Fact Sheet

Federal Home Loan Bank Board

1700 G Street, N.W., Washington, D.C. 20552

Telephone (202) 377-6680

QUESTIONS & ANSWERS ABOUT AMIRS

1. Question: What is AMIRS?

Answer: AMIRS is a research study conducted by the Board concerning alternative mortgage instruments. The study, the Alternative Mortgage Instruments Research Study, was conducted over a one and one half year period and contains analysis papers on numerous aspects of the design and impact of a variety of new mortgage instruments.

2. Question: Does the Bank Board have immediate plans to implement these new types of mortgage instruments through regulation?

Answer: No. The study is being made available to the Congress, consumer groups and the public for the first time today. The Board intends to discuss with members of Congress and consumer groups the results of the study and to consider appropriate implementation in light of these discussions. Any regulatory action would follow these discussions.

3. Question: Can the Board issue regulations in these areas on their own or do they have to go to Congress for permission?

Answer: The Board recognizes the importance of Congressional input in this area. The Board has had a continuous dialogue with Congress concerning alternative mortgage instruments and the study and will continue to seek Congressional input concerning implementation.

4. Question: What consumer safeguards are there?

Answer: We recognize the importance of safeguards for new mortgage instruments and will be discussing appropriate safeguards with Congress. The Board has always felt that various consumer safeguards should be promulgated to insure that borrowers are not exposed to unreasonable financial burdens. We would anticipate that the safeguards would fall into two categories-general safeguards and instrument-specific safeguards. The general safeguards are intended to apply to all types of new mortgage instruments while the instrument-specific safeguards are relevant only for specific selected new mortgage designs.

Two general safeguards explicitly recommended by the AMIRS staff are particularly relevant to insuring that borrowers are made aware that a choice among AMI's exists and that they receive the appropriate information so as to make intelligent decisions. One safeguard is "documented choice" which would require lenders desiring to offer AMI's to have to present the borrower with a statement of the terms of a traditional fixed rate instrument side-by-side with the offered terms of an AMI. "Comparative disclosure" is a second proposed safeguard which supplements "documented choice." This would require the lender to provide a direct comparison of monthly payments between the AMI and the traditional fixed-rate mortgage offered. Other safeguards would, for example, limit the frequency and the amount of mortgage changes permitted both annually and over the life of the mortgage.

5. Question: Will consumers have a choice of mortgage instruments?

Answer: Yes. The Board's thinking thus far is that any Federal S&L desiring to offer a new mortgage instrument will be required to offer the standard fixed payment mortgage as an alternative. Moreover, in implementing new mortgage instrument authority, the Board would want to take steps to insure that borrowers (1) are made aware that a choice exists, (2) received the appropriate information so that the choice is clearly understandable, and (3) have the ability to effectively "shop around" for the type of mortgage with the price and non-price terms they desire.

6. Question: How will reverse annuity mortgages assist older citizens?

Answer: A reverse annuity mortgage is a generic term for a financial instrument or package of financial instruments that enables the owner to liquidate equity in real estate while retaining rights of ownership, use, and possession. RAMs have been proposed primarily as vehicles for elderly citizens to use their accumulated real estate equity as a source of income and security during the remaining years without having to sell and leave their homes. A reverse annuity mortgage basically consists of a loan secured by real estate that is used to purchase rights to income in the form of one or more annuities. As such, reverse annuity mortgages can provide a fundamental financial service of major social significance by introducing a mechanism for the orderly and rational liquidation of wealth during an individual's years of retirement. In principle, reverse annuity mortgages are entirely feasible when properly applied and based on sound financial and insurance principles.

7. Question: Even if all the new mortgage instruments are adopted, will associations be obligated to offer these new instruments?

Answer: This is one of the items we would want to discuss with Congress. We would hope, however, that institutions would not be required or forced to offer these new mortgage instruments if they chose not to do so. However, we believe that the AMIRS study has indicated that there are substantial benefits to both consumers and lenders from introduction of alternative mortgage instruments.

8. Question: Will the advent of the new mortgage instruments eventually phase out the fixed-rate mortgage?

Answer: The fixed-rate traditional mortgage instrument would probably still be the dominant mortgage form even in a world of new mortgage instruments. The fixed-rate standard mortgage instrument has served a large segment of the population well for a long period of time and would still be a very desirable alternative from the perspective of a large segment of the population. The objective of AMIRS was not to find new mortgage instruments that would replace the standard fixed-rate mortgage instrument but rather to expand the number and range of alternatives available to consumers in financing their home purchases.

