend funds on limited dividend housing projects insured by the Federal Housing Administration. The National Housing Act states that mortgages should be insured only on limited dividend structures erected for "persons of low income". Some loaning agencies have stated that until the words, "persons of low income" have actually been legally defined they have no way of knowing whether an insured mortgage on a given piece of property actually comes within the intention of the law.

It is proposed that the National Housing Act be amended (by an amendment to the Wagner Bill) so as to delete the words, "persons of low income", and substitute therefor a clause which permits the Federal Housing Administration to insure limited dividend housing where the amount of the mortgage is not in excess of \$1,300 per room. Such an amendment will make it possible for the Federal Housing Administration to insure loans on limited dividend housing up to a maximum of this amount. It will be particularly effective in stimulating limited dividend housing in the larger metropolitan areas for families with incomes up to \$1,800 a year.

A second amendment is suggested to overcome a defect in the present National Housing Act, which fails to make specific authorization for the mortgage associations provided for in the Act to make loans to limited dividend housing corporations. Such mortgage associations are now only permitted to buy insured mortgages. They cannot go out and make a loan directly to a limited dividend housing corporation which is to engage in the construction of rental housing.

It is proposed to amend the National Housing Act (through amending the Wagner Housing Act) by permitting mortgage associations to make loans to limited dividend housing corporations. Such mortgage associations could then issue debentures against the insured mortgages which they have in their portfolios. The capital to purchase such debentures is available in all parts of the country. Since the passage of the National Housing Act most of the states have passed laws permitting banks, insurance companies, trustees, and building and loan associations to buy such debentures. Due to the limitations of the existing law, however, no debentures have been issued because of the fact that the mortgage associations have been prohibited from making loans to limited dividend housing corporations.