



December 23, 2009

The Honorable David H. Stevens  
Assistant Secretary for Housing-Federal Housing Commissioner  
U.S. Department of Housing and Urban Development  
Federal Housing Administration  
451 Seventh Street SW  
Washington, DC 20410-0500  
Submitted via [www.regulations.gov](http://www.regulations.gov)

Re: Docket No. FR 5356-P-01: Federal Housing Administration (FHA): Continuation of FHA Reform-Strengthening Risk Management Through Responsible FHA-Approved Lenders

Dear Commissioner Stevens:

The Office of Advocacy of the U.S. Small Business Administration (Advocacy) submits this comment on the Department of Housing and Urban Development, Federal Housing Administration’s (hereinafter, “FHA”) proposed rulemaking on *Continuation of FHA Reform-Strengthening Risk Management Through Responsible FHA-Approved Lenders*. Advocacy is concerned that the FHA has not analyzed properly the full economic impact of the proposal on small entities as required by the Regulatory Flexibility Act (RFA).<sup>1</sup>

### Advocacy Background

Congress established the Office of Advocacy under Pub. L. 94-305 to represent the views of small business before Federal agencies and Congress. Advocacy is an independent office within the Small Business Administration (SBA), so the views expressed by Advocacy do not necessarily reflect the views of the SBA or of the Administration. Section 612 of the RFA requires Advocacy to monitor agency compliance with the Act, as amended by the Small Business Regulatory Enforcement Fairness Act.<sup>2</sup>

<sup>1</sup> 5 U.S.C. §§ 601-612.

<sup>2</sup> Pub. L. No. 96-354, 94 Stat. 1164 (1980) (codified at 5 U.S.C. §§ 601-612) amended by Subtitle II of the Contract with America Advancement Act, Pub. L. No. 104-121, 110 Stat. 857 (1996). 5 U.S.C. § 612(a).

In addition, Executive Order 13272 enhances Advocacy's RFA mandate by directing Federal agencies to implement policies protecting small entities when writing new rules and regulations. Executive Order 13272 also requires Agencies to give every appropriate consideration to any comments provided by Advocacy. Under the Executive Order, the agency must include, in any explanation or discussion accompanying the final rule's publication in the *Federal Register*, the agency's response to any written comments submitted by Advocacy on the proposed rule, unless the agency certifies that the public interest is not served by doing so.

### **Requirements of the RFA**

The RFA requires agencies to consider the economic impact that a proposed rulemaking will have on small entities. Pursuant to the RFA, the federal agency is required to prepare an initial regulatory flexibility analysis (IRFA) to assess the economic impact of a proposed action on small entities. The IRFA must include: (1) a description of the impact of the proposed rule on small entities; (2) the reasons the action is being considered; (3) a succinct statement of the objectives of, and legal basis for the proposal; (4) the estimated number and types of small entities to which the proposed rule will apply; (5) the projected reporting, recordkeeping, and other compliance requirements, including an estimate of the small entities subject to the requirements and the professional skills necessary to comply; (6) all relevant Federal rules which may duplicate, overlap, or conflict with the proposed rule; and (7) all significant alternatives that accomplish the stated objectives of the applicable statutes and minimize any significant economic impact of the proposed rule on small entities.<sup>3</sup> In preparing the IRFA, an agency may provide either a quantifiable or numerical description of the effects of a proposed rule or alternatives to the proposed rule, or more general descriptive statements if quantification is not practicable or reliable.<sup>4</sup> The RFA requires the agency to publish the IRFA or a summary of the IRFA in the Federal Register at the time of the publication of general notice of proposed rulemaking for the rule.<sup>5</sup>

Pursuant to section 605(b), in lieu of an IRFA, the head of the agency may certify that the proposed rule will not have a significant economic impact on a substantial number of small entities. A certification must be supported by a factual basis.

### **The Proposed Rule**

On November 30, 2009, FHA published a proposed rule in the *Federal Register* on *Strengthening Risk Management Through Responsible FHA-Approved Lenders*.<sup>6</sup> The purpose of the proposed rule is to streamline, modernize, and strengthen the mortgage insurance functions and responsibilities of FHA, as authorized by provisions contained in the National Housing Act, as amended by the FHA Modernization Act of 2008, and

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<sup>3</sup> 5 USC § 603.

<sup>4</sup> 5 USC § 607.

<sup>5</sup> 5 USC § 603.

