

November 26, 1937

To: Mr. Eccles
From: J. M. Daiger
Subject: Ninety per cent Mortgages under State Laws

One of the questions that you will probably be asked at the press conference is whether State laws permit State-chartered institutions to make 90 per cent loans under the National Housing Act, or whether further enabling legislation will be required to accomplish this purpose.

The answer to this is that in the main the State enabling legislation looks toward the fact of insurance by the Federal Housing Administration, rather than toward the percentage of the loan. Some of the enabling legislation explicitly provides that the authority to make loans insured by the Federal Housing Administration extends to loans made under future amendments to the National Housing Act as well as under the provisions of the act at the time the enabling legislation was adopted.

Experience has shown that the State legislatures are disposed to act promptly in the passage of such enabling legislation. Where further amendments may be required, therefore, to make the 90 per cent provision effective as to State-chartered institutions, it is reasonable to assume that these amendments will be made without delay soon after the legislatures convene.

If reporters ask for information in regard to particular States, I would suggest that you refer them to the Public Relations Division of the Federal Housing Administration. Mr. Ferguson is having one of his assistants go particularly into the question of what State laws expressly limit lending institutions to 80 per cent in making loans under the National Housing Act.

J. M. Daiger



November 23, 1937 (D)

Summary of Proposed Amendments to National Housing Act
and Federal Housing Administration Regulations

The measures recommended by the informal group recently designated by the President to consider a program to stimulate private housing construction have the following principal objectives:

1. Lowering the costs of financing.
2. Making it easier for families of moderate means to buy or rent new houses.
3. Providing mechanisms that will make it practicable for private enterprise to engage in large-scale housing operations for the mass market.

Enlargement of the framework of the National Housing Act is suggested as the most effective means to encourage and facilitate private construction and private financing. The system of mortgage financing provided for in this legislation is the only one that is applicable to all types of institutions that make loans for housing purposes. It enables these institutions to make high percentage loans at a low rate of interest on 20-year amortized mortgages.

1. Reduction of Financing Costs

At the present time the overall cost of financing under the FHA is $6\frac{1}{4}$ per cent. This includes an interest charge of 5 per cent, a service charge of $\frac{1}{2}$ of 1 per cent, and a mortgage-insurance charge of $\frac{1}{2}$ of 1 per cent on the original face amount of the mortgage, which is equivalent to $\frac{3}{4}$ of 1 per cent in terms of true interest.

It is proposed by an amendment to the administrative regulations to reduce the combined interest and service charge from an authorized maximum of $5\frac{1}{2}$ per cent to 5 per cent. It is proposed by legislative amendment to authorize a reduction in the minimum insurance premium from $\frac{1}{2}$ of 1 per cent on the original face amount of the mortgage to $\frac{1}{2}$ of 1 per cent on the diminishing balance of the mortgage. The effect of these administrative and legislative changes would be to make the overall cost $5\frac{1}{2}$ per cent instead of the present $6\frac{1}{4}$ per cent.

In the case of loans insured prior to July 1, 1939, where the appraised value of the property does not exceed \$6,000, it is proposed by legislative amendment to authorize a minimum insurance charge of $\frac{1}{4}$ of 1 per cent, making the overall cost of financing in such cases $5\frac{1}{4}$ per cent.

2. Reduction of Down-Payment on Small Houses

The insurable limit of mortgages on single-family houses at the present time is 80 per cent of the appraised value, thereby making a down-payment requirement of 20 per cent. It is proposed by legislative amendment to increase the insurable limit to 90 per cent in the case of mortgages where the appraised value of the property does not exceed \$6,000, thereby reducing the down-payment requirement to 10 per cent.

3. Encouragement of Group-Housing and Rental-Housing Construction

It is proposed by legislative amendment to authorize the insurance of mortgages up to \$200,000 on groups of houses built for sale or for rent, or for lease with an option to purchase, and on multi-family structures where the amount of the mortgage does not exceed \$1,000 per room. In the case of groups of houses, the financing would be by means of a blanket mortgage, from which mortgages on individual properties could subsequently be released without impairing the insurance contract.

The insurable limit in the case of group housing and rental housing within this classification up to \$200,000 would be 80 per cent and the minimum insurance premium authorized would be 1/2 of 1 per cent. ~~In practice,~~ The overall interest and service

charge authorized would be 5 per cent, but in practice this would probably be $4\frac{1}{2}$ per cent in the case of substantial loans on apartment buildings where the mortgage servicing cost is lower than in the case of mortgages on single-family houses.

