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Highlights

Highlights of GAO-07-1033T, a testimony before the Subcommittee on Housing and Community Opportunity, Committee on Financial Services, House of Representatives

Why GAO Did This Study

The Federal Housing Administration (FHA) differs from other key mortgage industry participants in that it allows borrowers to obtain down-payment assistance from nonprofit organizations (nonprofits) that operate programs supported partly by property sellers. Research has raised concerns about how this type of assistance affects home purchase transactions. To assist Congress in considering issues related to down-payment assistance, this testimony provides information from GAO's November 2005 report, *Mortgage Financing: Additional Action Needed to Manage Risks of FHA-Insured Loans with Down Payment Assistance* (GAO-06-24). Specifically, this testimony discusses (1) trends in the use of down-payment assistance with FHA-insured loans, (2) the impact that the presence of such assistance has on purchase transactions and house prices, and (3) the influence of such assistance on loan performance.

What GAO Recommends

In the report discussed in this testimony, GAO made recommendations designed to better manage the risks of loans with down-payment assistance generally and from seller-funded nonprofits in particular. Consistent with our recommendations, HUD recently issued a proposed rule that would prohibit the use of seller-funded down-payment assistance with FHA-insured loans.

www.gao.gov/cgi-bin/getrpt?GAO-07-1033T.

To view the full product, including the scope and methodology, click on the link above. For more information, contact William B. Shear at (202) 512-8678 or shearw@gao.gov.

June 22, 2007

MORTGAGE FINANCING

Seller-Funded Down-Payment Assistance Changes the Structure of the Purchase Transaction and Negatively Affects Loan Performance

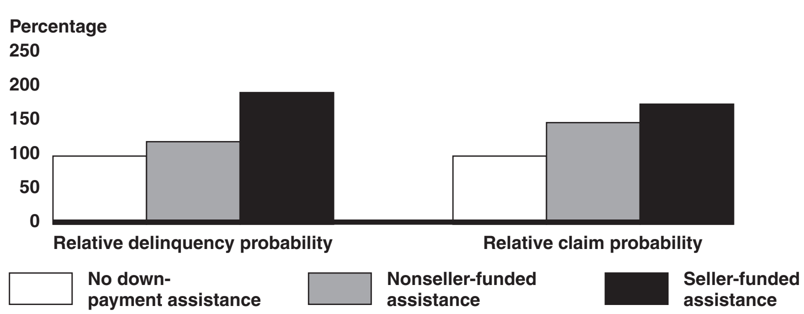
What GAO Found

The proportion of FHA-insured purchase loans that were financed in part by down-payment assistance increased from 35 percent to nearly 50 percent from 2000 through 2004. Assistance from nonprofit organizations that received at least part of their funding from property sellers accounted for much of this increase, growing from about 6 percent of FHA-insured purchase loans in 2000 to approximately 30 percent in 2004. More recent data indicate that in 2005 and 2006, the percentages of FHA-insured loans with down-payment assistance from all sources and from seller-funded nonprofits were roughly equivalent to 2004 levels.

Assistance from seller-funded nonprofits alters the structure of the purchase transaction in important ways. First, because many seller-funded nonprofits require property sellers to make a payment to their organization, assistance from these nonprofits creates an indirect funding stream from property sellers to homebuyers. Second, GAO analysis indicated that FHA-insured homes bought with seller-funded nonprofit assistance were appraised at and sold for about 2 to 3 percent more than comparable homes bought without such assistance.

Regardless of the source of assistance and holding other variables constant, GAO analysis indicated that FHA-insured loans with down-payment assistance have higher delinquency and insurance claim rates than do similar loans without such assistance. Furthermore, loans with assistance from seller-funded nonprofits do not perform as well as loans with assistance from other sources (see fig.). This difference may be explained, in part, by the higher sales prices of comparable homes bought with seller-funded assistance and the homebuyers having less equity in the transaction.

Effect of Down-Payment Assistance on the Probability of Delinquency and Claim



Source: GAO.

Note: Loans without assistance are set at 100 percent. Data are from a national sample of FHA-insured loans from 2000, 2001, and 2002; and the analysis controlled for selected variables.