<sup>6</sup> 74 Fed. Reg. 62521.

further supported by the Helping Families Save Their Homes Act of 2009.<sup>7</sup> First, FHA proposes no longer to approve loan correspondents as participants in FHA programs. Mortgagees would be required to ensure that their loan correspondents meet applicable requirements. The FHA-approved mortgagee will, in turn, act as a sponsor as it has in the past. However, in using a sponsor/correspondent relationship, the sponsoring mortgagee must agree to assume responsibility for any loan correspondent that works with the mortgagee in the FHA insured loan, and assume liability for the FHA insured loan underwritten and closed in the name of the FHA-approved mortgagee.<sup>8</sup> Second, the proposal would update the FHA regulations to incorporate criteria specified in the Helping Families Save Their Homes Act of 2009 that precludes certain lending entities from originating an FHA-insured loan.<sup>9</sup> Third, FHA proposes to increase the net worth requirement for FHA approved mortgagees for the purpose of ensuring that approved mortgagees are sufficiently capitalized.<sup>10</sup>

### **FHA's Compliance with the RFA**

FHA prepared a certification for the Regulatory Flexibility Act (RFA) section of the preamble. As noted above, Section 605(b) of the RFA allows an agency to prepare a certification in lieu of a regulatory flexibility analysis if the proposed rule is not expected to have a significant economic impact on a substantial number of small entities. The gist of the certification is that small entities will be able to continue to participate in the FHA loan process as loan correspondents without having to come under the FHA approval process and meet the net worth requirements. As such, the proposed rule will not have a significant economic impact on a substantial number of small entities. After working with industry representatives, Advocacy questions the basis of the certification.

### **The Proposed Rule May Impact A Substantial Number of Small Entities**

The certification states that the small entities affected by the rule are largely loan correspondents who will be able to participate in the origination of FHA-insured loans and not have the administrative burden of obtaining FHA approval.<sup>11</sup> However, it appears as though the proposal may still impact a substantial number of small entities. In its certification, FHA states that there are 13,831 FHA-approved lending entities. Of the approved entities, 28 percent are approved mortgagees, 68 percent are approved correspondents, and the remaining 4 percent constitute government mortgagees or investing mortgagees. Of the FHA-approved mortgagees, only 60 percent have a net worth of \$1 million or more.<sup>12</sup> This means that 40 percent have a net worth of less than \$1 million. Of the approved mortgagees, 20 percent have a net worth less than \$1 million but greater than \$500,000<sup>13</sup> and 20 percent of which have a net worth of \$500,000 or less.

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<sup>7</sup> 74 Fed. Reg. at 62522.

<sup>8</sup> Id.

<sup>9</sup> Id.

<sup>10</sup> Id.

<sup>11</sup> 74 Fed. Reg. at 62528.

<sup>12</sup> Id.

<sup>13</sup> Id.

The proposal increases the net worth requirements for FHA approval from the current amount of \$250,000 to be a mortgagee to \$1 million in the first year. Within three years from the effective date of the final rule, mortgagees would be required to have a net worth of \$2.5 million.<sup>14</sup> This means that the rule will impact at least 40 percent of the approved mortgagees. Although HUD does not state that these approved mortgagees are small, it is fair to assume that at least 40 percent probably are small given their net worth.

### **There May Be a Significant Economic Impact on Small Entities**

In addition, it also appears as though this rule may have a significant economic impact. As noted above, approximately 40 percent of the current FHA mortgagees do not meet the proposed net worth requirements. According to the National Association of Mortgage Brokers (NAMB), the new net worth requirements will eliminate a large number of smaller wholesale lenders who are currently servicing mortgage brokers. Those lenders will lose the current income that they receive by participating in the FHA program. In addition, these mortgage brokers may have a difficult time finding new lenders to obtain the FHA product.

Moreover, because only FHA-approved mortgagees are allowed to request FHA case numbers and other information,<sup>15</sup> according to NAMB the proposal interferes with a correspondent's ability to obtain information for FHA loans or access FHA's website. The restrictions will make it difficult to determine whether customers are eligible for FHA financing. It will also make it difficult for correspondents to assign FHA-approved appraisers to the loans that they are preparing. This lack of access is time consuming and potentially costly if the customer decides to go elsewhere for the loan.

### **Conclusion**

Advocacy encourages FHA to prepare an IRFA to determine the economic impact that this proposal may have on small entities. In doing so, Advocacy encourages FHA to consider less costly alternatives such as a net worth requirement that is not so excessive. Advocacy recognizes that the net worth requirement has not been increased in fifteen years. However, to double, and in some instance quadruple the amount in one year is unduly burdensome on the small participants in the FHA program. A longer time period to obtain the net worth requirement may reduce that burden.

In addition, Advocacy encourages HUD to consider allowing correspondents access to the FHA Connection so that they can obtain case numbers and obtain the information that they need to prepare loans. Correspondents should also have full access to HUD to ensure that correspondents have full access to education and information about the program. Furthermore, considering the number of regulations that have been or are being implemented to regulate the mortgage industry, NAMB strongly encourages HUD to evaluate whether there are conflicting, overlapping, or duplicative rules as required for an IRFA that complies with the RFA.

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<sup>14</sup> 74 Fed. Reg. at 62525.

<sup>15</sup> 74 Fed. Reg. at 62523.

Thank you for the opportunity to comment on this important proposal and for your consideration of Advocacy's comments. Advocacy is available to assist the agencies in their RFA compliance. If you have any questions regarding these comments or if Advocacy can be of any assistance, please do not hesitate to contact Jennifer Smith at (202) 205-6943.

Sincerely,

/s/

Susan M. Walthall  
Acting Chief Counsel

/s/

Jennifer A. Smith  
Assistant Chief Counsel  
For Economic Regulation & Banking

Cc: The Honorable Cass Sunstein