4. Encouragement of Large-Scale Rental Projects

It is proposed by legislative amendment to clarify and simplify the provisions now applicable to limited-dividend housing companies by (a) eliminating the ambiguous phrase "persons of low income," (b) limiting the amount of mortgage insurance to \$1,200 per room, (c) fixing the insurable limit at 80 per cent of the appraised value of the property, (d) providing that mortgages may be insured up to \$5,000,000 instead of \$10,000,000, the latter figure being higher than is needed for practical purposes and being open to some objections, (e) providing that large-scale mortgages may be insured on groups of houses built for sale as well as on rental projects, and (f) authorizing FHA debentures to be issued, in event of default of a large-scale mortgage, upon assignment of the mortgage instead of after the completion of foreclosure proceedings.

5. Encouragement of Large-Scale Private Financing

It is proposed by legislative amendment to authorize the National Mortgage Associations provided for in the National Housing Act to make loans on large-scale projects that are subject to special

regulation and restrictions by the Federal Housing Administrator. It is further proposed by legislative amendment to authorize these associations to issue debentures up to twenty times the amount of their capital and surplus instead of twelve times as now provided.

In order to assure immediate availability of private funds for large-scale financing, it is proposed to authorize by administrative amendment the creation of a national mortgage association with \$50,000,000 of capital supplied by the RFC Mortgage Company. This would make available \$1,000,000,000 of private funds through the sale of National Mortgage Association debentures.

6. Concentration of FHA on New Construction

It is proposed by legislative amendment to have the FHA concentrate its mortgage insurance activities after April 1, 1938 on mortgages on new construction. It is further proposed to have the \$2,000,000,000 of mortgage insurance which the FHA is authorized to issue apply to the amount of insurance outstanding at any time, instead of constituting a flat limitation as at present. It is also proposed by legislative amendment to eliminate the provision by which the contingent governmental guaranty would expire on July 1, 1939.

7. Encouragement of Repair and Modernization Loans

It is proposed by legislative enactment to revive in modified form Title I of the National Housing Act, authorizing

the insurance of repair and modernization loans where the face amount is not less than \$200 and not in excess of \$10,000. It is proposed that the amount of insurance heretofore and hereafter issued under Title I shall not exceed \$100,000,000, which was the sum originally fixed by Congress when the National Housing Act was enacted in 1934.

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Memorandum on 90 Per Cent Loans and State Mortgage Laws

The proposal to make it possible for families of moderate means to buy houses upon a first payment of 10 per cent is potentially one of the most important in the new program. Manifestly, the number of families that can and would pay, say, from \$300 to \$500 to get into a new house is enormously greater than the number that can pay from \$500 to \$1,000 or more.

What is being undertaken here is in line with the experience of Great Britain. There the prevailing first payment in recent years has been 10 per cent and the prevailing mortgage 90 per cent. The result of this, in combination with low interest rates and low construction costs, has been to provide a workable basis for large-scale operations and to put home-ownership within reach of millions of families for whom it would otherwise have been unattainable.

In this country, however, State laws will be a determining factor in the practical working of the 90 per cent mortgage. Where the State laws result in protracted delays and excessive costs in acquiring title to a property in the event of default, lending institutions will naturally be reluctant to make 90 per cent loans, even though they are insured by the Federal Housing Administration.

Mortgage insurance under the National Housing Act covers the principal of the mortgage and interest up to 3 per cent. It does not cover foreclosure costs. For this reason, a lending institution has to take into account the possibility that, if a mortgage does default, ultimate sale of the property may not yield enough to meet the unpaid principal, interest, and taxes, and still leave enough to cover foreclosure costs.

In Illinois, for example, the Home Owners' Loan Corporation has found that the average cost of its foreclosures is approximately \$350, and that the time involved is more than a year and a half. In New York, the cost is more than \$300; in New Jersey, more than \$200. In a number of states, the time involved runs from a year to fifteen months or longer, and in the case of Alabama the time is more than two years.

Contrasted with these high costs and long delays, the cost of an HOLC foreclosure in Massachusetts is about \$30, and the time involved is about two months.

These are conditions that can be remedied only by the action of State legislatures. To meet the situation, the Subcommittee on Laws and Legislation of the Central Housing Committee has drafted a proposed uniform mortgage and foreclosure act. This is designed to give adequate protection to both the mortgagor and the mortgagee, and at the same time eliminate excessive expense and time-consuming procedure.