9. Question: With reverse annuities, what happens when there is not equity left in a house for the association to pay back to the homeowner? Can they still live there or are they forced to move?

Answer: A reverse annuity mortgage is basically a loan secured by real estate that is used to purchase one or more annuity contracts. The borrower retains equity at the margin that encourages maintenance of the property, provides protection to the lender, allows the borrower to enjoy any increase in the property value and permits bequest at death. One misconception about reverse annuity mortgages is that they leave no real estate equity for the owner. This is not valid since most borrowers and lenders will require that the borrower retain ownership, possession, and a significant equity interest at all times.

10. Question: Will any of the new instruments directly affect lending in urban areas?

Answer: The new mortgage instruments are not directly designed to alter the mix of urban/suburban lending patterns. While some of the instruments are designed to increase the homeownership capabilities of some segments of the population, it is not necessarily the case that these individuals will be located in or necessarily use their mortgage credit for purchase of homes in urban areas as opposed to suburban areas.

11. Question: Will the Federal Home Loan Mortgage Corporation be able and is it planning to purchase these new types of mortgage instruments?

Answer: The AMIRS analysis of the secondary market implications of AMIs indicates that there are no real barriers to trading AMIs in the secondary market and that there is no real reason to doubt that a viable secondary market can exist for the new mortgage instruments. However, there is no sure way to assess the secondary market potential of any mortgage instrument until a primary market history is established.

12. Question: How will the various disclosure requirements under the Truth in Lending Act and the Real Estate Settlement Procedures Act (RESPA) affect the AMIs?

Answer: There will have to be adjustments in the regulations implementing these statutes to accommodate new mortgage design disclosures.

13. Question: Do AMIs present any potential legal problems?

Answer: Yes. There is an extensive study of legal problems in the AMIRS report. We have found that State law restrictions are such that at present no AMI studied can be used on a widespread basis. At the Federal level, it may be necessary to modify various requirements.

14. Question: When will the Bank Board authorize the new mortgage instruments?

Answer: The next phase of the process is discussion with Congress and interested groups. The Board does not contemplate any specific action before receiving their input.

15. Question: What will AMIs do to make housing more affordable, especially to lower and moderate income families?

Answer: In terms of borrowers' current income levels, GPMs have the potential of increasing homeownership by up to 5 percent. At 1976 levels, this represents almost 2.5 million households. GPM's could enable up to 11 percent of current renters under age 35 to own their own homes. In this respect, the experience with GPM borrowers under the HUD-FHA experimental program are interesting. Approximately 75 percent of the GPM borrowers were first-time homebuyers and they were younger and had lower incomes than the typical FHA-203 mortgagor.

Definitions of Alternative Mortgage Instruments

The following are brief definitions of some alternative mortgage instruments (AMIs) compared to the standard fixed payment mortgage (SFPM) most prevalent today. It should be noted that there are a great many variants and hybrids of each AMI design.

Graduated Payment Mortgage (GPM). A graduated payment mortgage has scheduled monthly payments that start out at a low level, as compared to those of an SFPM, but rise later. The graduation rate, the term of graduation, and the interest rate are fixed throughout the life of the loan.

Deferred Interest Mortgage (DIM). The DIM is a type of GPM, with low initial payments for a period of years as if based on a lower interest rate than on an SFPM. Negative amortization accrues and is paid off with higher payments later.

Variable Rate Mortgage (VRM). The interest rate on a VRM is tied to some reference index that reflects changes in market rates of interest. Thus, future monthly payments are not known at the time the loan is originated. Constraints on the VRM rate and other safeguards can limit the amount of uncertainty involved.

Rollover Mortgage (ROM). The ROM (currently used extensively in Canada) is a renegotiated loan for which the interest rate and monthly payments are renegotiated (typically) every five years. This rate usually adjusts according to current market conditions.

Price Level Adjusted Mortgage (PLAM). The interest rate is fixed, but the outstanding balance and monthly payments change according to the changes in some price index.

Reverse Annuity Mortgage (RAM). The RAM provides a stream of monthly payments to homeowners through an annuity purchased by a loan against their accumulated equity in the house.