



## **CRS Report for Congress**

# **The Recovery Rebates and Economic Stimulus for the American People Act of 2008 and Jumbo Mortgages**

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### **Summary**

H.R. 5140, the Recovery Rebates and Economic Stimulus for the American People Act of 2008,<sup>1</sup> would temporarily increase the maximum size of loans that Fannie Mae and Freddie Mac can purchase, and that the Federal Housing Administration (FHA) can insure. These new maximums would vary depending on area housing prices, but would be \$729,750 or less.

The likely result of these provisions would be to reduce interest rate and mortgage payments on mortgages above the current \$417,000 limit. For example, the monthly principal and interest payments on a 30-year fixed-rate mortgage for \$600,000 are likely to fall from \$3,824 to \$3,377, saving \$447 per month. Monthly tax and insurance payments would be additional. A mortgage of this size would require an annual income of more than \$140,000. This could stimulate the demand for housing costing \$429,900 to \$768,000.

Fannie Mae and Freddie Mac probably would conduct cost-benefit and risk analyses of making these loans. The Department of Housing and Urban Development (HUD) could insist on reviewing these new products. Regardless of its decision on reviewing the programs, HUD would be required to calculate and publish the new loan limits. A possible result of these procedures would be to slow Fannie Mae's, Freddie Mac's, and FHA's implementation of the programs.

This report will be updated as events warrant.

H.R. 5140, the Recovery Rebates and Economic Stimulus for the American People Act of 2008, would increase the conforming loan limit for mortgages originated between July 1, 2007, and December 31, 2008, to a maximum of \$729,750 in high-cost areas. This

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<sup>1</sup> H.R. 5140 was introduced in the 110<sup>th</sup> Congress by Rep. Nancy Pelosi on January 28, 2008, as a bipartisan bill with 15 cosponsors. It was passed by the House and sent to the Senate on January 29, 2008.

means that the housing government-sponsored enterprises (GSEs), Fannie Mae and Freddie Mac, could purchase qualifying mortgages above the current conforming loan limit of \$417,000 and at or below the new limit. The limit for any area would be the greater of (1) the 2008 conforming loan limit (\$417,000); or (2) 125% of the area median house price, but no more than 175% of the 2008 conforming loan limit (\$729,750, which is 175% of \$417,000).

H.R. 5140 would grant the Federal Housing Administration (FHA) temporary authority to insure mortgages in high-cost areas up to this \$729,750 limit. The authority would expire December 31, 2008. Currently the FHA limit ranges from \$200,160 to \$362,790 in high-cost areas.<sup>2</sup> The Secretary of the Department of Housing and Urban Development (HUD) would be required to publish the increased GSE and FHA limits.

Many of those supporting the increases believe they would provide a needed stimulus to housing and mortgage markets.<sup>3</sup> The immediate impact of the changes affecting Fannie Mae and Freddie Mac, however, is unclear. The Office of Federal Housing Enterprise Oversight (OFHEO), an independent office within HUD, which oversees the safety and soundness of the GSEs, has announced that it is “disappointed” that increasing the limit was not part of general regulatory reform, and that the GSEs should subject the higher priced mortgages to rigorous new product development, risk management, and capital reserves requirements.<sup>4</sup> This suggests that HUD might require the GSEs to submit their plan to purchase the larger mortgages for regulatory review.<sup>5</sup> Unlike the GSEs, FHA (part of HUD) is not under independent regulatory authority.

Given implementation delays and the limited lives of the programs, it is not clear how much use the GSEs or FHA would make of their temporary authority. As stockholder-owned companies, the GSEs would balance their fiduciary responsibility to earn profits with the requirements in their congressional charters to assist housing markets. FHA would probably consider the risk to the financial soundness of their insurance fund against temporary assistance to parts of the housing market.

Other factors tending to limit the impact of the increased mortgage limits are as follows:

- Existing loan-to-value limits would continue to apply. This would prevent homeowners who owe more on a house than its appraised value from participating in the program. For conforming loans using a standard

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<sup>2</sup> FHA limits are available from HUD's website at [<https://entp.hud.gov/idapp/html/hicost1.cfm>].

<sup>3</sup> James R. Haggerty and Damian Paletta, “Details Lacking on Mortgage-Relief Plan,” *Wall Street Journal*, January 26, 2008, p. A6.

