09/04/2007

Understanding the Government's Role in Your Mortgage

With all the trouble in today’s mortgage market, plenty of lawmakers are eager to get the government involved in correcting the industry ills. Government intervention in the mortgage arena is nothing new, however. Here’s a quick lesson in American mortgage history as well as how government involvement might affect your current mortgage.

The federal government first started to take part in the mortgage world back in 1913, when policy makers enacted a law allowing homeowners to deduct their mortgage interest from their taxes. Since that time, lawmakers have constantly debated what role if an, the government should play in a regulating the mortgage market, a power that has no Constitutional basis, per se. As the ‘American dream’ has come to be defined by homeownership however, the government’s role in perpetuating that dream has grown considerably.

During the Depression, Franklin Roosevelt and his Congress stepped in to alleviate the national foreclosure crisis of the day. As unemployment became widespread, foreclosures skyrocketed to a rate of 50 percent. One of major problems for homeowners of the day was the lack of refinance loans that could have adjusted rates or terms on those borrowers’ home loans. FDR created the Federal Housing Administration to provide government-insured mortgages to middle and low-income buyers. That action drastically changed the face of the mortgage industry as home loans then became low-risk commodities perfect for sale on the secondary market.

One of the most recent government mortgage market laws was a law passed last year that allows new home buyers to deduct the entirety of their private mortgage insurance from their tax returns during 2007.

All such actions have been designed to help more and more Americans become homeowners. During the past five years or so, people realized that dream at a higher rate than ever before in American history. As the housing market boomed, mortgage bonds gained popularity on the secondary market and more funding was available for home loans. With home price appreciation shooting up with seemingly no end in sight, lenders took greater chances on subprime or poor credit borrowers, offering them all sorts of risky nontraditional mortgages.

Now that housing industry has begun to recede and correct itself, foreclosure rates have exploded among those with dicey adjustable rate mortgages. In fear of a larger recession, many congressmen and senators have tried to expand the government’s powers to end the foreclosure crisis. The most recent step was a plan revealed by President Bush, outlining updates to FHA lending policy.

“The government's got a role to play," Bush said during a speech at the White House Friday. "But it is limited. ...
It's not the government's job to bail out speculators or those who made the decision to buy a home they knew they could never afford," he said. "Yet there are many American homeowners who could get through this difficult time with a little flexibility from their lenders or a little help from their government."

Bush has proposed lowering the down payment requirement on FHA mortgages, as well as increasing the house price maximum allowed on such loans. What this means for you if you are a homeowner facing foreclosure, is that it may soon be much easier for you to refinance out of your expensive exotic loan into a safer FHA loan.