September 2016

HOME MORTGAGE GUARANTEES

Issues to Consider in Evaluating Opportunities to Consolidate Two Overlapping Single-Family Programs

GAO Highlights

Highlights of GAO-16-801, a report to the Chairman, Subcommittee on Housing and Insurance, Committee on Financial Services, House of Representatives

Why GAO Did This Study

RHS and FHA help borrowers finance homes by guaranteeing single-family mortgage loans made by private lenders, and both operate in rural areas. However, eligibility for RHS guarantees is restricted to RHS-eligible areas and to low- and moderate-income households. A prior GAO report (GAO-12-554) found overlap in the products offered, borrower income levels, and geographic areas served by the two guarantee programs and recommended that RHS and FHA evaluate and report on opportunities for consolidating similar housing programs.

GAO was asked to expand on the analysis in its 2012 report. This report compares the characteristics, performance, and borrower costs of RHS- and FHA-guaranteed loans in RHS-eligible areas.

GAO analyzed RHS and FHA data for home purchase loans guaranteed in fiscal years 2010–2014 (which allowed for analysis of loan performance over multiple years). GAO also interviewed RHS and FHA officials, eight lenders (selected to capture variation in rural areas served, origination volume, and mix of RHS and FHA business), and industry associations.

What GAO Recommends

GAO makes no new recommendations in this report but maintains that RHS and FHA should evaluate and report on opportunities to consolidate their similar housing programs.

View GAO-16-801. For more information, contact Daniel Garcia-Diaz at (202) 512-8678 or garciadiazd@gao.gov.

What GAO Found

GAO's comparison of single-family home purchase loans guaranteed by the Rural Housing Service (RHS) and the Federal Housing Administration (FHA) in fiscal years 2010–2014 identified significant overlap and some differences in the borrowers served. Within statutorily defined rural areas (RHS-eligible areas):

- Both agencies served large numbers of rural borrowers, but FHA served over 35 percent more than RHS, while RHS reached a greater number of borrowers in the more rural parts of RHS-eligible areas.
- Most of the borrowers served by each agency had annual incomes below $60,000. But consistent with RHS's statutory income limits, the median borrower income for RHS ($44,000) was well below that for FHA ($57,000).
- RHS and FHA borrowers had similar credit scores (around 685 at the median) and ratios of housing expenses to monthly gross income (23–24 percent at the median).
- Borrowers in both programs had high loan-to-value (LTV) ratios (loan amount divided by home value). But RHS's no-down-payment requirement and FHA's statutorily required 3.5 percent down payment resulted in higher LTV ratios for RHS than for FHA (medians of 101 and 96.5 percent, respectively).
- Significant portions of RHS and FHA borrowers could have met the criteria of the other program. For example, at least 36 percent of RHS borrowers could have met FHA's criteria, including the 3.5 percent minimum down payment.

In RHS-eligible areas, RHS loans guaranteed in fiscal years 2010–2011 performed worse than corresponding FHA loans after 3 years. Specifically, for borrowers whose incomes fell within RHS limits, RHS's 3-year troubled loan rate (the share of loans 90 or more days late, in foreclosure, or terminated with a claim) was 7 percent, compared with 6 percent for FHA. GAO estimated that RHS's loans would be expected to perform worse than FHA's due partly to RHS borrowers' higher LTV ratios.

Borrower costs—at loan closing and paid monthly—were lower for RHS loans than for FHA loans. Due to differences in down-payment requirements, a borrower purchasing a $125,000 home in 2014 would have paid $4,375 more in up-front costs with an FHA loan than with an RHS loan. Also, FHA (which must maintain a capital reserve) charged borrowers a higher annual guarantee fee than RHS, which has no capital requirement. Due largely to the difference in this fee (charged monthly), a borrower's initial monthly payments would have been about 7 percent lower with an RHS loan (assuming a 3.75 percent interest rate).

GAO's analysis provides additional evidence of how the programs overlap in terms of income, location, and borrower qualifications. It also highlights issues for RHS and FHA to consider in evaluating opportunities to consolidate these programs, as GAO recommended in 2012. Specifically, differences in the performance and borrower costs of RHS and FHA loans underscore important tradeoffs. Higher LTV ratios and lower guarantee fees help make mortgages more affordable. However, these features also may elevate financial risks to the federal government from increased loan defaults and less revenue to cover unanticipated costs. Agency consideration of these issues would aid congressional decision-making about potential program consolidation.