<sup>4</sup> James Lockhart, *Statement of OFHEO Director James B. Lockhart on Conforming Loan Limit Increase*, January 24, 2008, available at [[http://www.ofheo.gov/NewsRoom\\_Print.aspx?ID=410](http://www.ofheo.gov/NewsRoom_Print.aspx?ID=410)]. See, also, OFHEO, “Potential Implications of Increasing the Conforming Loan Limit in High-Cost Areas,” *Mortgage Market Note*, January 11, 2008. Available at [<http://www.ofheo.gov/media/research/MMNOTE11108.pdf>].

<sup>5</sup> The Secretary of the Department of Housing and Urban Development has new program approval authority. See 12 U.S.C. 4542.

5% downpayment, this would affect homes worth \$438,900 to \$768,000 and for FHA loans with a 3% downpayment this would allow the purchase of homes worth \$351,900 to \$752,000.

- Existing credit worthiness and debt-to-income requirements would apply. This would prevent those not current on their mortgage from refinancing.
- The GSEs' retained portfolios currently are close to the maximum amount that they can hold without raising additional capital. They could, however, follow the sense of Congress suggestion in H.R. 5140 to buy these mortgages, add their guarantees, package them into mortgage-backed securities (MBS), and sell the MBS to large investors.

The mortgage provisions of H.R. 5140 would

- help purchasers of homes above the current loan limits and below the temporarily higher ones who have good credit;
- mostly help home buyers in high cost areas, such as California, New York City and its suburbs, the Boston area, the Seattle area, and the Washington, D.C. area. The monthly principal and interest payments on a 30-year fixed-rate \$600,000 mortgage are likely to fall from \$3,824 to \$3,377, saving \$447 per month.<sup>6</sup> FHA's guidelines state that mortgage payments, and insurance and taxes should not exceed 29% of monthly income. A combined monthly housing expense of \$3,377 would require a minimum annual income of \$140,000;
- not count mortgages purchased by the GSEs as a result of the higher loan limit for the purpose of low- and moderate-income housing goals and underserved areas goals. HUD establishes numeric goals based on the Housing and Community Development Act of 1992;<sup>7</sup> and
- help FHA compete against private sector lenders and possibly open homeownership to borrowers who for one reason or another could not qualify for a conforming mortgage to purchase a more expensive home.

The approach taken in H.R. 5140 to raising the conforming loan limit differs from that in H.R. 1427, Federal Housing Finance Reform Act of 2007, which passed the House on May 22, 2007, and S. 2036, the Protecting Access to Safe Mortgages Act, which was introduced in the Senate by Senator Charles E. Schumer on September 10, 2007.<sup>8</sup> H.R.

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<sup>6</sup> Interest rates are based on mortgage rates reported by Bankrate.Com at [[http://www.bankrate.com/brm/graphs/graph\\_trend.asp?tf=91&ct=Line&prods=1,325&gs=275,250&st=zz&c3d=False&web=brm&cc=1&prodtype=M&bgcolor=&topgap=&bottomgap=&rightgap=&leftgap=&seriescolor=](http://www.bankrate.com/brm/graphs/graph_trend.asp?tf=91&ct=Line&prods=1,325&gs=275,250&st=zz&c3d=False&web=brm&cc=1&prodtype=M&bgcolor=&topgap=&bottomgap=&rightgap=&leftgap=&seriescolor=)]. The jumbo loan interest rate used in this calculation is 6.58% and the conforming loan interest rate is 5.42%.

<sup>7</sup> 12 U.S.C. 4562-4564 and 4566.

<sup>8</sup> Representative Barney Frank introduced H.R. 1427, the Federal Housing Finance Reform Act (continued...)

1427 and S. 2036 would increase the conforming loan limit for Fannie Mae and Freddie Mac to the area median house price subject to a maximum of 150% of the national limit. In 2008, absent H.R. 5140, the national limit is \$417,000, making the high-cost limit \$625,500. H.R. 5140 has a higher absolute maximum (\$729,750 versus \$625,000 in 2008), is permanent instead of temporary, and would increase the limit in areas where 125% of the median house price exceeds the current national limit of \$417,000. For example, the most recent median existing home price data from the National Association of Realtors (third quarter 2007), in Barnstable, Massachusetts was \$400,600. The conforming loan limit under H.R. 5140 would increase to \$500,750 in Barnstable.

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<sup>8</sup> (...continued)

of 2007, on March 9, 2007. The five cosponsors were from both parties. Senator Schumer introduced S. 2036 without cosponsors; it was referred to the Committee on Banking, Housing, and Urban Affairs.